CYBG

A DIFFERENT WAY OF BANKING

ANNUAL REPORT AND ACCOUNTS 2017

Who we are

CYBG PLC is a full-service bank focused on UK consumers and small and medium-sized enterprises (SMEs), operating under the Clydesdale Bank, Yorkshire Bank and B brands.

We serve nearly three million customers through an omni-channel model of online, mobile and telephone banking, together with a network of 169 branches and 40 business banking centres, located mostly in the UK's economic heartlands of Scotland, the north of England and the Midlands.

What's inside this report

Certain figures contained in this document, including financial information, may have been subject to rounding adjustments and foreign exchange conversions. Accordingly, in certain instances, the sum or percentage change of the numbers contained in this document may not conform exactly to the total figure given.

The forward-looking statements disclaimer can be found on page 263.

Group at a glance

Our significant scale

2.7m customers
£32bn loans
£28bn deposits
169 retail branches

Our business is delivered through our key brands ...

CYBG operates through the retail and commercial banks Clydesdale Bank, established in 1838 in Glasgow, Yorkshire Bank, founded in 1859 in Halifax, and through the digital banking service B, created in 2016.

Clydesdale Bank

Yorkshire Bank

... underpinned by our three strategic priorities ...

Drive sustainable customer growth
by investing to broaden the franchise across our target segments and core regions while enhancing the customer experience.

Improve efficiency
by making our network, operations and organisation more efficient and agile for staff and customers.

Capital optimisation
by securing Internal ratings-based (IRB) accreditation and deploying our capital to support our business ambitions while balancing risk and reward.

... and distributed through our omni-channel model

Our omni-channel model is focused on delivering an improved service across every channel where we serve and support our customers.

Our strong and growing digital offering, combined with the branch network, contact centre and extensive broker channel, provides an enviable position from which to grow our business.

To achieve our objectives, we are streamlining our front and back office, investing in our digital platform to accelerate the adoption of mobile and online tools and increasing in-branch automation.

2017 highlights

Delivering sustainable customer growth	**+7.5%** mortgage lending annual growth **+5.9%** SME core lending annual growth
Stable net interest margin (NIM)	**2.27%**
Improving efficiency	**7.4%** reduction in underlying costs **Positive** jaws
First statutory profit in over 5 years	**£182m** statutory profit
Strongly capitalised	**12.4%** Common Equity Tier 1 (CET1) ratio
Improving returns	**7.5%** underlying Return on Tangible Equity (RoTE)
Inaugural dividend recommended by the Board	**1.0** pence per share

Note: the key performance indicators (KPIs) used by management in monitoring the Group's performance and reflected throughout this section are determined on a combination of bases (including statutory, regulatory and alternative performance measures), as detailed in the Glossary on page 253.


a pioneer

Chairman's statement

❝ I am pleased to report on another year of strong progress for CYBG as we continue to execute our strategy to create the only credible alternative to the big UK banks. **❞**

2017 was another year of strong progress for CYBG, with good momentum in the execution of the three pillars of our strategic plan – sustainable customer growth, efficiency and capital optimisation – and with it the successful delivery of our financial targets for 2017. The hard work of the Board, the Executive Leadership Team and all of our colleagues means I am pleased to be able to reiterate our medium-term guidance with renewed confidence.

The Group's successful delivery this year means that I am pleased to announce that the Board is recommending the payment of our inaugural dividend of 1.0 pence per share. Since the Initial Public Offering (IPO) we have talked about being a dividend paying stock and this proposed dividend represents a landmark event in the process of transforming CYBG into a bank that generates and distributes a sustainable return on its equity to shareholders. The continued delivery of our strategy should help us to build on this firm foundation as we move forward.

As well as their commitment to our customers, I am very proud of the way my colleagues support the communities in which we operate. Almost 7,000 volunteering hours were undertaken during 2017 and, with matching through our charity foundation, we have raised over £5.8m for our charity partner Hospice UK among a number of other initiatives.

Economic conditions in the UK remain muted but, for the moment at least, stable. Despite the uncertainty surrounding Brexit negotiations and increased inflation causing real wage deflation, we have not seen a deterioration in the quality of our assets and we remain focused on delivering sustainable growth within our prudent risk appetite.

I would like to thank all of our colleagues, the Executive Leadership Team and the Board for their continued dedication and commitment to the transformation of CYBG. I would also like to personally thank Richard Gregory who left the Board in January for his contribution over many years.

Our performance in 2017 represents a significant achievement. It is only the first step in delivering our three-year plan. We therefore remain focused on executing the strategy we outlined at our Capital Markets Day in September 2016, in order to deliver an exceptional customer experience for our personal and SME customers and sustainable returns to our shareholders.

Jim Pettigrew
Chairman

20 November 2017

Our strategy

“We are committed to delivering a strong, customer-centric banking proposition in the UK.”

This means continuing to focus on transforming our culture and being recognised as a leading consumer brand and a great place to work.

Our strategy is simple, is working and remains unchanged – our strategic priorities of sustainable customer growth, efficiency and capital optimisation are being delivered through a strong customer-focused culture, a robust change management and investment approach and parallel development of our omni-channel capabilities, and all of these within a framework of prudent risk management and governance. Our primary focus is on building a better organisation for our customers and staff and our organic plan is predicated on continuing to improve the areas of our performance that we can control, such as costs, efficiency and customer experience improvements.

We will continue to evaluate potential inorganic opportunities to enhance our business provided they are in line with our strategic objectives and create value for our shareholders. We have established a set of capabilities that gives us significant confidence in our ability to execute, should such inorganic opportunities arise.

Our strategic priorities

Underpinned by omni-channel delivery

Drive sustainable customer growth

- A 'deposit first' philosophy – secure primary account relationship
- Acquire customers in key target segments (younger, more affluent)
- Leverage our third party mortgage broker relationships
- Agile approach to product development
- Enhance our SME offering to meet the needs of an under-served marketplace
- Simplify operational processes
- Focus on end-to-end product profitability
- Further integration of product and service across channels

Improve efficiency

- Improve our cost structure by delivering:
  - Network efficiency through our customer banking transformation
  - Operational efficiency through improved customer service
  - A streamlined lower cost management model
  - More for less through improved central cost management
- Clear internal accountability for delivery
- Providing capacity to reinvest in our digital and growth agenda

Capital optimisation

- Secure IRB accreditation for:
  - Mortgage book during 2018
  - Remainder of bank in 2019
- Improve capital deployment decisioning and reduce exposure to lower yielding mortgages and SME lending

Chief Executive Officer's review

"Whether it is prototyping new technologies, opening our first consumer innovation lab, Studio B, or collaborating with Fintech partners with the development of our new small business e-lending solution, we are building a bank focused on a differentiated customer experience that will put customers more in control of their money."

I am delighted to report that we have maintained momentum in delivering our strategic priorities and commitments and, as a result, we are delivering significantly improved financial performance, have recorded our first statutory profit in over five years and are recommending an inaugural dividend to shareholders.

As the only truly full-service challenger bank of scale across both Retail and SME in the UK market, we have delivered ahead of market growth in both mortgages and SME lending and we remain on track to deliver our commitment to provide up to £6bn of lending to SMEs by the end of 2019.

Our results show improved underlying profit, sustainable loan growth, a stable margin and improved returns – all achieved in a highly competitive market and a continuing low growth, low interest rate environment. Our cost efficiency programme is also ahead of plan, with underlying operating costs coming in at £675m, down 7% year on year. We have also continued to work through our legacy conduct issues and our statutory profit includes the impact of a conduct charge of £58m primarily due to historical payment protection insurance (PPI) mis-selling.

CYBG is perfectly placed to disrupt the market – we have the size and full-service Retail and SME capabilities that no other UK challenger bank can offer, yet we are smaller and more agile than the complex structures of the 'big five' UK banks. We are well capitalised, have a high-quality loan book and prudent risk appetite, along with powerful, established local brands. These have now been joined by an innovative brand in B, which has broadened our customer demographic and reach outside of our core regions. We have over 100,000 B customers since launch in 2016 and we were proud to receive the FStech Award 2017 for Digital Launch of the Year.

The pace and scale of transformation across our business has been considerable in 2017. We have kept up our relentless focus on enhancing our customers' experience through operational improvements and have maintained excellent progress on the delivery of our plan to provide a truly omni-channel model for customers. As part of our digital journey, over the past year we have introduced straight-through online account opening, Apple and Android Pay, as well as piloting an innovative new online SME lending facility through one of our Fintech partnerships. In addition, our migration of our Clydesdale and Yorkshire Bank accounts to our digital platform, iB, is well advanced and we expect all personal customers to begin migrating to iB on the web by the end of 2017 with SME customers to begin migration onto iB, both mobile and web, in 2018.

Like other banks and high street retailers we are seeing a shift in the way customers choose to do business with us and more often customers are using telephone, internet and mobile channels to do day-to-day banking. As a result, the number of transactions which take place in branches is falling, with customers increasingly using a branch only when they want to speak with us about a significant life event. We are constantly reviewing our branch footprint and while a number of branches were closed this year, we opened new flagship branches in Edinburgh and Birmingham as part of a broader multiyear strategy to expand our presence in key northern cities.

In April, we opened our innovation lab, Studio B, in London. Unlike anything else on the high street, Studio B enables us to collaborate directly with customers and other interested parties on the design of future banking products and services, then showcase and test our best ideas with colleagues, customers and members of the public – all within a fully functioning customer banking centre. While in September we expanded our UK presence into Birmingham with the opening of a next generation B store which, as well as being a fully operational branch, is also a showcase for customers to experience our digital innovations.

Over the next 12 months I am confident we have both the opportunity and the ability to create a differentiated customer experience that positions us as a progressive, forward-looking organisation able to thrive today, tomorrow and in the future, delivering on commitments to our customers, our people and our shareholders. Finally, I am very grateful to the Chairman, the Board and our colleagues for their backing and insight as we continue on our journey.

David Duffy
Chief Executive Officer

Highlights of the year

JANUARY

October | November | December | January | February | March

OUR FIRST AGM AS A LISTED BUSINESS

Our Board and members of our Executive Leadership Team travelled to Australia in January for our first AGM as a listed business. We fully recognise that a significant proportion of our shareholders are not based in the UK and we believe it's important that we are able to speak to people face to face about CYBG and our strategy for growing the business.

The decision to host the AGM in Melbourne was warmly received and well attended – we welcomed more than 250 people to the event and an even wider audience joined via a live webcast.

The overall tone of the event was positive, reflecting on the solid progress we have made in our landmark first year.

How we create value

Our core business strengths…

– Simple, low-risk banking model
– Scale and scope of larger players, with the agility of a smaller bank
– Long-established franchise in core regional and selected national markets
– Resilient and strongly capitalised balance sheet with a diverse range of funding sources available
– Cutting-edge, scalable and full-service digital operating platform positioned for the future
– Experienced Executive Leadership Team and dedicated colleagues

… means we can offer our broad customer base…

– 2.7m retail and business customers
– Strong market shares in our core regions of Scotland and the North of England
– Perfectly positioned to support and benefit from the UK Government's 'Northern Powerhouse' initiative
– Customer proposition increasingly attracting new customers from our underrepresented demographic segments (young and affluent)

… a full-service retail and SME banking proposition…

– We offer a range of simple banking products supported by great customer service

Retail
– Personal current accounts
– Savings accounts and term deposits
– Mortgages
– Personal loans
– Credit cards
– Overdrafts

SME
– Business current accounts
– Savings and deposits
– Term lending
– Overdrafts
– Working capital solutions
– Payment and transaction services

… through our three brands…

Clydesdale Bank
cbonline.co.uk

B
youandb.co.uk

Yorkshire Bank
ybonline.co.uk

… in whichever way our customers choose to interact with us…

Omni-channel delivery…

- Mobile
- Internet banking
- Telephony
- Branches and business centres
- Intermediary

… benefits the customer with

- Improved experience
- Deeper relationships
- Broadened offering
- Extended reach
- Increased ease and convenience

… enabled and driven by our digital capability

Digital is at the heart of everything we do

– Our commitment to digital is preparing us for a radically different banking environment in the future

– We are investing c.£350m to drive a transformation in our customers' experience and at the heart of this investment is our iB digital platform

– Our methods of working are evolving to become more flexible and allow us to bring our products to market more quickly, leveraging existing channels

– Our products are increasingly designed to be sold across all of our distribution channels

– We created B, our digital-only brand, in 2016 and already have over 100,000 customers

Strategy in action

Our strategic priorities	Our progress during FY2017	Change since FY2016
Drive sustainable customer growth by investing to broaden the franchise across our target segments and regions while enhancing customer experience	– Current account growth of 5.3% driven by continued success of B and higher business current account balances – Enhancements to our mortgage application process contributed to mortgage growth significantly ahead of market – Reinvigoration of our SME franchise drove SME loan drawdowns up 13% – Number of digital users up 10% annually – over 40% of B app users from younger, more affluent target markets – Continuous enhancement to digital functionality: straight through online account opening, Android Pay for B, B on Web, paperless statements, and Touch ID log in – Flagship locations opened as part of an ongoing improvement in our physical network	**+7.5%** Mortgage lending growth **+5.9%** SME core lending growth
Improve efficiency by making our network, operations and organisation more efficient and agile	– Efficiency programme ahead of schedule – Improvements to business banking experience, including 80% reduction in time taken to open a business account – 40% increase in SME credit application decisions reached in same day – We have reduced the time taken from mortgage application to offer by c.50% for all applicants – Enterprise-wide actions to reduce third-party costs have already achieved run-rate savings of £27m – Transitional Service Agreement (TSA) programme milestones successfully delivered with 22 out of 29 TSAs now complete – Core full time equivalent (FTE) reduction of 9% in FY2017 – Reconfiguration of network, with 79 branches closed – Designed, developed and deployed world-leading robotic solutions across the PPI operation – Cumulative run rate savings of £90m since efficiency programme began – On track to deliver FY2019 efficiency targets	**-7.4%** Underlying costs year on year
Capital optimisation by securing IRB accreditation and exploring opportunities across the asset portfolio	– Significant improvement in underlying RoTE to 7.5% – Defined benefit pension scheme (the Scheme) closed to future accrual – The triennial valuation of the Scheme has also been agreed, resulting in a reduced deficit of £290m and no requirement for the Group to increase contributions to the Scheme – On track to deliver double-digit RoTE by FY2019 – Recommending inaugural dividend to shareholders – IRB waiver application submitted to the Prudential Regulation Authority (PRA) and overall programme on track – IRB modelling development and data assessment improvements ongoing	**+2.3%** pts RoTE year on year

Our KPIs for FY2017

+6.0%
Loan growth

2.27%
NIM

115%
Loan to deposit ratio (LDR)

Outlook

- Mid-single digit % customer loan growth in FY2018
- LDR below 120% in FY2018
- NIM of c.220bps in FY2018

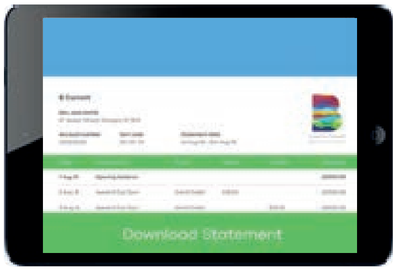
Our strategy in action

The B brand was extended in April with the addition of a B credit card.

£675m
Underlying costs

67%
Underlying cost to income ratio (CIR)

- Underlying cost guidance of below £650m in FY2018



Digital statements were introduced in March to help customers manage their money more conveniently.

12.4%
CET1 ratio

7.5%
Underlying RoTE

- Expecting IRB accreditation for mortgages during 2018 and the remainder of the bank during 2019
- CET1 ratio of 12-13%

Both Clydesdale and Yorkshire Banks launched a mortgage challenge in January offering customers the chance to review their current mortgage in 5 minutes.

Measuring our performance

"After a strong performance during FY2017, I am pleased to reiterate our commitment to our medium-term financial guidance."

In September 2016, CYBG announced a number of medium-term financial targets which represented an acceleration of the strategic plan articulated at the time of the Group's demerger and IPO. Following our strong performance in FY2017, the Board has reiterated its commitment to the Group's strategy and the medium-term targets.

We outline our medium-term targets and progress towards them opposite.

Efficiency

Sustainable customer growth

LDR

Capital

RoTE

Dividend

Medium-term financial guidance

55-58%

CIR by FY2019

- We have made good progress in improving the Group's efficiency to date and are currently ahead of schedule in delivery of our FY2019 net cost savings target
- The next phase of our cost reduction programme will be focused more heavily on procurement and operational efficiency enhancements
- The Board remains confident in management's ability to deliver a CIR of 55-58% by FY2019

Mid-single digit loan growth

% CAGR to FY2019

- Loan growth of 6% was delivered in FY2017 and we expect to continue a mid-single digit growth trajectory through to 2019
- Operational and customer experience improvements will underpin our ability to continue to capture market share in both Retail and SME markets
- Despite macroeconomic uncertainty in the UK, the Board remains confident that CYBG can grow its loan book sustainably and within risk appetite in the current environment

<120%

LDR

- CYBG's LDR of 115% remains comfortably below our internal target of 120%
- The Board still considers 120% LDR to be an appropriate limit in light of CYBG's continued use of the Term Funding Scheme (TFS) to support its growth ambitions

12-13%

CET1 ratio

- The Group's CET1 ratio of 12.4% remains comfortably within our operating range of 12-13%
- The Board considers a 12-13% operating range to be an appropriate range for CYBG prior to IRB accreditation
- CYBG's capital generation (pre-exceptional charges) was positive in FY2017 and demonstrates the capital generation potential of the business as exceptional charges decline in the future

Double-digit

RoTE by FY2019

- FY2017 saw a significant increase in underlying RoTE to 7.5% driven by increased revenue and cost reduction
- The Board remains confident that CYBG will be able to generate a RoTE of at least 10% by FY2019
- Achieving our medium-term guidance would be a significant achievement given that a double-digit RoTE would represent a doubling of returns in the space of three years

Clear dividend ambition

Recommendation of an inaugural dividend and targeting a 50% payout of earnings over time

- The Board has recommended an inaugural dividend of 1.0 pence per share in respect of FY2017
- The Board will consider the payment of progressive, sustainable dividends having regard to the growth opportunities available, the ongoing investment in our business and any anticipated changes in capital requirements
- The Board continues to target a 50% payout of earnings over time (after payment of Additional Tier 1 (AT1) distributions)

Environment and market outlook

“The UK economy has remained resilient over the past year, despite the uncertain political environment, although recent economic data releases suggest that the UK consumer is starting to feel spending pressures heading into 2018.”

UK GDP has continued to grow but the rate of growth has started to slow. The preliminary estimate of GDP growth of 0.4% in the July to September quarter was up slightly from second quarter growth of 0.3%, but year-on-year growth reduced to 1.5%, down from 1.7% the previous quarter. In response to this slowing growth, the Bank of England (BoE) has reduced its economic growth forecasts for both 2017 and 2018, to 1.7% and 1.6% respectively.

Other key UK macroeconomic indicators continued to improve in 2017, with unemployment falling to 4.3%, which is the joint lowest level since 1975, and the employment rate remaining high at 75.0%.

Inflation, as measured by the Consumer Price Index (CPI), has picked up considerably during 2017 and rose to 3.0% in the year to September. This remains relatively high in comparison to recent years and is above the BoE's target of 2.0%. As inflation outpaced wage growth, real earnings fell by 0.4% in the 3 months to September from the same period in 2016, meaning households will start to feel a squeeze on disposable incomes.

In response to this, the BoE increased the base rate by 25 basis points to 0.50% at the Monetary Policy Committee meeting on 2 November 2017 and guided that any future increases would be expected to be at a gradual pace and to a limited extent. Further base rate increases are expected to be positive for the earnings of UK banks, particularly those banks with a high proportion of current account funding, including CYBG.

The rate of UK mortgage growth slowed in 2017 with balances up 2.9% in the year to September versus a 3.1% increase in 2016. This was predominantly due to lower buy-to-let (BTL) mortgage lending, following stamp duty and tax changes and lower owner occupied growth, which has been attributed to uncertainty caused by Brexit. Mortgage approvals were up 2.4% in comparison to the previous year and housing transactions were down 3.7%. The outlook for the mortgage market remains muted but broadly solid with pressures from any potential base rate rises, UK economic uncertainty and a squeeze on disposable income, partially offset by continued government support.

Growth in UK average house prices overall continued in 2017, up 5% in the year to September. This continues the strong growth seen since the end of 2013 as a result of resilient economic conditions, together with sustained low mortgage rates and government support. However, there is evidence of an emerging divergence now appearing between London and the rest of the country, with London prices growing at a slower rate than the rest of the UK.

The outlook for SMEs remains more cautious, particularly with regards to Brexit, although the CYBG SME Health Check Index showed that the operating environment for Britain's small and medium sized businesses improved in the second quarter of 2017 with a number of improvements including increased lending to SMEs and a falling number of business bankruptcies. The index rose from 46.9 to 58.9 in Q2 2017, which is the highest reading since 2015, although confidence dipped in the quarter. Confidence will be a key driver of the SME market over the coming period as investment decisions are deferred.

Pricing in the customer deposit market is now beginning to intensify. In addition to some larger banks aiming to fund their mortgage growth ambitions there is also competition from some of the smaller institutions who have funded recent growth from the TFS and this will need to be replaced with customer funding over time.

Overall, the economic environment for CYBG remains broadly supportive of our growth ambitions but uncertainty over future conditions remains.

Regulatory and political environment

The Group continues to operate in a demanding regulatory and political climate. Following the result of the EU referendum in 2016, in March this year the Government formally triggered Article 50, giving notice of the UK's intention to leave the EU. While formal negotiations are underway between the EU and UK regarding the terms of the UK's exit from the EU, the terms of 'Brexit' are still unknown. In June's general election the Government lost its majority in Parliament, which has added to this uncertainty.

The regulatory environment in which the Group operates continues to develop and the Group is responding to the following key changes:

- General Data Protection Regulation comes into effect on 25 May 2018. Key changes include a requirement to notify regulators of breaches within 72 hours, responding to subject access requests within 30 days and the imposition of financial sanctions of up to 4% of annual global turnover for serious breaches. The Group has a programme of activity underway to meet the requirements;
- Payment Services Directive 2 (PSD2) comes into force on 13 January 2018. The Group is progressing the necessary developments which include changes to information and transparency requirements on payments, new security requirements including 'strong customer authentication' (the date for this is still unknown) and faster handling of payment-related complaints. In the innovation and competition space two new types of service are brought within the regulation – third-party payment instructions from accounts and account aggregation. The Group is continuing to develop its long-term strategy in this respect;
- the Financial Conduct Authority (FCA) has implemented a time bar on PPI complaints of August 2019 with a two year consumer communications campaign already launched;
- over 2018, the Group will be taking steps to ensure compliance with ring-fencing legislation that takes effect from 1 January 2019. The Group will achieve compliance with the legislation with no material changes to its business operations or corporate structure and so there will be very little impact on the Group's customers;
- the Competition and Markets Authority (CMA) retail banking investigation identified a number of adverse effects on competition in the personal and business current account and SME banking markets. Consequently the CMA introduced a package of remedies designed to address these, some of which are now in force. The remainder will come into effect by summer 2018 with the Group on track to meet these remedies;
- the FCA and PRA have published a number of papers which relate to consumer credit. While the PRA is focusing on firms' asset quality and underwriting practices the FCA is focusing on consumer protection, with specific interest in assessing creditworthiness including affordability and the high cost credit market which includes overdrafts. The FCA has also set out a package of remedies designed to make the credit card market work better and the Group has a project in place to meet a number of the requirements by January 2018 and the remainder by June 2018;
- the European Commission published a package to amend CRD IV in November 2016. The amendments cover a variety of areas including Pillar 2; counterparty credit risk; trading book/market risk; large exposures; IRRBB; the SME supporting factor; and, support for infrastructure lending;
- the Basel Committee on Banking Supervision (BCBS) revisions to the standardised approach to credit risk (CRSA), operational risk, and IRB floors are yet to be finalised. Uncertainty remains around the final shape of these rules. The strategic intent to pursue IRB accreditation will minimise some of the impacts to the Group of the revised CRSA, although those rules will also affect the IRB floors;
- the recovery and resolution regime for UK banks is still being finalised. The BoE has established a framework on setting the minimum amount of loss absorbing resources (MREL) banks should hold so they can be resolved when failing. The Group has been advised of its interim MREL and has submitted a plan to the BoE on how its market issuance will be phased to reach this. The PRA has also finalised its rules on ensuring banks' critical shared services are able to continue operating while in resolution. The Group is well placed to comply with these requirements; and
- the Markets in Financial Instruments Directive II (MiFID II) and Packaged Retail and Insurance-Based Investment Products (PRIIPs) Regulation come into effect in January 2018. MiFID II imposes significant changes in a number of areas including transparency, market structure and transaction reporting. The PRIIPs Regulation requires firms producing or selling packaged retail investment products and insurance-based investment products to produce key information documents to make it easier for retail investors to compare products. The Group has a programme in place to implement these requirements.

Risk overview

> **“** Effective management of risk is a key capability for a successful financial services provider and is fundamental to the Group’s strategy. The Group has continued to advance and strengthen its risk management capabilities, evolving in line with industry developments and best practice. **”**

The Group’s approach to risk

Risk exists in every aspect of the Group’s business, is an integral part of the operating environment, and is a core consideration inherent within the Strategic Plan.

The Group’s approach to risk management is based on the principle that risk management capability must be embedded across all areas of the Group to be effective.

The Group has a clearly defined strategy in place to monitor, manage and mitigate risk and that strategy is defined with the Group’s Risk Management Framework (RMF).

The risk strategy includes: ensuring all principal and emerging risks are identified and assessed; that risk appetite is clearly articulated and influences the Group’s strategic plan; the maintenance of a clearly defined risk culture which emphasises risk management while maintaining independent oversight; the need for ongoing analysis of the environment in which the Group operates to proactively address potential risk issues as they arise; and a requirement to ensure that appropriate risk processes, systems and controls exist to support all colleagues in their decision making.

Integral to the RMF is the Group’s process for setting its Risk Appetite. The Risk Appetite Statement (RAS) defines the level and types of risk the Group is willing to assume within the boundaries of its risk capacity, to achieve its strategic objectives. Ultimately, the RAS provides the definitive view on the broad direction of risk taking activity the Board is comfortable that the Group undertakes and allows decision makers to exercise judgement with greater confidence and speed.

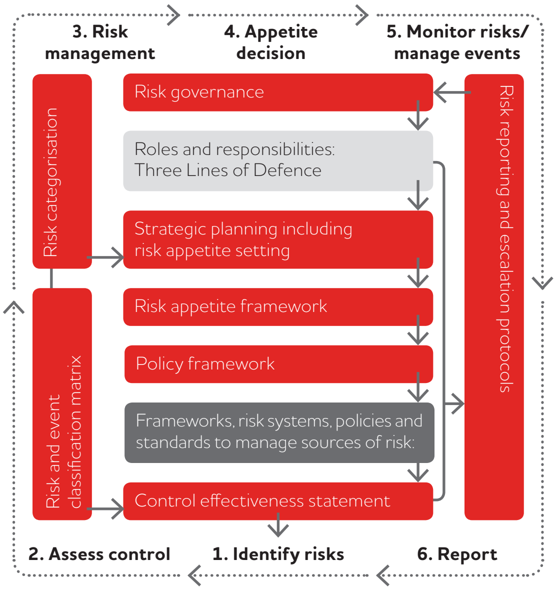
Risk culture

The consistent fair treatment of customers is fundamental to the success of the Group’s business model and strategy and is underpinned by a risk culture which shapes behaviours and decision making at all levels of the Group. The interests of customers, colleagues, shareholders and the communities within which the Group operates are all aligned to deliver the Group’s strategic aim of sustainable customer growth. This is supported by the RMF, underpinned by a robust risk framework and independent risk management function driven by the Group’s expected behavioural standards and values.

A strong risk culture is founded on a risk management accountability model and formal delegation framework where personal accountability empowers colleagues to take ownership. It is a consideration in all people management practices, particularly performance management. It is supported by a formal whistleblowing framework that allows colleagues, in confidence and anonymously, to raise concerns about matters of conduct, including inappropriate behaviour and breaches of the Group’s Code of Conduct.

Risk Management Framework (RMF)

The Group identifies and manages risk using the RMF (see diagram below), which is the totality of systems, structures, policies, processes and people that identify, measure, evaluate, control, mitigate, monitor and report all internal and external sources of material risk. The Group’s Policy Framework is a key component of the RMF providing structure and governance for the consistent, effective management of Policies. This aligns with the behavioural expectations for all colleagues which form a core part of our performance management approach. Policy statements and supporting policy standards define the minimum control requirements which must be observed across the Group to manage material sources of risk within risk appetite.



The Group manages risk using a “Three Lines of Defence” model. The Three Lines of Defence are the operational Business Units, the Risk Management function and Internal Audit. Control is exercised through a clearly defined delegation of authority, with communication and escalation channels throughout the Group.

Principal risks are overseen by the dedicated second line risk management function

Credit risk is the risk of loss of principal or interest stemming from a borrower's failure to meet contracted obligations to the Group in accordance with the terms agreed. Credit risk is evident at both a portfolio and transactional level.

How this risk is managed

- Significant credit risk strategies, credit risk appetite and tolerances for credit risk are approved and reviewed by the Board and Boards' Risk Committee.
- The credit portfolio is closely monitored with actions initiated where required.

Balance sheet and prudential regulation risk covers a number of categories of risk, which affect the manner in which the Group can support its customers in a safe and sound manner. The risks include the need to withstand times of stress for the loss of funding (liquidity), the impact of restricted access to future sources of deposits (funding), the impact of providing a defined benefit scheme to colleagues (pension) and the need to withstand severe unexpected losses (capital).

How this risk is managed

- Liquidity is managed in accordance with standards that are approved by the Board and supported by annual Funding and Contingency Funding Plans. The Group also completes a formal annual assessment of liquidity adequacy which is shared with the PRA.
- The Group completes a formal annual assessment of its capital requirements which is shared with the PRA.
- The Group's Pension Risk Management Committee has implemented a range of reforms to benefits to reduce the Group's exposure to Pension Risk.

Regulatory and compliance risk is the risk of failing to identify, understand, monitor and comply with relevant laws, regulations, licence conditions, supervisory requirements, self-regulatory industry codes of conduct and voluntary initiatives. In doing so, the Group risks damaging its relationship with its regulator. It is also the failure of not keeping regulators informed of relevant issues and not responding effectively to information requests and regulatory reviews.

How this risk is managed

Continued and significant Board and senior management focus is directed towards maintaining regulatory compliance. The Board or Executive Risk Committee approves all material changes to regulatory policy and protocols.

Conduct risk is the risk of undertaking business in a way which is contrary to the interests of our customers, resulting in the delivery of inappropriate customer outcomes, customer detriment, regulatory censure, redress costs and/or reputational damage.

How this risk is managed

- The Group has a Conduct Framework, with supporting target outcomes and operating principles. Governance oversight and reporting are in place to ensure those objectives are met.

Operational risk is the risk of loss resulting from inadequate or failed internal processes and systems or from external events. It includes legal risk, and operational risks associated with the execution of the strategy.

How this risk is managed

- The Group has an established Operational Risk Framework to enable identification, management and mitigation of operational risks. Risk categories are used to categorise and facilitate the consistent identification, assessment, mitigation, monitoring and reporting of risks and events.

Financial crime risk is the risk that the Group's products and services will be used to facilitate financial crime against the Group, its customers or third parties.

How this risk is managed

- The Group has an established Financial Crime Framework supporting ongoing management, monitoring and mitigation of financial crime risk. The Group operates zero tolerance for financial crime risk and has a control framework in place to mitigate this risk.

Strategic, business and financial performance risk is the risk of significant loss, loss of earnings and/or damage arising from business decisions that impact the long-term interests of stakeholders or from an inability to adapt to external developments.

How this risk is managed

- The Board approves and oversees the execution of the Strategic Plan and associated strategic risk following the recommendations of the CEO and Executive Leadership Team. The Group's risk appetite statement (RAS) sets out the risks it is able and willing to take to achieve its strategic objectives.

People risk is the risk of not having sufficiently skilled and motivated colleagues who are clear on their responsibilities and accountabilities and who behave in an ethical way.

How this risk is managed

- Roles, responsibilities and performance expectations are defined in role profiles and expanded through objective setting and ongoing performance management.
- The quality and continuity of our leadership is reviewed and assessed through succession planning and talent management activity.

Highlights of the year

October | November | December | January | February | March

STUDIO B OPENS

We opened our innovation lab in London during April. Studio B is a physical manifestation of our digital ambitions and gives us the opportunity to lead the way on innovation and shape the future of our industry.

It allows us to collaborate directly with customers and third parties, including Fintechs, to solve the banking problems of tomorrow, offering insight into the sort of technologies and services that could be available in the future. We are able to rapidly develop new concepts with consumers in a test and learn environment, with the best being deployed across our channels and customers.

APRIL

April | May | June | July | August | September

CYBG's long-established Retail and SME franchises have significant scale and strong market share in personal current accounts, business current accounts, mortgages and SME business lending in our core regions. In 2017, we made significant operational progress with improvements in our customer experience taking effect. This in turn is enabling us to deliver the mid-single digit loan growth we are targeting and which is prudently funded through our strong customer deposit franchise.

Deposits/funding

Above: The first B store in Birmingham opened in September – a flagship property for CYBG in the heart of the Midlands.

We offer a wide range of current accounts, savings accounts and term deposit products for personal and business customers. At 30 September 2017, the Group had £13.9bn of current account balances, £7.7bn of savings account balances and £6.0bn of term deposit balances.

CYBG has a loyal personal current account (PCA) customer base that represents a stable source of funding and sets us apart from most other challenger banks. We had approximately 1.8m PCA customers as at 30 September 2017, of which 37% also held savings accounts, 14% held CYBG credit cards and 6% held mortgages with us. Last year we identified key customer demographics in which we are underweight and have targeted growth across younger and more affluent customers. A key element of our strategy that supports our targeted growth in these demographics is the launch of B – our digital banking proposition, with current account, linked savings account, and credit card products that help customers manage their money and plan their savings through the use of customer-defined savings pots. As B develops, further features will become available for customers in the future including loans and mortgages.

B's product offering and advanced functionality has resulted in a market-leading customer experience and, at September 2017, B had a Net Promoter Score (NPS) of over 40. As a result, since its launch in May 2016, B has over 100,000 accounts and deposit balances of c.£1bn. B's success to date, combined with its low cost to serve and nationwide presence, means it remains a key element of our customer and deposit strategy.

We made improvements to our PCA proposition during the year, including a reduction in the time to open a bank account from 45 minutes when opened within a branch and 12 days on phone, down to 20 minutes for each. We also introduced Android Pay, in addition to Apple Pay that was introduced last year.

> B's product offering and advanced functionality has resulted in a market-leading customer experience

Business current accounts have shown healthy growth over the year, both in terms of volumes and the number of customers. This is partly due to our renewed investment and commitment to the SME market, which we believe is underserved by the larger incumbent banks, and the 25 months fee free offer currently available to new customers or switchers. Progress is currently being made to extend the B account for micro and small business customers in 2018, so that businesses can manage their money and forecast in the same way as personal customers.

Term deposits and cash ISA savings products remain an important part of our customer offering and a key element in our funding strategy. In line with our channel development strategy, a range of digital and omni-channel offers have been tested with customers. Demand has been high for these offers and very positive feedback has been received from customers on the process and proposition.

Total term deposit and savings account balances did reduce over the course of the year as CYBG took advantage of relatively low cost funding from the TFS and used the opportunity to run off more defensive term deposit and savings balances. However, these reductions were partially offset by an increase in B savings account balances.

Overall customer deposit balances including current accounts increased by 2.5% or £0.7bn in the year as part of a balanced approach to funding our loan growth.

We continue to have a diverse wholesale funding strategy which includes balances secured on our high-quality mortgage book and deposits with other banks. During the year we drew down £1.9bn from the BoE's TFS and completed our inaugural MREL issuance transaction which was £300m of senior debt and was well received by the market.

Mortgages

We have a strong and growing mortgage franchise, with the majority of customers sourced through a network of brokers that allows us to diversify risk across the entire UK. As at 30 September 2017, we had 164,000 retail mortgage accounts, diversified across multiple regions in the UK.

The total mortgage book increased by 7.5% in the year to £23.5bn, compared with market growth of 2.9% over the same period. We advanced £5.5bn of new mortgages in the year with 80% of this coming through our broker network, while our proprietary mortgage business delivered 20% to our retail and private banking customers. The UK mortgage market continues to be dominated by brokers and, while digital capability is emerging, this remains a very small part of the market. The journey customers go through when choosing a mortgage with us is a key area of focus, with multiple enhancements made to our service offering in 2017, most notably a 50% reduction in time from application to offer for all customers and the delivery of a fully packaged application to offer in less than 10 days. This enhanced customer journey makes a real difference to both customers and brokers, with customers having certainty quickly over our ability to lend to them. We are committed to enhancing both customer and broker journeys, which will position us well as the market continues to evolve.

We are continually looking to enhance our mortgage offering and 2017 saw further progress in improving our customer proposition. For example, our mortgage offers are now valid for 180 days, up from the previous 90 days. We have also reduced the amount of documentation we request from brokers as part of the application process without compromising our data capture, making it easier for brokers to do business with CYBG.

These incremental process improvements have enabled us to increase our share of broker business and reduce the proportion of consumers that drop out part way through the application process. This has enabled us to capture market share in the mortgage market without compromising on pricing or weakening our underwriting standards.

Left: In the B app, customers can set up and name 'savings pots' making it easier to put money aside regularly. Other B smart tools, such as the sweep facility and budgets, have also been designed to help make saving simpler.

We also have a successful mortgage retention proposition and customers are now able to switch to a new deal up to three months before the end of a fixed rate term without incurring an early repayment charge. We have also launched an online broker switch portal that makes it easier for brokers to switch to a new deal for their customers.

> Incremental process improvements have enabled us to increase our share of broker business and reduce the proportion of consumers that drop out part way through the application process.

The BTL market represented a smaller proportion of the growth in the mortgage portfolio in the year to 30 September 2017, due to regulatory changes and our continued focus on the owner occupier market. The changes in the taxation regime, coupled with tightening underwriting standards, have slowed growth in the market as a whole. Our BTL strategy remains unchanged and we continue to lend to this segment within our clear and prudent risk appetite.

The average loan to value (LTV) of the mortgage book is 57.5% and the average LTVs of the owner occupied and BTL portfolios are 56.9% and 58.6% respectively. The loss rate on the mortgage portfolio continues to be at historically low levels and the book is well diversified across the UK. This strong position is partly due to the underwriting process, where the Group primarily uses automated credit decision tools to support its underwriting services, supplemented by a robust manual underwriting process. Successful IRB accreditation should enable CYBG to be more competitive in other areas of the mortgage market, while maintaining a healthy risk position.

SMEs

SMEs are the engine of the British economy and we believe CYBG has a critical role to play in providing banking services for start-ups, cultivating established businesses as they scale up and encouraging sector expansion and innovation. At CYBG, we have a proven track record of being a regional economic champion and in April we announced a £6bn lending commitment, available to UK SMEs over three years to 2019. We advanced over £2bn of new loans and facilities in the first year and our SME business is a key differentiator for us in the market.

We have a strong belief that we need to understand how SMEs are performing UK-wide, both now and in the future, in order to support them in the best way possible. With this is mind, we launched our SME Health Check Index, a quarterly report, in collaboration with the Centre for Economics and Business Research (Cebr), in June, which analyses different statistics to evaluate the health of the business and macroeconomic environment. Despite being in its infancy, the index has already been well received by business and industry – our business banking teams are relishing the opportunity to discuss the regional results with current and potential customers, while analysts have used the report findings in their work.

This year has seen excellent momentum in our SME business, with a strong pipeline and drawdowns up 13% year on year. In support of our lending pledge our core SME balances grew 6%, in line with our expectations.

We provide SME customers with a full range of products and services including a deposit portfolio, which consists of business current accounts, variable rate savings accounts and fixed rate term deposits. We also have a range of lending products and services for SMEs across a £7.3bn portfolio, which consists of term lending, overdrafts, revolving credit facilities, working capital, trade and treasury solutions. We also offer business banking products and services to larger SMEs and mid-corporate businesses where we have the sector expertise, experience and relationships to do so competitively and have a range of propositions designed for specific industries. We are proud that 57% of our business customers have been with the Bank for more than 10 years and retain a commitment to local relationship management for all businesses with turnover above £2m.

SMEs are the engine of the British economy, and we believe CYBG has a critical role to play in providing banking services for start-ups, cultivating established businesses as they scale up and encouraging sector expansion and innovation.

We are continuing to develop our product, service and sector propositions for key customer segments as we actively seek to grow our lending portfolio and support our SME customers. The Fintech partnership we have launched will provide an innovative online lending facility for our small business customers who will benefit from faster decision making and fulfilment of funds, through an easy to use online application. The technology will eventually provide a fully automated review and approval for the customer, with funding provided on acceptance.

In addition, SME customers will begin to migrate onto iB for both mobile and web in 2018; this will enhance our service offering for small businesses by leveraging the capabilities of our iB platform already built and tested in other channels.

We also provide relationship banking for our small business customers delivered through 79 centrally based relationship managers via telephone (Business Direct). This channel will also next year be migrated to our iB digital platform enabling an integrated approach to banking.

Given our history of supporting the economies of the north of England, we are very supportive of the Government's Northern Powerhouse initiative and its aim to spread economic growth more evenly across the UK. CYBG believes passionately that the Northern Powerhouse offers significant opportunities for SMEs in the North of England and we believe that we are uniquely placed to help them benefit from this opportunity.

Our non-core portfolio continued to run off as planned, reducing by 30% in the year and is now £0.5bn or less than 7% of the total portfolio.

Personal lending

The Group has taken a cautious approach to the unsecured lending market and has continued to invest judiciously in our digital capabilities as part of our omni-channel approach. During the year, our personal loans book increased by 2.7%, while the credit card book reduced by 1.1% due to the competitive pricing environment and long duration balance-transfer periods from peers, which CYBG has chosen not to compete with. We also introduced the B credit card in June of this year which has attractive features like an absence of charges for purchases made abroad as well as the ability to tag and track spending on the innovative B app, and this has been well received by our customers with over 10,000 cards already active.

We remain comfortable with the asset quality of our unsecured lending book and will continue to offer personal unsecured lending to customers in a manner reflecting our risk appetite and the emerging economic environment.

Highlights of the year

October | November | December | January | February | March

FINANCIAL INJECTION DOUBLES PRODUCTION AT SHETLAND MUSSELS

At CYBG, we understand that SMEs are the engine room of the UK's economy – with SMEs accounting for 99% of businesses in the private sector. It's therefore vital that we are supporting businesses offering the right support and finance to ensure their success.

One example of this is our support of Shetland Mussels Ltd, which is set to double production thanks to our multimillion pound finance package.

The company already supplies over 900 tonnes of mussels to restaurants, wholesalers and retailers up and down the UK every year, but it's expected that this will grow significantly by 2020. A family business, Shetland Mussels is owned by father and sons Lollie, Richard and Michael Tait. The company already provides jobs in Shetland and expects to increase their number of employees over the coming few years.

JUNE

April | May | June | July | August | September

Delivering to our stakeholders

Delivering sustainable value for our customers, colleagues and communities is an integral part of our overall business model and key to our future success. Continuing to address our broader responsibility to society and managing the environmental impact from our day-to-day operations remains fundamental to our strategy and long-term ambitions.

Customers
We care about our customers and their individual needs. Our strategy is designed to help us support our existing customers, as well as attract new ones, and achieve sustainable growth. We aim to help our customers develop a healthy relationship with money and make their day-to-day management of money simple through the development of our products such as B.

Listening to our customers and anticipating their needs, as well as addressing the root cause of any concerns, is a key input into the ongoing development of our products and services.

For more detail see page 29

Colleagues
Our colleagues are integral to our ongoing success and our overall business performance is dependent on their engagement and advocacy. In the same way that we are transforming our business for our customers, we are investing in our colleagues. We are creating a workplace where every colleague can reach their full potential in an environment which nurtures a diverse, inclusive and committed workforce. We are striving to build a high-performing culture where colleagues can use their initiative, act with greater autonomy, and connect with each other to deliver the right customer-focused outcomes, regardless of where they work or what they do across the Group.

For more detail see page 30

Communities
Our support for our customers and the wider communities, through our range of initiatives, form part of our corporate responsibilities. Our community initiatives, together with our community partnerships, collectively support the communities where we live and work and help demonstrate how 'we care about here'.

For more detail see page 32

Environment
The Group's commitment to operating in a sustainable way is underpinned by our Environmental Standard that recognises our need to meet key legislative compliance requirements, voluntary commitments and covers our approach to environmental management, controls and reporting. The Group acts to prevent pollution and the use of natural resources through increased recycling and transition to lower emissions energy sources where practicable.

For more detail see page 34

Customers

Understanding our customers is part of our DNA. We constantly seek customer feedback and put this at the core of the development of our products and services. Customer advocacy is monitored continually through various ways, including NPS. This focus on our customers' perception of our offering enables us to respond, build and innovate around real customer needs and ambitions. Indeed our digital banking solution - B - was built as a direct result of what our customers told us they needed from a bank in today's always-on world.

We also understand that customers can become vulnerable at any point in their lives and as a result may need our support. We encourage our customers to let us know if they need our support and through our omni-channel service and empathetic staff, are able to work with customers as individuals, identifying solutions and providing the appropriate support as and when they need it.

Progress in FY2017

We continue to serve over 2.7m customers, with overall customer numbers remaining stable, while our B customer numbers have grown to over 100,000. Customer satisfaction and advocacy are key measures and we have enjoyed steady levels of satisfaction across all of our brands. The highest levels of satisfaction being for B customers – with 86% happy with the service they received, and 45% giving the service the maximum 10 out of 10.

At the forefront of our strategy to drive sustainable customer growth is the need to continually innovate, creating unique, customer-led propositions that attract new customers to the Group. In April we opened the doors of Studio B in Kensington, an innovation lab which operates on the high street within a fully operational customer banking centre. The mission of Studio B is for the next generation of customers to design the next generation of banking. The lab within Studio B works directly with customers to co-create new concepts and solutions, publishing the best concepts to a public website to gather direct customer feedback. The best of these concepts are taken forward into full development and deployment across our channels.

We aim to get our service right first time every time, learning from any mistakes and driving continuous improvement. This year the Financial Conduct Authority (FCA) changed the way customer complaints are reported. To comply with these new rules on improving complaints handling we now include complaints resolved in shorter timescales when reporting our complaints numbers.

When we do make mistakes, our goal is to provide our customers with fair outcomes consistently and promptly.

Development of B and the iB platform

B is our digital first brand, offering customers a current account, savings account, credit card and app that together help customers to take effortless control of their money. B is supported by the existing CB and YB customer banking centre network, and a 24/7 dedicated B contact centre. As the primary brand for attracting new target retail customers, the customer centric development of B drives the underlying development of the iB platform, to the broader benefit of CB and YB customers.

Throughout 2017 a range of B and iB developments have been implemented, responding directly to customer feedback. Examples of these improvements include:

- the redesign of the navigation within B to make it easier for customers to use on the go;
- the introduction of fingerprint login to make it easier to securely login to the app;
- the launch of the B credit card to give customers greater control of their everyday finances; and
- the introduction of digital statements to enable customers to go paperless without losing control.

In August, we relaunched the CB and YB mobile apps on the iB platform, migrating existing customers from a 3rd party provided service. By moving customers onto the iB platform, they are able to benefit from some of the customer experience improvements first developed for B, such as the fingerprint login and digital statements. Our ambition to grow our customer base outside of our traditional CB and YB heartlands means the launch of our B store in Birmingham was a hugely exciting milestone, enabling us to increase our presence in one of the UK's most vibrant regional economies. The design and customer experience within the B store has been directly influenced by the design and concepts developed and tested within Studio B (London). As well as being a fully operational customer banking centre, the store provides an exciting and inspiring location for customers to experience our digital services and to participate in concept co-creation.

Delivering to our stakeholders

Serving our business customers
As we continue to digitise our bank and create a more innovative business, we are driving growth in the business sector through strategic associations with Fintech companies. Our first Fintech collaboration is an innovative online lending solution for SME customers.

This year we announced that we would lend at least £6bn to SMEs over three years to help promote the growth of these businesses in the UK. In June, we launched our SME Health Check Index, taking the temperature of small businesses in the UK – this quarterly report with the Centre for Economics and Business Research (Cebr) is a new industry report that measures business performance and the macroeconomic environment affecting SMEs, including business costs, capacity, confidence, lending and revenue.

Recognition for our work
We have won a number of awards this year, including:

- Best Digital Bank United Kingdom at the Capital Finance International Awards;
- Fairbanking Foundation – best current account with overdraft for B;
- Digital Launch of the Year for B at the 2017 FStech Awards; and
- Challenger Bank of the Year at the Corporate Entrepreneur Awards 2016.

Colleagues

Our colleagues are integral to our ongoing success and our overall business performance is dependent on their engagement and advocacy, with significant progress made during the year to improve our offering, including:

Our culture
This year, we began a major programme to develop the positive culture we are aiming for. This programme has several critical elements:

- **Our values and behaviours** were refreshed in June and define the desired behaviours for every colleague in the Group. Our values (Be ambitious, Be courageous, Be curious, Be all over it and Be connected) are brought to life through their associated behaviours. Every team has personalised the behaviours to their business area, and every colleague has a personal goal in relation to our values to support their own development. By turning these words into actions, we are helping to build a Group where colleagues are focused on meeting the needs of both their own development and our current and future customers.
- **Great leadership** is our new leadership framework and was introduced at the same time as our refreshed values. All leaders play a critical role in creating culture and driving performance and so Great Leadership sets the expectations of all leaders. Our leaders are being supported with targeted leadership development to help them to Lead with Purpose, Drive Inclusion, be Always Agile, Grow Trust, Be Connected and Stretch Possibilities.
- **Recruitment and performance management** have both been updated to reflect our cultural aims. Internal and external selection is now based on our values, ensuring we recruit and promote colleagues who align with our culture. Our performance management approach has been transformed to a team-focused, forward-looking approach, which helps every colleague to achieve their personal best.

Engagement and communication
This has been a year of transformational change and ensuring that our colleagues remain engaged is critical. MyVoice (our annual colleague feedback survey) provides us with insight in relation to our values and behaviours, alignment with our strategy and focus on serving our customers. 90% of colleagues understand how the work they do contributes to the Group's goals while 84% fully support our values.

Our primary digital communications channel is our intranet home page, Our World, and in its first year (to August 2017) there was an average of c.6,000 unique visitors per day, with over 370 articles published relating to our leadership, strategy, culture, business success and community activity. This site is increasingly used for two-way engagement through the use of polls, discussion threads and invitations to get involved in activities. This year our communications won the award for the 'Best Use of Interactive Media' at the IoIC Scotland Awards.

Inclusion
Inclusion is at the heart of our culture. It's written into our values. We are committed to fostering and sustaining a truly inclusive culture where every colleague and customer feels they belong. We want all colleagues to recognise this and work together to ensure that inclusion achieves its promise.
We ensure equality, diversity and inclusion by concentrating on ensuring that every colleague feels comfortable to be themselves, to ask questions, to be curious and operate at their personal best.

Reflecting the importance of inclusion, this year our five network groups for gender, age, disability, ethnicity and sexual orientation were re-energised and sponsored by members of the Executive Leadership Team, unlocking access across the Group and acting as ambassadors for the Group externally.

Some specific highlights of the year include:

– events and activities held to celebrate and improve awareness of World Aids Day, International Women's Day, International Transgender Day of Visibility, National Inclusion Week, Carers Week, and religious celebrations including Ramadan and Vaisakhi;

– becoming a signatory of the Women in Finance Charter. With a long-term objective to be gender-balanced in senior management, we have committed to a target of 40% of those in senior management roles to be female by 2020. We are making good progress and as at 30 September 2017, 35% of our senior managers are female;

– helping ensure colleagues have the right tools available to break down the stigma of talking about mental health by launching new enablement and wellbeing resources. These included a new mental health awareness training module, a people leader toolkit and online support materials. We also supported Mental Health Awareness Week in May; and

– worked closely with LGBT Youth Scotland to broaden our reach and connection in the community. We have also significantly increased our participation in Pride Glasgow, connecting campaigning, social responsibility and commercial opportunity.

As at 30 September 2017, our strong, diverse and engaged network of colleagues included:

– 5,813 permanent FTE, 63% of which are female, 37% male

– three women and nine men on our Board

– three women and seven men in our Executive Leadership Team

Gender pay gap

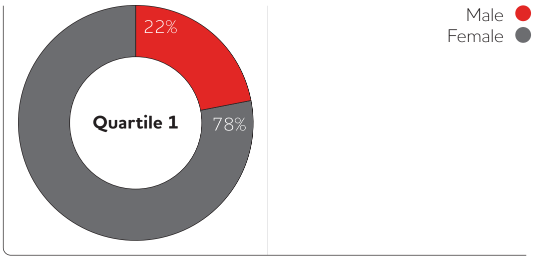
An important element of inclusion is to reduce our gender pay gap. As part of this year's Annual Report and Accounts, for the first time, we are disclosing our April 2017 gender pay gap in accordance with the UK Government regulations for gender pay gap reporting.

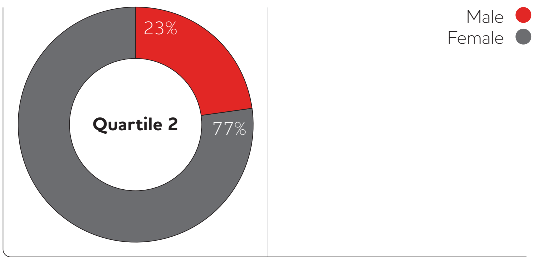
Our overall mean and median gender pay and bonus gap based on a snapshot date of 5 April 2017 (pay) and bonus paid in the 12 months to 5 April 2017 is:

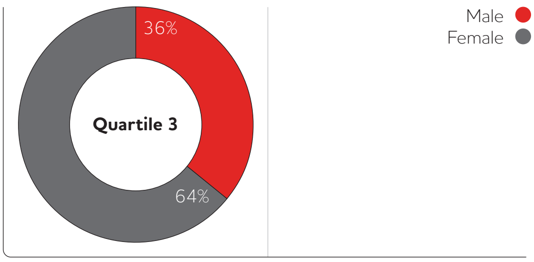
Pay and bonus – difference between males and females

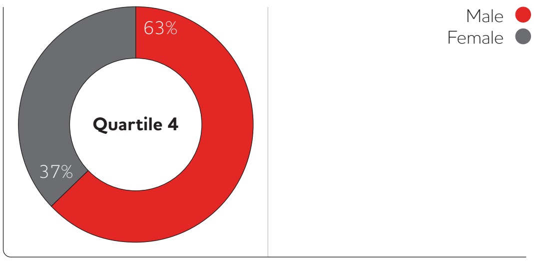
	Mean	Median
Hourly pay gap	37%	36%
Bonus pay gap	58%	39%

Proportion of males and females in each pay quartile (each containing just over 1,690 colleagues, shown lowest to highest)









Delivering to our stakeholders

Proportion of males and females receiving a bonus payment

	Male	Female
	85%	90%

We are confident that we do not have equal pay issues, and conduct a biannual equal pay audit in partnership with our trade union, Unite. Through this audit we review the gender distribution of performance, base pay, allowances and bonuses paid to our staff. We are confident that performance is not gender biased and where pay gaps exist they are not driven by gender.

Our gender pay gap is largely driven by the fact that we have more men than women in senior roles. Our Women in Finance Charter commitments are a public demonstration of our ambition to increase the proportion of women in senior roles. We are also working to increase career progression at all grades.

This commitment includes:

- reviewing our approach to parental leave to encourage shared parental leave;
- reviewing other working policies to make flexible working easier, particularly in more senior roles;
- ensuring our recruitment processes attract a diverse range of candidates;
- making our unconscious bias training mandatory for all colleagues;
- establishing a sponsorship programme to develop more diverse leaders;
- formally linking executive reward to our inclusion targets;
- continuing to undertake our equal pay audits in conjunction with our trade union Unite;
- transforming our performance management approach to encourage ongoing personal improvement, removing the risk of any gender bias; and
- reviewing our reward practices to ensure they help us reduce any gender pay gaps.

Through all of these practices we are aiming to create meaningful progress with regards to inclusion in senior management, based on robust pipelines of diverse talent.

Community

We bring our social purpose to life through our commitment to make a positive contribution to the local communities in which we live and work. This is expressed through a series of community partnerships and initiatives that deliver our 'We care about here' ethos. The Group recognises the important role we play as an enabler of change in local communities and society at large.

Our charitable foundation supports our colleagues by enabling them to help causes they support regularly in their local communities by providing grants and encouraging volunteering of their time and expertise. The Group supported National Volunteering Week in June and encouraged colleagues to use their two day entitlement to support local charities. 287 employee grants were awarded totalling over £141,000 and almost 7,000 volunteering hours were undertaken during the year.

Support for charities is provided through our annual **Spirit of the Community Awards**. Now in its fifth year, awards of £5,000 were made to 30 charities under three categories of Employability, Financial Education and Environment. Over 300 applications were received and the charities collected their awards at ceremonies in Leeds and Glasgow in June. The event in Glasgow was attended by the full CYBG Board. Awards totalling £160,000 were given out and the total over five years amounts to £860,000 awarded to 143 charities.

Financial education – Our 'Count me in 123' financial education programme is available in our branches, online and via public libraries in Leeds and Glasgow. The materials support parents and carers to engage with their pre-school children and have fun with maths. Over 65,000 booklets have been distributed via our branches and the game is available to download on Apple and Android tablets. Our colleagues also support children in schools by volunteering with reading and numbers programmes.

Hospice UK charity partnership – We celebrated our 10th year supporting Hospice UK. Through the tremendous enthusiasm of our colleagues and the matched funding through our foundation we raised £5.8m for the charity to help provide hospice care across the country. In addition to fun events throughout the year, colleagues took part in a marathon challenge in the Tweed Valley of the Scottish Borders in September and raised over £100,000.

European City of Culture – During the year, Yorkshire Bank supported Leeds' bid to be European City of Culture 2023. The Group is supporting a programme of cultural events in 2017 and 2018 that aim to showcase and enhance existing Leeds festivals, as well as giving scope for new ones.

Community partnerships

The Royal Zoological Society of Scotland (RZSS) – Our 'Wild about Scotland' educational outreach programme, in partnership with RZSS, continued to travel the length and breadth of Scotland teaching primary school aged children about Scotland's native species and natural environment. It helped engage the next generation of conservationists, while bringing RZSS' expertise to communities that might not otherwise have been able to benefit from it.

A team of volunteers supported the programme at a series of community events across the country at weekends and school holidays. Families hopped on the bus to take part in fun activities on Scottish wildlife, such as guess the animal skulls, build a beaver dam and look at minibeasts under microscopes.

An extra special community event took place at RZSS' Edinburgh Zoo on Father's Day in June, when over 400 guests from five different Scottish charities visited the Zoo and took part in the second annual Wild about Scotland Day.

Scotland's Charity Air Ambulance (SCAA) – Our support for SCAA is now in its third year and has helped to keep the aircraft in the air saving lives across Scotland. Last year the aircraft responded to over 300 emergency call outs.

Volunteers from the Group supported the charity at the Blair Atholl Horse Trials. Our colleagues, along with our agencies, also dedicated their expertise to help design and print customer communications, including their Annual Report and Accounts.

SSE Hydro – Our support for the SSE Hydro, the world's second busiest music venue, continued during the year. We continued to use the SSE Hydro to reward customers and the wider public for playing an active role in their local communities through our 'Centre Stage' reward programme and to date, over 250 people have enjoyed attending a series of concerts. Our unique seat upgrade initiative, 'Get me in the Vault', together with other competitions, proved very popular with more than 46,000 entries into 250 competitions.

Yorkshire Bank Bike Libraries (YBBL) – The legacy community initiative from the Grand Departé of the Tour de France in 2014 rolled into its third year. A total of 46 bike libraries have been established across the county and the public continued to donate their old and unwanted bikes with over 5,000 being distributed. This resulted in over 48,000 opportunities for children and their families to borrow a bike.

The initiative was recognised and shortlisted for three prestigious awards during the year from the European Sponsorship Association, The Sponsorship Awards 2017 and BT Sports Industry Award for Community Programme of the Year.

The YBBL programme was the official partner of Stage 3 of the Tour de Yorkshire, with children's parades and activation tents promoting the service. We supported the Tour de Yorkshire in our customer banking centres and our colleagues volunteered to help with the free fun activities for the local communities in large tents at the start and finish towns each day. The Tour de Yorkshire attracted 2.2m spectators along the route and was viewed by c.10m people in 180 countries.

Environment

During the year, the Group made a contribution towards the drive for a low carbon and more resource efficient economy through:

- establishing a standalone Environmental Standard for the Group and setting up a standalone group system to capture and report on greenhouse gas (GHG) emissions;
- procuring 100% renewable green energy for electricity within Group's direct control;
- continuing to roll out advanced building efficiency management systems as part of the branch refurbishment programme. Such systems help automate controls to ensure we only operate air conditioning units and boilers within set operational hours and can respond quickly to changes in temperatures; and
- retention of our ISO 14001 environmental accreditation in our Leeds offices.

Reporting on GHG emissions

The reporting period for GHG emissions in the Group ran from 1 July 2016 to 30 June 2017.

Total emissions for the Group have reduced by 14% in the last year. Nearly half of the reduction is driven by changes in the emission factors as defined by the Department for Business, Energy & Industrial Strategy guidelines. The Group used the 2016 Department for Business, Energy & Industrial Strategy conversion factors due to the timing of the release of the 2017 conversion factors. The largest change in emission factors is the decarbonisation of electricity generated by the National Grid. Using the same emission factor for both the 2016 and 2017 reporting years and accounting for the impact of FTE and portfolio changes, the reduction in emissions would be 3%.

GHG emissions CO_2e tonnes

Scope	2017	2016
Scope 1 emissions Generated from the gas and oil used in all buildings where the Group operates; emissions generated from Group-owned and leased vehicles used for business travel; and fugitive emissions arising from the use of air conditioning and chiller/refrigerant plant to service the Group's property portfolio.	3,297△	3,835
Scope 2 emissions Generated from the use of electricity in all buildings from which the Group operates.	14,247△	16,743
Scope 3 emissions Relate to business travel undertaken by all colleagues using rail, private vehicles, hired vehicles, contracted taxi services, air travel, waste, water and paper.	6,803	7,595
Total	**24,347**	**28,173**

The Group reports GHG emissions in accordance with the GHG Protocol, which sets a global standard for how to measure, manage and report GHG emissions, with the exception of reporting market based emissions in addition to location based. The Group are working towards this.

Intensity ratio

The Group has chosen to use an intensity ratio of GHG per average FTE for scope 1 and 2 emissions. Using FTE offers a simple way to measure and monitor Group performance on emissions and is also a useful way to benchmark and compare with others.

Scope (1 & 2)	2017	2016
GHG emissions per average FTE	2.61	2.83

The only estimated emissions in the GHG emission data relate to energy consumed in properties where the landlord controls the supply and recharges the Group via a service charge arrangement or where actual meter readings were not available before year end. In these instances an average rate per kWh has been used.

Independent limited assurance

The Group engaged KPMG LLP to undertake an independent limited assurance engagement over the selected information highlighted in this report with a △. KPMG has issued an unqualified opinion over the selected information. The full statement is available on the CYBG website.

Use of resources

In 2017, we created four new environmental targets to measure the Group's performance over the next three years in comparison to a baseline in June 2016. We have made good progress against three, but there is work to do in the next 12 months to increase the volume of recycling across the Group's operational business through promoting staff awareness and improving in-house recycling processes.

Area	2016 restated baseline*	2017 Actual	2016-17 % change	2019 % target	2017 performance
GHG – measured by CO_2	25,096	**24,347**	↓ 3%	↓ 9%	**On target**
Energy (gas and electric) – measured by gigajoules (GJ)	179,649	**172,743**	↓ 4%	↓ 9%	**On target**
Water consumption – measured by m^3 volume	71,528	**69,055**	↓ 3%	↓ 5%	**On target**
Recycling first line waste – measured by % volume	74%	**73%**	↓ 1%	↑ 6%	**Behind target**

*2016 Baseline has been restated to reflect changes in emission factors, property portfolio and FTE numbers during the course of 2016/17.

Highlights of the year

October | November | December | January | February | March

SEPTEMBER

COLLEAGUES STRIDE OUT TO SUPPORT HOSPICE UK

Supporting local communities across the UK is important to the Group and our colleagues undertake around 11,000 volunteer hours a year in support of our charity partners. In September, 150 colleagues pulled on their walking boots and trekked the rolling hills of the Scottish Borders in a fundraising challenge to support Hospice UK.

This is the fifth time we have supported a large fundraising event for Hospice UK and this year the challenge raised £50,000 for the charity's work across the UK, which was matched by the Group to a total of £100,000, adding to the £5.8m raised for hospice care by colleagues since 2008.

Overview of Group results

Our FY2017 results reflect a year of strong financial performance as we have delivered on our strategic priorities in a period of challenging market and economic conditions. We have grown our customer lending without compromising on asset quality, delivered cost savings well ahead of our targets in the first phase of our three year efficiency programme, and taken concrete steps to improve our capital position. We are firmly focused on building a solid base for delivering sustainable returns to our shareholders.

Summary balance sheet

as at 30 September	**2017 £m**	2016 £m
Customer loans	**31,967**	30,147
Other financial assets	**10,469**	9,223
Other non-financial assets	**795**	559
Total assets	**43,231**	39,929
Customer deposits	**(27,679)**	(27,000)
Wholesale funding	**(8,602)**	(5,810)
Other liabilities	**(3,548)**	(3,908)
Total liabilities	**(39,829)**	(36,718)
Ordinary shareholders' equity	**(2,952)**	(2,761)
AT1 equity	**(450)**	(450)
Equity	**(3,402)**	(3,211)
Total liabilities and equity	**(43,231)**	(39,929)

Summary income statement – underlying and statutory basis(1)

for the year ended 30 September	**2017 £m**	2016 £m
Net interest income	**844**	806
Non-interest income	**172**	183
Total operating income	**1,016**	989
Total operating and administrative expenses	**(675)**	(729)
Operating profit before impairment losses	**341**	260
Impairment losses on credit exposures(2)	**(48)**	(39)
Underlying profit on ordinary activities before tax	**293**	221
Restructuring expense	**(67)**	(45)
Separation costs	**(8)**	(11)
Impairment of intangible assets	**–**	(45)
Conduct charges	**(58)**	(51)
Gain on defined benefit pension scheme reforms	**88**	–
Gain on disposal of VocaLink share	**20**	–
Gain on disposal of Visa share	**–**	7
Net gain on debt restructuring	**–**	1
Statutory profit on ordinary activities before tax	**268**	77
Tax expense	**(86)**	(241)
Statutory profit/(loss) attributable to equity holders	**182**	(164)

(1) The summary income statement is presented on a statutory and underlying basis. In addition, the financial key performance indicators (KPIs) used by management in monitoring the Group's performance and reflected throughout this section are determined on a combination of bases (including statutory, regulatory and alternative performance measures), as detailed in the Glossary on page 253. A reconciliation from the underlying to statutory basis is shown on page 47.

(2) Impairment losses on credit exposures relate solely to loans and advances to customers (refer to note 3.5 to the financial statements) and exclude credit risk adjustments on loans at fair value through profit or loss which are incorporated in the movement in other assets and liabilities at fair value within non-interest income (refer to note 2.3 to the financial statements).

Capital position

	2017 £m	2016 £m
Common Equity Tier 1 capital	**2,437**	2,397
Additional Tier 1 capital	**450**	450
Tier 2 capital	**627**	625
Total capital	**3,514**	3,472
Risk weighted assets (RWAs)	**19,678**	19,029

Profits up overall

The Group has successfully delivered on each financial target set out at the Capital Markets Day in September 2016 and reported a statutory profit for the first time since 2011 of £182m (2016: loss of £164m). Significant progress has been made against the Group's strategic priorities, which has led to FY2017 underlying profit before tax increasing to £293m, up £72m (33%). Together with a stable capital base, this has been the primary driver of the increase in underlying RoTE, from 5.2% to 7.5% and underlying basic earnings per share (EPS) from 16.2p to 21.5p. Our disciplined approach to managing our balance sheet has enabled us to increase tangible net asset value (TNAV) from 284.1p to 295.6p per share.

As a result of the progress we have made in improving the performance of our business, we are pleased to declare our intention to pay an inaugural dividend to our equity shareholders.

£1.8bn growth in customer lending

The Group's performance was delivered against a backdrop of challenging economic and market conditions, as the effects of the base rate cuts in 2016 and the corresponding fall in LIBOR rates, together with lower UK credit growth competitive pricing across the industry, prevailed throughout the year. In spite of these pressures, we delivered growth in our mortgage and core SME lending portfolios, up £1.6bn and £0.4bn respectively, and saw an increase in our mortgage market share. We remain cautious in the unsecured lending market, taking a disciplined approach to pricing in a competitive market; nevertheless, our unsecured lending portfolio saw a modest increase in balances year on year.

Growth in the customer lending book has been achieved without compromising asset quality. The Group's cost of risk has remained relatively low at 14bps (2016: 9bps), reflective of the quality and mix of our book with the mortgage portfolio accounting for a high proportion of total customer lending (2017: 73.4%; 2016: 72.4%).

Active management of customer deposits

Customer deposits increased year on year as we saw 5.3% growth in current account balances, with strong recruitment of business current accounts and substantial growth in B savings balances. This growth more than offset the managed reduction in volumes of variable rate savings accounts as we rationalised and repriced our ISA portfolio.

This repricing was part of an overall plan to improve our funding mix, with a shift from higher cost deposits towards lower cost funding. The Group's participation in the Government's TFS was another element of this plan, and together these actions helped to drive down the Group's funding costs, with the blended rate on interest-bearing liabilities falling by 25bps to 75bps.

While the rate environment dampened growth in interest income, the actions taken across the liability portfolio allowed us to grow net interest income by £38m (4.7%). Overall, these factors combined to drive a 1bps increase in NIM to 227bps.

↑ **Underlying profit before tax**
£293m
2016: £221m

↑ **RoTE – underlying**
7.5%
2016: 5.2%

↑ **Basic EPS – underlying**
21.5p
2016: 16.2p

↑ **Loan growth**
6.0%
2016: 4.7%

↑ **Cost of risk**
0.14%
2016: 0.09%

↑ **Deposit growth**
2.5%
2016: 2.2%

↑ **NIM**
2.27%
2016: 2.26%

Overview of Group results

Cost savings well ahead of plan

We continued to improve our operational efficiency during the year through the restructuring and streamlining of our business. We incurred restructuring charges of £67m to deliver gross run rate cost savings of £90m, we saw the benefits of these actions as the year progressed as our full year underlying costs fell by £54m (7%) to £675m, well below our FY2017 guidance of £690m–£700m. As a result, and combined with the increase in income, our underlying cost to income ratio improved from 74% to 67%.

Optimisation of our capital base – CET1 ratio 12.4%

Our key capital ratios remain within our required operating range. The core business generated 13bps of CET1 capital over the year. Offsetting the growth in our core business were the costs associated with restructuring, separation from our former parent and legacy conduct issues which together absorbed 61bps of CET1.

The capital position benefited from the closure of the defined benefit pension scheme (the Scheme) to future accrual for the majority of employees, improving the IAS 19 position by £88m and contributing to an IAS 19 surplus of £207m at the year end. In addition, the trustees completed the 2016 triennial valuation, which resulted in a reduction in the Scheme deficit (on a trustee funding basis) from £450m to £290m and no change to the existing deficit repayment schedule agreed with the Trustee in June 2014.

In April 2017 we submitted our application to the PRA for permission to use the IRB approach to calculating credit RWA. This marked a key milestone in our path to IRB accreditation.

Outlook for 2018

The lending market will, we expect, remain competitive, especially for home loans. However, our pipeline in both our mortgage and SME businesses is strong and supports our plans to deliver continued asset growth. It is likely that we will see further price pressure in the mortgage and unsecured personal loan markets. Our strong deposit-gathering capability, founded on our personal and business current account franchise, will ensure that we fund our growth in a sustainable and cost-effective manner. We expect to see modest pressure on net interest margin and our NIM guidance for FY2018 is 220bps.

Our efficiency programme will capitalise on the momentum seen over the past 12 months, and will focus on procurement and organisational design enhancements in the coming year. With a track record of achieving sustainable cost savings, we are confident in our ability to deliver savings in line with our guidance and further reduce our cost income ratio.

We will manage our capital base within our stated operating range for CET1 of 12 to 13%.

↓ **Underlying CIR**
67%
2016: 74%

↓ **CET1 ratio**
12.4%
2016: 12.6%

↓ **Total capital ratio**
17.9%
2016: 18.2%

Financial performance review

1. Sustainable customer growth

2017 has been a year of strong business growth against of a highly competitive backdrop and uncertain economic conditions. In targeting sustainable growth in our customer balances we enhanced our product offerings to attract the right mix of customer profile to deliver longer-term value. In doing so we have delivered growth while maintaining asset quality, adhering to our underwriting standards and controlled risk appetite leading to a well-balanced and diverse portfolio.

The asset quality of the Group's credit exposures remains stable relative to the growth in portfolio size, evidenced by the reduction in the level of impaired assets to £179m (2016: £233m) and a modest increase in 90 days past due (DPD) to £161m (2016: £150m). In aggregate, impaired assets and 90 DPD represent 1.06% of gross loans (2016: 1.27%).

We have managed our deposits base throughout the year – growing balances, improving the mix and reducing funding costs.

	2017 £m	2016 £m*
Mortgages	**23,480**	21,836
SME lending[1] – core	**6,821**	6,438
– non-core	**504**	720
Unsecured personal lending	**1,162**	1,153
Gross loans and advances to customers	**31,967**	30,147
Current accounts	**13,948**	13,248
Variable rate savings accounts	**7,730**	8,240
Fixed rate term deposits[2]	**5,983**	5,500
Other wholesale deposits	**18**	12
Total customer deposits	**27,679**	27,000

*The 2016 comparative has been restated to reflect the reclassification of £80m of SME loans from the non-core to the core portfolio.

Mortgages

The mortgage book remains the Group's largest asset portfolio and has a significant impact on our overall financial performance. This year we delivered record levels of new mortgage business, which supported net growth of 7.5% in the year, higher than system growth[3] of 2.9%, and saw our market share increase from 1.67% to 1.73%.

In line with our competitors, we continued to see a growing number of customers favour fixed rate mortgage products, as they sought to further capitalise on the prevailing low interest rate environment. As a result, the fixed rate book grew to 73% of mortgage balances (2016: 68%) and accounted for 95% of mortgages drawn in the year (2016: 93%).

The split of our mortgage book between BTL and owner occupied properties remained broadly stable, although owner occupied accounted for 70% of drawdowns in the year (2016: 59%) as we focused on our strategy to support the residential market and manage within our risk appetite limits. The average LTV of new lending was 71% and, as a consequence, the average LTV of the mortgage book increased from 55.8% to 57.5%.

Our proportion of residential mortgages 90 days in arrears has remained stable at 0.52% (September 2016: 0.51%).

(1) Includes financial assets at fair value of £477m (September 2016: £750m).
(2) Includes financial liabilities at fair value of £26m (September 2016: £48m).
(3) System growth is sourced from the BoE 'Mortgages outstanding by type of lender, UK (BOE)' report (MM4).

Financial performance review

SME lending

Our core SME lending portfolio increased by £383m (5.9%) in the year, ahead of system growth[1] of 3.9%. The main drivers for the increase were improved origination flows, coupled with lower attrition in the second half of the year as we implemented a number of new propositions and developed new capabilities to better support the funding needs of our SME customers. These included a new proposition for the financial services sector, and the establishment of an agency capability. Growth finance and cash flow finance also performed well.

We maintained a robust approach to credit decisions on new lending in the year, reflective of the continued reduction in the impaired asset portfolio to £126m (2016: £146m). Notwithstanding an increase in specific provisions on a small number of exposures, the underlying credit quality of the portfolio has remained stable.

In line with our strategy we continued to run off our non-core portfolio, which reduced from £720m to £504m.

Unsecured personal lending

Following a brief period of contraction in our unsecured personal lending book, which comprises credit cards, personal loans and overdrafts, the second half of the year saw modest growth of £9m year on year. Within this, the fixed rate personal loan book was the largest contributor, showing growth of £33m (5%) from £625m at 30 September 2016 to £658m at 30 September 2017. This growth was driven in the main by the launch of an improved personal loan proposition with competitive pricing in the third quarter, supported by enhanced scorecards and a simplified online application process. The uptake in this new offering contributed to higher loan origination in the second half of the year.

Credit card balances were broadly flat at £396m (2016: £400m).

The smallest element of our unsecured lending portfolio is comprised of variable rate personal loans and overdrafts, which fell by £20m in the year from £131m to £111m. Variable rate loans continue to reduce as although these products remain on sale, they are not actively promoted or targeted.

Current accounts

Funding provided by current accounts increased by £0.7bn (5.3%) since September 2016, due principally to continued growth in business current account balances (up £387m) driven by the 25-month fee free offer we launched in December 2016, and system growth. Personal current account balances also continued to grow, with the B current account (up £200m) attracting both existing and new to bank customers throughout the year as we delivered further enhancements in product functionality. Our Current Account Plus product also contributed growth of £140m with the average case size offsetting a declining stock balance. While stock levels across the book fell overall, new account openings were in line with our strategy to grow sustainably in a way that recruits the right profile of customer with whom we have an opportunity to build a long-term relationship.

(1) System growth is sourced from the BoE 'Industrial analysis of monetary financial institutions' lending to UK residents' report (C1.2), and excludes individuals and individual trusts, activities auxiliary to financial intermediation, insurance companies and pension funds, and financial intermediation (excluding insurance and pension funds) results.

Variable rate savings accounts
Funding from variable rate savings accounts benefited from growth of £0.7bn in B savings accounts and £0.3bn in business savings accounts. This partially offset attrition of £1.2bn following the product rationalisation and repricing of our ISA portfolio. In addition we saw attrition of £0.2bn across other savings products as, in line with market trends, we saw a shift in consumer behaviour towards easier access accounts such as instant access and current accounts.

Fixed rate term deposits
Our fixed rate term deposit book increased by £483m (8.8%) as a result of actions taken in the second half of the year, including the repricing of maturing term deposits and competitive retail product launches in the digital bond space and fixed rate cash ISAs, along with the launch of new notice accounts for SME depositors.

Funding and liquidity
The Group continues to maintain its strong funding and liquidity position and seeks to achieve an appropriate balance between profitability, liquidity risk and capital optimisation. Our focus on delivering customer growth, together with a managed reduction in volumes of variable rate savings accounts, and drawdown of £1.9bn of lower cost funding from the Bank of England's Term Funding Scheme, has resulted in an increase in LDR from 112% to 115%, well within our guidance for the year of <120%.

The Liquidity Coverage Ratio (LCR) was higher at 164% at 30 September 2017 (2016: 140%) due to the pre-funding of residential mortgage-backed securities (RMBS) callable in November 2017. Net Stable Funding Ratio (NSFR) was 118% at 30 September 2017 (2016: 124%).

The Group has evolved its approach to managing the liquid asset buffer (LAB) to more efficiently utilise cash to reduce the cost of the LAB while still holding high quality, low risk liquid assets, by broadening the composition of the portfolio. The Group has diversified by investing in a broader range of supranational and covered bond issuances. Previously, liquidity was mainly held in BoE accounts, earning base rate, alongside holdings of UK Sovereign bonds (Gilts).

The issue of £300m of senior debt in June provided further funding to the Group and marked an important first step in our journey towards meeting the BoE's Minimum Requirement for Own Funds and Eligible Liabilities (MREL) by 2022.

Financial performance review

Net interest income

Average balance sheet	2017 Average balance £m	2017 Interest income/ (expense) £m	2017 Average yield/ (rate) %	2016 Average balance £m	2016 Interest income/ (expense) £m	2016 Average yield/ (rate) %
Interest-earning assets						
Mortgages	**22,439**	**652**	**2.91**	21,261	672	3.16
SME lending[1]	**7,110**	**264**	**3.71**	6,904	263	3.80
Unsecured personal lending	**1,172**	**105**	**8.99**	1,216	119	9.76
Liquid assets	**6,007**	**21**	**0.34**	6,001	31	0.51
Other interest-earning assets	**969**	**33**	**3.41**	875	16	1.83
Total average interest-earning assets	**37,697**	**1,075**	**2.85**	36,257	1,101	3.04
Total average non-interest-earning assets	**2,489**			2,759		
Total average assets	**40,186**			39,016		
Interest-bearing liabilities						
Current accounts	**11,032**	**(6)**	**(0.05)**	10,701	(11)	(0.10)
Savings accounts	**7,832**	**(32)**	**(0.41)**	8,034	(63)	(0.78)
Term deposits	**5,190**	**(89)**	**(1.71)**	5,397	(114)	(2.11)
Other wholesale deposits	**8**	**–**	**(0.58)**	70	(1)	(0.95)
Wholesale funding	**6,932**	**(104)**	**(1.51)**	5,140	(95)	(1.85)
Other interest-earning liabilities	**–**	**–**	**–**	303	(11)	(3.54)
Total average interest-bearing liabilities	**30,994**	**(231)**	**(0.75)**	29,645	(295)	(1.00)
Total average non-interest-bearing liabilities	**5,926**			5,905		
Total average liabilities	**36,920**			35,550		
Total average equity attributable to ordinary equity holders	**3,266**			3,466		
Total average liabilities and average equity attributable to ordinary equity holders	**40,186**			39,016		
Net interest income		**844**			806	

(1) Includes loans designated at fair value through profit or loss.

The growth in our customer lending in the year has tempered the impacts of base rate cuts and, together with lower funding costs driven by active management of rates across the savings portfolio, has contributed to an increase in net interest income of £38m (4.7%). As average interest-bearing assets saw a similar increase, Group NIM similarly increased by 1bps to 2.27% (2016: 2.26%).

This was achieved in spite of rate pressures across the board, as a consequence of the base rate reduction in August 2016 and a corresponding fall in LIBOR rates, which together impacted 45% of the Group's customer lending portfolio which is on a variable rate. The effects of these rate reductions combined with competition in the market continued to exert downward pricing pressure on the Group's lending portfolio, with average yields reducing by 19bps to 2.85%. Conversely, average rates on interest-bearing liabilities reduced by 25bps to 0.75% as a result of the rate cuts, a shift in mix in the deposits portfolio and lower wholesale funding costs.

Non-interest income

Non-interest income reduced by £11m (6.0%), largely driven by a reduction in fees and commission income, principally in relation to insurance revenues from off-sale products which have continued to unwind, lower account fees on the Signature current account and lower home insurance profit share due to a higher level of claims.

Impairment losses on credit exposures

The increase in impairment charge, from £39m to £48m, reflects a modest increase in charges taken on our unsecured Retail portfolios together with impairment of a small number of individual SME exposures. The cost of risk has consequently increased by 5bps, but remains low reflecting the continuing benign credit environment.

	2017				2016			
	Retail – secured	**Retail – unsecured**	**SME**	**Total**	Retail – secured	Retail – unsecured	SME	Total
Gross cost of risk	2	266	70	28	4	210	76	29
Specific provision releases and recoveries				(12)				(16)
Fair value loans				(2)				(4)
Net cost of risk (bps)				**14**				9

2. Delivering on our efficiency programme

Operating and administrative expenses	**2017 £m**	2016 £m
Personnel expenses	**248**	280
Depreciation and amortisation expenses	**87**	88
Other operating and administrative expenses	**340**	361
Total underlying operating and administrative expenses	**675**	729
Restructuring expense	**67**	45
Gain on defined benefit pension scheme reforms	**(88)**	–
Separation costs	**8**	11
Conduct charges	**58**	51
Impairment of intangible assets	**–**	45
Total statutory operating and administrative expenses	**720**	881

This year marked the first phase of the Group's three-year efficiency programme, during which we demonstrated our ability to execute on our strategy with clear focus and at pace, and have set a strong foundation to deliver the next phase of savings in 2018.

We continued to improve our operational efficiency during the year through the restructuring and streamlining of our business. As our strategic initiatives gathered pace, the costs required to deliver the programme amounted to £67m in the year. These largely comprised property closure, redundancy and consultancy costs and arose in the main as we implemented our branch closure and voluntary severance programmes. We started to reap the benefits of these actions as the year progressed, and saw our full year underlying costs reduce by £54m (7%) from £729m to £675m, exceeding our FY2017 cost guidance of £690m–£700m. As a result, and combined with the increase in net interest income, our underlying cost to income ratio improved from 74% to 67% for the full year (61% for the second half).

During the year we implemented a new reward programme for colleagues across the business, including a revised pensions proposition. As part of these reforms, the Group closed the defined benefit pension scheme to future accrual on 1 August 2017, for the majority of current employees, with affected employees' future benefits being provided through an enhanced defined contribution scheme. The closure of the Scheme resulted in the recognition of a past service credit of £88m.

On an underlying basis, personnel expenses reduced by £32m in line with headcount, which reduced from 6,718 to 6,040[1]. Other operating and administrative expenses fell by £21m due to the impact of branch closures and tighter cost control across the board.

(1) Based on average core FTEs during the year. Actual core FTEs were 5,739 as at 30 September 2017 (2016: 6,313). Core FTEs exclude legacy conduct FTEs.

Financial performance review

While our priorities have been focused on maximising efficiencies across the business, we have nevertheless sought to maintain investment in our key strategic priorities. During the year we invested heavily in significantly transforming the personal customer experience, through increasing online account opening capability, enhancing service functionality and releasing new applications across all brands. In addition, we continued to invest to ensure we remain compliant with our regulatory obligations, and in enhanced security, to maintain and strengthen the resilience of our operations.

During the year the Group continued to make progress on removing its reliance on National Australia Bank (NAB) for certain processes and systems. Spend in the year in relation to separation costs was £8m (2016: £11m) and the Group is on track to exit all NAB services provided under Transitional Services Agreements by December 2018.

3. Capital optimisation

	Capital change bps	CET1
At 30 September 2016		**12.6%**
Generated	168	
Asset growth	(42)	
Investment spend	(93)	
AT1	(20)	
Core business – net capital generated	13	
Restructuring costs	(31)	
Separation costs	(3)	
IAS 19 pension movement	21	
Conduct costs	(27)	
Other	7	
Total net capital absorbed	(20)	
At 30 September 2017		**12.4%**

The Group continued to maintain its strong capital position throughout the year, delivering a fully loaded total capital ratio of 17.9% and CET1 ratio of 12.4% at September 2017.

Underlying capital generation by the core business post AT1 distribution was 13bps, largely driven by strong underlying profits offset by growth in mortgages and SME lending and investment spend, with RWAs increasing by £649m. After absorbing the net impact of AT1 distributions, pension movements, and exceptional charges such as restructuring charges, separation costs and the Group's proportion of conduct provision charges, the Group's CET1 ratio was 20bps lower at 12.4%.

During the year the Group reassessed the level of provision that was considered appropriate to meet current and future expectations in relation to the mis-selling of PPI policies and concluded that a further charge of £494m was required, incorporating the Group's estimate of the impact of the Regulator's policy statement issued on 2 March 2017 relating to a proposed time bar for complaints in August 2019. It also incorporated a reassessment of the costs of processing cases and the impact of experience adjustments. The Group also raised further provisions of £98m for other non-PPI conduct related matters. In aggregate, only 9.7% of the charge, or £58m, impacts the income statement as a result of the Capped Indemnity, and has absorbed 27bps of capital in the year.

Strengthening our capital base

The Group continually considers opportunities to further strengthen its capital base. The closure of the Scheme to future accrual for the majority of employees, coupled with the impact of the Scheme's triennial valuation, resulted in a reduction in the Scheme deficit (on a trustee funding basis) from £450m to £290m.

In addition, the submission of our waiver application to the PRA requesting permission to apply IRB modelling in the calculation of credit risk RWAs marked a key milestone in our path to IRB accreditation.

The Group is working towards implementation of the requirement to meet the minimum requirements for own funds and eligible liabilities (MREL) on 1 January 2022, and issued £300m of senior bail-in debt in June as the first step to meeting this requirement. The BoE provided the Group's MREL guidance, including transitional arrangements, in late 2016. An interim MREL requirement of 18% of RWAs has been set at the Group level from 1 January 2020 until 31 December 2021. The BoE will advise the Group on its ultimate MREL requirement in 2020. The Group expects to issue further senior debt gradually over the next four years to ensure compliance with MREL in 2022.

Reconciliation of statutory to underlying results

The underlying results presented within this Financial performance review reflect the Group's results prepared on an underlying basis and as presented to the CEO and his Leadership Team and the Board. These exclude certain items that are included in the statutory results, as management believes that these items are not reflective of the underlying business and do not aid meaningful year-on-year comparison. The table below reconciles the statutory results to the underlying basis, and full details on the adjusted items are included in the Glossary on page 252:

2017 income statement

	Statutory results £m	Legacy conduct costs £m	Business restructuring £m	Pension scheme reforms £m	AFS investment disposal £m	Underlying basis £m
Net interest income	**844**	–	–	–	–	**844**
Non-interest income	**192**	–	–	–	(20)	**172**
Total operating income	**1,036**	–	–	–	(20)	**1,016**
Total operating and administrative expenses before impairment losses	**(720)**	58	75	(88)	–	**(675)**
Operating profit before impairment losses	**316**	58	75	(88)	(20)	**341**
Impairment losses on credit exposures(1)	**(48)**	–	–	–	–	**(48)**
Profit on ordinary activities before tax	**268**	58	75	(88)	(20)	**293**
Tax expense	**(86)**	(5)	(11)	31	(2)	**(73)**
Profit attributable to equity holders	**182**	53	64	(57)	(22)	**220**
Financial performance measures						
CIR	**69%**	(5)%	(7)%	8%	2%	**67%**
RoTE	**6.1%**	2.1%	2.3%	(2.1)%	(0.9)%	**7.5%**
Basic EPS	**17.3p**	5.9p	7.3p	(6.5)p	(2.5)p	**21.5p**

(1) Impairment losses on credit exposures relate solely to loans and advances to customers (refer to note 3.6 to the financial statements) and exclude the credit risk adjustments on loans at fair value through profit or loss which are incorporated in the movement in other assets and liabilities at fair value within non-interest income (refer to note 2.3 to the financial statements).

Underlying profit after tax attributable to ordinary equity holders is equal to the underlying profit attributable to equity holders less dividends and distributions (net of tax relief) of £29m (2016: £34m) and amounted to £191m (2016: £143m).

Financial performance review

2016 income statement

	Statutory results £m	Legacy conduct costs £m	Business restruc-turing £m	Intangibles impairment £m	AFS investment disposal £m	Deferred tax asset write-off £m	Underlying basis £m
Net interest income	806	–	–	–	–	–	806
Non-interest income	191	–	(1)	–	(7)	–	183
Total operating income	997	–	(1)	–	(7)	–	989
Total operating and administrative expenses before impairment losses	(881)	51	56	45	–	–	(729)
Operating profit before impairment losses	116	51	55	45	(7)	–	260
Impairment losses on credit exposures(1)	(39)	–	–	–	–	–	(39)
Profit on ordinary activities before tax	77	51	55	45	(7)	–	221
Tax expense	(241)	(5)	(10)	(9)	1	220	(44)
(Loss)/profit attributable to equity holders	(164)	46	45	36	(6)	220	177
Financial performance measures							
CIR	88%	(5)%	(5)%	(5)%	1%	–	74%
RoTE	(7.2)%	1.7%	1.6%	1.3%	(0.2)%	8.0%	5.2%
Basic EPS	(22.5)p	5.2p	5.2p	4.1p	(0.7)p	24.9p	16.2p

(1) Impairment losses on credit exposures relate solely to loans and advances to customers (refer to note 3.6 to the financial statements) and exclude the credit risk adjustments on loans at fair value through profit or loss which are incorporated in the movement in other assets and liabilities at fair value within non-interest income (refer to note 2.3 to the financial statements).

GOVERNANCE

Chairman's letter

"Strong and effective corporate governance underpins our business."

Dear shareholder,

I am pleased to present our Corporate governance report for 2017, our first full year since IPO.

Your Board firmly believes that strong and effective corporate governance underpins our commitment to delivering a strong customer centric banking proposition in the UK and to generating sustainable returns for shareholders. The Board is focused on ensuring corporate governance is embedded across our business supporting better decision making and accountability.

This report sets out our approach to governance in practice, the work of the Board in 2017 and includes reports from the Board's four principal committees.

Strategy

The Board's role is to focus on the creation of long-term sustainable value for our shareholders. During the year the Board's focus was on supporting the Executive Leadership Team to deliver the Group's strategy. The Board spent considerable time in 2017 exploring the challenges arising from the evolving external economic, political and regulatory environment to ensure the continued effective execution and delivery of our strategic priorities against this backdrop and ongoing competitive success. The Board held several strategy focused sessions which are described on pages 62 and 63 and ensured that appropriate risk monitoring and oversight was taking place with plans in place to mitigate the impact of principal risks as described on page 19 of the Strategic report.

Culture

Our approach to culture and values is led by the Board which sets the tone from the top. The Board is committed to ensuring we continue to build a high performing culture which recognises that our colleagues are integral to our business success. During the year the Board supported the launch of our new Values and Behaviours and Great Leadership framework (described on page 30) which underpin our commitment to deliver the right customer focused outcomes by encouraging colleagues to use their initiative, act with autonomy and to work together.

The Board also spent time hearing about colleague feedback from our annual MyVoice survey which highlighted colleagues' commitment to deliver a strong customer-focused culture.

The importance of a genuinely diverse and inclusive culture where every colleague and customer feels they belong is a core part of our Values and Behaviours. During the year the Board refreshed its diversity commitment to maintain a minimum of 25% female representation on the Board with a target to achieve 33% by 2020. The Board recognises the value in having a membership which reflects diversity in the widest sense and which represents a broad range of social perspectives. While we have not set any diversity target beyond gender we will take opportunities through the natural refreshing of the Board to consider a number of diversity factors, however, it will always be the case that appointments to the Board are based on merit and breadth and depth of skills and experience.

Building stakeholder relationships

Hearing from our stakeholders supports us in delivering our strategy and helps us focus on the things that are important to them. Our stakeholders include our customers, shareholders and colleagues in addition to government, regulatory bodies, our suppliers and wider society. This year the Board adopted a refreshed stakeholder engagement programme to broaden its reach among stakeholder communities and we will further develop this in 2018. During the year the Board, either collectively or individually, undertook site visits, met with customers and representatives from our wider communities and the Board now receives a formal stakeholder update on a regular basis.

We engage with our shareholders through a calendar of meetings and events, including the AGM, and we use webcasting to allow all shareholders the opportunity to join the key meetings throughout the year. The Board is updated regularly on both retail shareholder and institutional investor feedback and my fellow Directors and I very much look forward to having the opportunity to meet with our shareholders at our 2018 AGM.

Board changes

Richard Gregory retired from the Board on 10 January 2017. Clive Adamson became Chair of the Risk Committee in January 2017 on Richard's retirement and Tim Wade became Chair of the Audit Committee in November 2016. The structure, size and composition of the Board and its committees will continue to be kept under review in 2018.

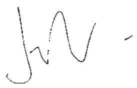
Board effectiveness

An important part of my role as Chairman is to ensure that the Board – both collectively and its individual members – operates effectively. This year the Board undertook its first externally facilitated performance evaluation since becoming a listed company. I am pleased to report that the key conclusion of the evaluation was that the Board and its committees are effective. The process and principal findings are described on pages 68 to 70 of this report. The Board adopts a continuous improvement approach to its effectiveness with a focus on achieving best practice across all aspects of corporate governance. The Board will therefore keep its corporate governance arrangements under review through 2018 to ensure they adapt to changes in regulation or legislation and remain effective.

Looking ahead

The Board remains focused on executing the agreed strategy and delivering an exceptional customer experience and sustainable returns to our shareholders and will continue to strengthen the effectiveness of the corporate governance framework to support this.

Finally, I would like to thank the Board and our colleagues for their support and commitment throughout 2017.



Jim Pettigrew
Chairman

Board of Directors

Left to right

Clive Adamson
Independent Non-Executive Director

Dr Teresa Robson-Capps
Independent Non-Executive Director

Paul Coby
Independent Non-Executive Director

David Duffy
Executive Director and
Chief Executive Officer

Jim Pettigrew
Chairman

Adrian Grace
Independent Non-Executive Director

Tim Wade
Independent Non-Executive Director

Fiona MacLeod
Independent Non-Executive Director

Debbie Crosbie
Executive Director and
Chief Operating Officer

David Browne
Independent Non-Executive Director

Ian Smith
Executive Director and
Chief Financial Officer

David Bennett
Deputy Chairman and Senior
Independent Non-Executive Director

Board of Directors

Board roles and responsibilities

The Board has agreed a clear division of responsibilities between the Chairman and Chief Executive Officer. The Chairman's priority is to lead the Board and ensure its effectiveness and the Chief Executive Officer's priority is to manage the day-to-day running of the Group's business. The roles of the Chairman, Chief Executive Officer and other Directors are clearly defined so that no single individual has unrestricted powers of decision. Their key responsibilities are set out below.

Position	Name	Roles and responsibilities
Chairman	**Jim Pettigrew**	Leading the Board and its effectiveness by organising its business and setting its agendas, ensuring that the Board as a whole plays a full and constructive part, being forward looking, and primarily focused on strategy, performance and key value creation issues. Promoting the highest standards of corporate governance and ensuring that the Board receives accurate, timely and high quality supporting information. Ensuring properly constructed Board induction, evaluation and development, and effective communications with the Group's shareholders.
Deputy Chairman and Senior Independent Non-Executive Director	**David Bennett**	**Deputy Chairman** – Supporting the Chairman, and when required, acting as the Chairman's delegate and ensuring continuity of Chairmanship, supporting the Chairman in representing the Board and acting as spokesperson. Being available to the Board for consultation and advising and representing the Group's interests at official enquiries and with review bodies. **Senior Independent Non-Executive Director** – Providing a sounding board for the Chairman and serving as a trusted intermediary between the Chairman and the other Directors when necessary, and ensuring that the views of all Directors are conveyed to the Chairman. Being available to shareholders in the event of any matters which cannot be resolved through the normal channels of communication with the Chairman or the Executive Directors. Maintaining contact as required with major shareholders to understand their issues and concerns, maintaining stability and cohesion within the Board particularly during periods of stress. Meeting with the Non-Executive Directors without the Chairman present at least annually and leading the Non-Executive Directors in the ongoing monitoring and annual evaluation of the Chairman.
Chief Executive Officer	**David Duffy**	Leading the day-to-day management of the Group's business ensuring its effective running. Leading the Executive Leadership Team, being responsible for developing, coordinating and proposing to the Board all activities to implement the Group's strategy and its overall objectives in accordance with the Group's risk appetite, and maintaining a close working relationship with the Chairman.
Independent Non-Executive Directors	**Clive Adamson, David Bennett, David Browne, Paul Coby, Adrian Grace, Fiona MacLeod, Dr Teresa Robson-Capps and Tim Wade**	Bringing an external perspective, knowledge, experience and insight from other industries and applying sound judgement and objectivity to the business of the Board. Developing and setting the Group's strategy and monitoring its implementation, reviewing the RMF, and supporting and constructively challenging Executive Directors. Satisfying themselves on the integrity of financial information, considering and taking account of the views and concerns of the Company's shareholders and other stakeholders. Having a principal role in appointing and, where necessary, removing Executive Directors. Devising appropriate succession plans and approving appropriate levels of remuneration for the Executive Directors following recommendations from the Remuneration Committee.

Key: Re Remuneration Committee
Ri Risk Committee
Au Audit Committee
Go Governance and Nomination Committee
● Chair

Jim Pettigrew
Chairman
Go Re

Joined the Group
September 2012 and became Chairman in 2014

Key areas of expertise
Finance, Governance, M&A

Skills and experience
Jim has over 30 years' experience in business and finance gained from executive and senior positions principally within financial services. Jim was formerly Chief Executive Officer at CMC Markets PLC, Chief Operating Officer at Ashmore Group PLC, Group Finance Director at ICAP PLC and Deputy Group Finance Director and Group Treasurer at Sedgwick Group PLC. He is a chartered accountant and has extensive Non-Executive Director experience in a listed environment. He was previously Non-Executive Director at Aberdeen Asset Management PLC, Non-Executive Director at AON UK Limited and Non-Executive Director at Hermes Fund Managers Limited. He is the immediate past President of the Institute of Chartered Accountants of Scotland. His breadth of experience, credibility with key stakeholders and strong leadership qualities make him an effective Chairman.

Key external appointments
Chairman of The Edinburgh Investment Trust PLC; Senior Independent Non-Executive Director of Crest Nicholson Holdings PLC; Senior Independent Non-Executive Director of Rathbone Brothers Plc and Rathbone Investment Management Limited (part of the Rathbone Brothers Plc group); Chairman of RBC Europe Limited, BlueBay Asset Management (Services) Ltd and BlueBay Asset Management LLP (members of the RBC Group); Chairman of Scottish Financial Enterprise; and Co-Chair of the Financial Services Advisory Board.

David Bennett
Deputy Chairman and Senior Independent Non-Executive Director
Au Go Re Ri

Joined the Group
October 2015

Key areas of expertise
Finance, M&A, Retail Banking

Skills and experience
David has significant experience in retail banking gained from a career spanning more than 30 years and including executive and senior roles in both the UK and internationally. David was Group Finance Director of Alliance & Leicester plc for six years before becoming its Group Chief Executive. Following the acquisition of Alliance & Leicester plc by Banco Santander he was appointed Executive Director on the Board of Abbey National plc. His in-depth experience of retail banking and involvement in organisational, operational and structural change is invaluable as we execute our Group strategy. He has significant Non-Executive Director experience in a listed environment which has included being a Non-Executive Director of Bank of Ireland (UK) PLC, Non-Executive Director of easyJet plc, and Non-Executive Director of CMC Markets PLC.

Key external appointments
Non-Executive Director of Ashmore Group plc, PayPal (Europe) S.a.r.l et Cie, S.C.A; Chairman of Homeserve Membership Ltd.; and Non-Executive Director of various companies within the Together Financial Services Limited group.

Board of Directors

Non-Executive Directors

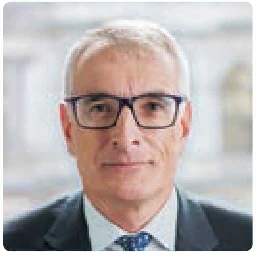
Clive Adamson
Independent Non-Executive Director
Au Ri

Joined the Group
July 2016

Key areas of expertise
Governance, Financial Services Regulation, Risk

Skills and experience
Clive has considerable experience of UK and global economic, banking and regulatory matters gained from an extensive career in banking and financial services regulation. He held senior executive and advisory positions with the FCA, the former Financial Services Authority and the BoE. He was previously Head of Supervision and an Executive Director of the Board of the FCA until May 2015. His strong understanding of the UK and global banking industry and related risks is invaluable to the Board.

Key external appointments
Chairman at JP Morgan International Bank Limited; Non-Executive Director of The Prudential Assurance Company Limited; Non-Executive Director at Ashmore Group plc; and senior adviser at McKinsey & Company.



David Browne
Independent Non-Executive Director
Au Re Ri

Joined the Group
May 2012

Key areas of expertise
Finance, Risk

Skills and experience
David has over 30 years' experience in debt capital markets, treasury and investor relations. He was previously Head of Group Funding and External Relations at Man Group PLC and spent a significant part of his career at JP Morgan where he held the positions of Assistant Vice President, Vice President and Managing Director. David is a founding partner of Pinnacle Partners Limited, a treasury consulting firm.

Key external appointments
Director of Pinnacle Partners Limited and Trustee and Director of London Youth Rowing Limited.

Paul Coby
Independent Non-Executive Director
Ri

Joined the Group
June 2016

Key areas of expertise
Information Technology, Strategy

Skills and experience
Paul is an accomplished IT professional with significant e-commerce, international and technology experience. In particular his understanding of how technology has changed consumer behaviour, how advances in digital technology can impact customer outcomes and his appreciation of the end-to-end customer journey in a strategic omni-channel context is invaluable to the Group as we develop new products and digital capability. Paul is the John Lewis Partnership's Chief Information Officer (CIO), responsible for leading and coordinating IT across the John Lewis, Waitrose and JLP Group. Prior to his CIO role, Paul was IT Director at John Lewis and previously CIO at British Airways for 10 years. Paul's previous roles include Non-Executive Chairman of the Societe Internationale de Telecommunications Aeronautiques (SITA), the global provider of systems, solutions and telecommunications to the air transport industry, Non-Executive Director at Pets at Home Group PLC and at P&O Ferries Limited, Chairman of the eSkills UK CIO Board and Chairman of the oneworld CIO Group which coordinated IT links across the 10 airline oneworld Alliance partners.

Key external appointment
CIO of the John Lewis Partnership.

Key: Re Remuneration Committee
Ri Risk Committee
Au Audit Committee
Go Governance and Nomination Committee
● Chair

Adrian Grace
Independent Non-Executive Director
Re (Chair)

Joined the Group
December 2014

Key areas of expertise
Finance, Financial Services Regulation, Strategy

Skills and experience
Adrian has extensive financial, business leadership and general management experience gained from a career which has spanned a range of consumer and commercial financial services sectors and involved a variety of senior roles. Adrian's experience of designing and implementing substantial change programmes and delivering transformational growth through simple customer focused visions and plans is aligned to the Group's strategy. Having started his career with the Leeds Permanent Building Society and then Mercantile Credit, Adrian joined GE Capital where he spent time in the UK, Asia, and the Americas. He became Managing Director of the Small Business Division at Sage Group plc. He was Chief Executive at Barclays Insurance and Managing Director of Commercial Banking within the Corporate Division of HBOS. Since 2011 Adrian has been Chief Executive Officer at Aegon UK having joined Aegon in 2009 as Group Business Development Director. He was previously on the boards of the Association of British Insurers and Scottish Financial Enterprise.

Key external appointments
Director of various companies within the Aegon Group and a member of the FCA Practitioner Panel representing the life and pensions sector.

Fiona MacLeod
Independent Non-Executive Director
Go Ri

Joined the Group
September 2016

Key areas of expertise
M&A, Marketing, Strategy

Skills and experience
Fiona has over 28 years' international business experience in leading complex, large-scale business transformation and in managing the commercial, human resources and cultural aspects of change programmes. A substantial part of her career was at BP Group plc where she held various executive positions including latterly the role of President Retail, USA & Latin America. Fiona's deep experience of operational business leadership, of transforming businesses and in understanding and managing the organisational design and people impacts of business change are invaluable to the Group as we focus on building a high performing, customer centric organisation and continue our cultural transformation. Fiona's experience of running retail businesses serving millions of customers per day is also of particular relevance. Fiona was formerly Senior Independent Non-Executive Director of SThree plc.

Key external appointment
Non-Executive Director of Denholm Oilfield Services Limited.

Dr Teresa Robson-Capps
Independent Non-Executive Director
Au

Joined the Group
October 2014

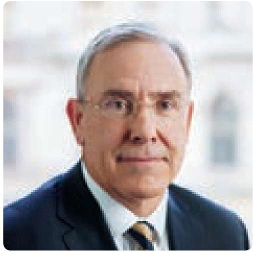
Key areas of expertise
Finance, Strategy

Skills and experience
Teresa has extensive financial, customer service and general management experience from across a range of industries including telecommunications, financial services and retail. She is a chartered management accountant and has a Doctorate in Accounting and Management Control. Teresa has a breadth of experience gained from executive leadership roles with BT Mobile, Sears plc, Eagle Star/Zurich Financial Services, Cable & Wireless, Reality & Accenture. She joined HSBC Group in 2006 and from 2010 was Deputy Head, Direct Bank & First Direct. Teresa also has strong board experience gained from her previous roles as Chairman of ACS Clothing Group Limited and Non-Executive Director of Broker Network Holdings Limited, Paymentshield Group Holdings Limited, PowerPlace Insurance Services Limited and Towergate Insurance Limited.

Key external appointments
Non-Executive Director of Hastings Group Holdings PLC and Non-Executive Director of Yorkshire Water Services Limited.

Board of Directors

Executive Directors



Tim Wade
Independent Non-Executive Director
Au Ri

Joined the Group
September 2016

Key areas of expertise
Finance, M&A, Retail Banking, Risk

Skills and experience
Tim has over 20 years' senior experience in retail financial services, including retail banking in both the UK and internationally. An Australian national, he is an experienced Chief Financial Officer, a chartered accountant and a Fellow of the Institute of Chartered Accountants of Australia. Tim was Managing Director at AMP International, responsible for AMP Bank and the Virgin Direct (now Virgin Money) joint venture. He began his career at Arthur Andersen working in Melbourne and Singapore, and in 1994 he joined Colonial Limited, the mutual financial services group, as Chief Taxation Counsel. He became Group Chief Financial Officer in 1997 and Executive Director of State Bank of NSW. Tim subsequently oversaw the IPO of Colonial and was involved in Colonial's subsequent acquisition by Commonwealth Bank – at the time the largest acquisition in Australian corporate history. His previous Non-Executive Director board experience includes Friends Life Group Limited and Monitise plc.

Key external appointments
Chairman at Macquarie Bank International Limited; Non-Executive Director of companies within the Chubb European Group Limited and The Access Bank UK Limited groups; and Non-Executive Director of The Coeliac UK Trading Company Limited.

David Duffy
Executive Director and Chief Executive Officer

Joined the Group
June 2015

Key areas of expertise
Banking, Finance M&A, Strategy

Skills and experience
David has significant international finance and banking experience gained from a career spanning almost three decades. David's proven ability to build and transform businesses and lead strong management teams brings significant value to all of the Group's stakeholders. Prior to joining the Group, David was Chief Executive Officer at Allied Irish Banks plc, one of the largest retail and commercial banks in Ireland. He was a former Chief Executive Officer of Standard Bank International with responsibility for operations in the UK, Europe, Latin America and Asia. He was also previously Head of Global Wholesale Banking Network with ING Group and President and Chief Executive Officer of the ING wholesale franchises in the United States and Latin America. David is a past President of the Banking and Payments Federation of Ireland and a past Director of the European Banking Federation. David's broad-based skills, leadership, energy and strategic vision are invaluable to the Group as it continues its strategic journey and cultural transformation.

Key external appointments
Non-Executive Director of NewTA Limited trading as UK Finance, the industry body representing leading firms providing finance, banking, markets and payments-related services in or from the UK.

Debbie Crosbie
Executive Director and Chief Operating Officer

Joined the Group
June 1997

Key areas of expertise
Information Technology, Retail Banking, Strategy, Operations

Skills and experience
Debbie has broad experience and knowledge gained over 20 years in the banking sector, particularly around information technology, complex project delivery, material outsourcing and strategy and planning. She has significant experience at a senior management level and is a strong advocate for customers and improving the customer experience by driving a change and transformation journey which has the customer as its core focus. Since joining the Group in 1997 Debbie has held a variety of positions including Head of Technology Governance, Head of Strategic Projects and Head of the Group's Development Centre. She was Chief Information Officer from 2008 to 2011, she became Operations and IT Director in 2011, was appointed Executive Director in 2014 and Chief Operating Officer in 2015. Debbie was Acting Chief Executive Officer from February 2015 to June 2015 and during this period led the preparation for the Group's demerger and IPO and was part of the management team which completed the transaction. She was previously a Non-Executive Director of the Scottish Court Service and is a Fellow of the Chartered Institute of Bankers.

Key external appointments
Vice-Chair of the Board of CBI Scotland and member of the Board of Glasgow Economic Leadership.

Company Secretary

Ian Smith
Executive Director and Chief Financial Officer

Joined the Group
November 2014

Key areas of expertise
Banking, Finance M&A, Strategy

Skills and experience
Ian has considerable experience in finance, audit and advising on bank strategy from a corporate transaction perspective gained from a career spanning more than 20 years. He has held senior finance roles in HBOS plc and Lloyds Banking Group plc and has provided advice to boards considering significant corporate transactions. He joined the Group in November 2014 from Deloitte LLP where he was a partner specialising in financial services.

Key external appointment
Non-Executive Director of 67 Pall Mall Limited.

Lorna McMillan
Company Secretary

Joined the Group
September 1994

Skills and experience
Lorna has responsibility for supporting the Chairman and the Board, as well as leading the delivery of shareholder services. She has over 20 years' experience gained from various roles in the Group across retail and business banking, wholesale banking, risk management and legal and governance areas. Lorna was appointed Company Secretary in October 2014 and led the corporate governance preparation for the Group's demerger and IPO during 2016.

Executive Leadership Team

The Executive Leadership Team operates under the direction and authority of the Chief Executive Officer and is responsible for supporting him in all aspects of his role. Each member has been assigned individual accountability for delivery of the overall strategy and the principal risks outlined in the Strategic report. They also have accountability for delivering against the initiatives designed to underpin our strategic priorities of capital optimisation, improving efficiency and driving sustainable customer growth.

David Duffy
Executive Director and
Chief Executive Officer

Debbie Crosbie
Executive Director and
Chief Operating Officer

Ian Smith
Executive Director and
Chief Financial Officer

Enda Johnson
Group Corporate Development Director

Joined the Group
September 2015

Skills and experience
Enda has responsibility for the Group's strategic development, corporate affairs and investor relations. He has over 14 years' experience in financial services and before joining the Group he worked at Allied Irish Banks plc as Head of Corporate Affairs and Strategy and was a member of the Executive Leadership Team. Enda previously worked in the banking unit of the Irish National Treasury Management Agency (NTMA), where he worked on the recapitalisation and restructure of Irish banks following the global financial crisis. Before the NTMA he worked internationally with Merrill Lynch in its investment banking and capital markets divisions.

Kate Guthrie
Group Human Resources Director

Joined the Group
January 2016

Skills and experience
Kate has responsibility for human resources and internal communications, focusing on talent and leadership development, colleague engagement and culture. She has over 30 years' domestic and international HR experience, having worked in six different blue chip organisations in four industrial sectors, including financial services. Prior to joining the Group, Kate spent a decade with Lloyds Banking Group plc where she was latterly the HR Director responsible for leading the group culture, capability and engagement.

Fergus Murphy
Group Customer Value Director

Joined the Group
January 2016

Skills and experience
Fergus has responsibility for the delivery of the Group's product suite, including pricing, propositions, customer liability strategy, capital allocation and product development. He has over 20 years' experience in financial services gained from Allied Irish Banks plc, Rabobank Group, BNP Paribas Group and KBC Bank Ireland plc. At Allied Irish Banks plc, he held roles including Director of Products and Capital Markets and latterly, Director of Corporate and Institutional Banking. During his tenure with AIB, he redesigned the customer product offering to better meet customers' needs and led the rebuilding of AIB's operating model. He is a former CEO of Rabobank Asia and was responsible for the overall strategy and performance of Rabobank in the region.

Gavin Opperman
Group Customer Banking Director

Joined the Group
November 2015

Skills and experience
Gavin has responsibility for developing and leading the Group's customer banking strategy. He is a senior executive with over 30 years of banking experience in leadership, risk, operations and customer facing roles across retail, commercial, corporate and investment banking and within a wide range of geographies. Gavin has experience of different levels of complexity, market and team dynamics. He was previously Regional Head of Consumer Banking for Standard Chartered plc, based in China, and prior to that held a number of senior positions in a career spanning 20 years with Barclays Group including being Chief Executive Officer of Absa Bank Limited, a subsidiary of Barclay's Africa Group.

Helen Page
Group Innovation and Marketing Director

Joined the Group
December 2012

Skills and experience
Helen has responsibility for the Group's marketing and customer innovation strategy. She has over 25 years' experience in marketing, product and customer innovation and brand strategy, principally within the financial services industry. Helen spent eight years at Royal Bank of Scotland Group plc in a number of roles and was latterly Managing Director for Marketing and Innovation, with responsibility for all UK brands across the Retail, Commercial and Corporate divisions. Helen was previously Head of Brand Marketing at Argos (part of the Home Retail Group plc) and prior to Argos, held a number of product and marketing roles at Abbey National plc (now Santander) where she became Head of Marketing.

James Peirson
Group General Counsel

Joined the Group
November 2014

Skills and experience
James has responsibility for leading the Group's legal and governance strategy. He joined NAB in 2005, where he led the NAB London Branch legal team. James also held roles supporting NAB and Clydesdale Bank PLC Treasury activities as part of NAB's capital and funding legal team in both Melbourne and London. Prior to joining NAB he worked in private legal practice at Hogan Lovells International LLP.

Mark Thundercliffe
Group Chief Risk Officer

Joined the Group
September 2016

Skills and experience
Mark is responsible for the management of significant risks and opportunities across the Group, including strategic, reputational, operational, financial, credit and regulatory. He has over 29 years' international retail and business banking experience. Mark was previously Chief Risk Officer at HSBC, responsible for management and oversight of risk for HSBC's Retail Banking and Wealth Management business across the UK, Europe, the Middle East and Africa. Mark has also held a number of senior international positions in financial services firms up to Chief Executive Officer and Executive Director level.

Corporate governance report

Statement of compliance

The Annual Report and Accounts for the year ended 30 September 2017 has been prepared in accordance with the UK Corporate Governance Code 2016 ('Code') which was issued in April 2016. The Code is publicly available at www.frc.org.uk. The Board confirms that the Company has applied the main principles and complied with the provisions of the Code.

The Group has also adopted the British Bankers' Association Code for Financial Reporting Disclosure, which is available at www.bba.org.uk, and the financial statements have been prepared in compliance with its principles.

Leadership

The Board is the principal decision-making body of the Group and is collectively responsible to shareholders for promoting the long-term success of the Company.

The Board's role is to provide leadership to the business as a whole within a framework of prudent and effective controls which enable risk to be assessed and managed. It sets strategy and oversees its delivery and establishes its culture, values, ethics and standards. It sets the Group's risk appetite, monitors operational and financial performance and reporting, ensures the Group is adequately resourced and has effective controls and remuneration policies, and that there are appropriate succession planning arrangements.

In order to assist the Board in carrying out its functions and to ensure that there is independent oversight of financial reporting, internal controls, risk management, governance and remuneration matters, the Board delegates certain clearly defined responsibilities to its four principal committees. Reports from the Governance and Nomination Committee, the Audit Committee and the Risk Committee are contained in this report. A report from the Remuneration Committee is included in the Directors' remuneration report.

As required, the Board may also establish special purpose Committees to assist the Board in the oversight of specific areas that may require more detailed attention. The Board established a special purpose IRB and Credit IFRS 9 Committee to oversee the transition from a standardised approach to calculating capital requirements for credit risk to an IRB approach, and the implementation of the credit element of the IFRS 9 accounting standard which will be effective for the Group in the reporting period beginning 1 October 2018. During the year, the activities of the Committee included overseeing the submission of the Group's application to the PRA for IRB accreditation and system changes covering critical delivery of IFRS 9 and stress testing to embed an advanced Credit Risk Management capability.

The chart on page 132 of the Risk report illustrates the Board and management structure as at 30 September 2017.

Matters reserved to the Board and delegated authorities

In order to retain control of key decisions and ensure there is a clear division of responsibilities at the head of the Company, the Board has identified certain 'reserved matters' that only it can approve. Other matters, responsibilities and authorities have been delegated to its committees and the Chief Executive Officer.

The matters reserved to the Board are set out in the Charter for the Board and this, as well as the Charters for each principal Board committee, is available to view on the Company's website (www.cybg.com/about-us/corporate-governance). The Charters are also available on request from the Company Secretary at the Company's registered office. During the year the Board and each of the Board committees reviewed its Charter.

The authorities delegated by the Board to the Chief Executive Officer are set out in the Delegation of Authority Framework.

Board and strategic planning

During the year the Board's focus was on supporting executive management to deliver the Group's strategy. The strategy communicated at our Capital Markets Day in September 2016 is unchanged and the Board's discussions throughout the year focused on overseeing delivery of the strategic priorities of sustainable customer growth, improved efficiency and capital optimisation.

A key objective during the year was to deepen and embed the strategy to align with the evolving competitive, economic and regulatory environment with a focus on execution and de-risking delivery. As part of this process the Board was engaged in three in-depth strategic review and planning sessions with the management team and received regular updates on the initiatives under way to build core capabilities and support strategic delivery.

During the first half of the year the areas of focus for the Board included discussing the impacts of the challenging external environment including the political uncertainty arising from the UK's exit from the European Union and the potential for a second Scottish Independence Referendum. It was also updated on progress in transforming the distribution model and evolving channel capabilities, developments in building digital capability and improving customer service and the banking experience. Potential inorganic strategic opportunities, including Fintech partnerships, to achieve scale and asset growth and to capitalise on existing operational leverage were considered, as was performance against the target cost structure and our structured approach to cost reduction. The Board also monitored progress in delivering the refreshed people strategy, the simplification of the governance framework and on the cultural transformation to enable strategic delivery.

In the second half of the year the Board continued its review and discussion of strategic performance in the context of the economic, political and competitive environment. In addition the Board was deeply engaged in discussing the evolving UK banking landscape and the Group's future participation choices. The Board also participated in an evaluation of the underpinning fundamentals of the strategy in the context of the market environment and considered different growth alternatives to increase value for investors. The Board also held a challenge session on potential inorganic opportunities and alignment with the Group's strategic priorities and broader market dynamics. Each of these areas of strategic focus was informed by external insights and input which strengthened the debate.

The Board also spent time considering updates from the Board committees which informed the Group's strategy.

The output of the review and planning sessions was a refreshed strategic and financial plan to be approved by the Board along with a revised RAS. During the process the Board considered very carefully the issues informing the strategic and financial plan to ensure that the business will be able to continue to drive sustained performance for the benefit of all stakeholders, to be monitored by the Board through a set of key performance indicators.

Board attendance
The core activities of the Board were carried out in 11 scheduled meetings of the Board. Two additional *ad hoc* meetings of the Board were arranged when matters required to be brought to the Board's attention or when decisions were required outside scheduled meetings.

The attendance of Directors at scheduled Board meetings, which they were eligible to attend, and the number of meetings attended in the year ended 30 September 2017 is shown in the following table.

Director	Number of scheduled Board meetings eligible to attend	Number of scheduled Board meetings attended
Chairman		
Jim Pettigrew	11	11
Non-Executive Directors		
Clive Adamson	11	11
David Bennett	11	11
David Browne	11	11
Paul Coby	11	11
Adrian Grace	11	11
Richard Gregory [(1)]	3	3
Fiona MacLeod	11	10[(2)]
Dr Teresa Robson-Capps	11	11
Tim Wade	11	10[(2)]
Executive Directors		
David Duffy	11	11
Debbie Crosbie	11	11
Ian Smith	11	11

(1) Richard Gregory retired from the Board on 10 January 2017.
(2) Unable to attend the meeting due to a prior business commitment.

Board activity

Setting the Board agenda
There is a comprehensive and continuous process in place for ensuring the Board has full and timely access to all relevant information in an insightful format.

The Chairman is responsible for setting the Board agenda and is assisted by the Chief Executive Officer and Company Secretary. The Board agenda is structured to ensure it covers each of the three strategic priorities and underpinning core capabilities to support strategy engagement and the challenge and debate on performance and delivery at Board level. The Chairman reviews the time allocation with the Company Secretary to ensure adequate time is allowed to discuss material matters. The Company Secretary keeps the Chairman informed of any agenda items requested by Non-Executive Directors. In order to carry out its work, a yearly planner is prepared by the Company Secretary to map out the flow of key items of business to the Board and to ensure that sufficient time at the meeting is provided for debate and challenge. Directors are sent papers for Board meetings up to five working days in advance of the meeting (whether they are able to attend or not) in order that they may have the time to consider the proposals put forward, seek clarification or, if required, request further information.

Corporate governance report

At each main meeting the Board discusses:

- the Chief Executive Officer's report – including performance against the strategic plan, key developments in the external environment, the economic outlook and impacts for the Group, business performance, product and proposition developments, stakeholder engagement and investor relations matters, material regulatory issues, and key matters relating to people, cultural and organisational transformation and capability;
- the Chief Financial Officer's report – including performance against the financial plan, key performance indicators, capital, liquidity and funding matters;
- the Chief Operating Officer's report – including delivery against customer service commitments, operational efficiency, IT service and security, and the status of major investment programmes; and
- the Group Chief Risk Officer's report – including the risk profile and risk categorisation and principal and emerging risks, key risk issues and RAS performance and trends.

How Board meetings are run

Prior to the start of a scheduled Board meeting, the Senior Independent Non-Executive Director meets with Non-Executive Directors (excluding the Chairman and then with the Chairman present) to discuss matters of concern or focus. Both the Chairman and the Senior Independent Non-Executive Director report to the Board on issues to be brought to the Board's attention at the commencement of each meeting and these are recorded in the Board minutes. The Chairman ensures Board meetings are structured to facilitate open discussion, debate and challenge with dissenting views of Directors being freely expressed and discussed within the decision-making process, leading to Board decisions being made on a sound and well-informed basis.

All Directors are expected to attend each Board meeting and committee meeting for which they are members, save for in exceptional circumstances. Reasons for non-attendance are generally unavoidable conflicts with prior business commitments, personal reasons or illness, and non-attendance must always be notified in advance to the Chairman, relevant committee Chair or the Company Secretary. In the rare event of a Director being unable to attend a meeting, he/she has the opportunity to discuss with, or notify, the Chairman, relevant committee Chair or the Company Secretary of any matters he/she wishes to raise and to follow up the decisions made at the meeting. The Chairman and Company Secretary, together with members of the Executive Leadership Team, are available to discuss issues relating to meetings or other matters with Directors.

During the year, the Chairman held a number of meetings with Non-Executive Directors without the Executive Directors being present.

Board committees

The Board delegates certain clearly defined responsibilities to its four principal Board committees, namely: the Governance and Nomination Committee; the Audit Committee; the Risk Committee; and the Remuneration Committee.

The committee Chairs report to the Board on the activities of the committees at each Board meeting. Each principal committee membership comprises Non-Executive Directors only and is chaired by an experienced Chair. Committee memberships are spread between the Non-Executive Directors, drawing on each of their relevant skills and experience. Only members of the committees are entitled to attend their meetings, but others may attend at the discretion of the committee Chair.

Board focus in 2017

The significant matters addressed by the Board during the financial year ended 30 September 2017 and in evaluating the Company's 2017 Annual Report and Accounts are described below.

Regular agenda items

Chairman's report
Senior Independent Non-Executive Director's report
Chief Executive Officer's report
Chief Financial Officer's report
Chief Operating Officer's report
Group Chief Risk Officer's report
Reports from committee Chairs
Board administration and governance

Strategy and financial

Monitored delivery of the Group's strategic plan and performance of the financial plan including the impacts of changes in the economic, political, regulatory and competitive environment

Development and monitoring of key performance indicators

Approved the Company's Annual Report and Accounts, Interim Financial Report, related announcements and supporting analyst presentations

Reviewed the capital, funding and liquidity frameworks, and approved the Capital Plan and the Funding Plan

Approved the Internal Liquidity Adequacy Assessment Process (ILAAP)

Approved Internal Capital Adequacy Assessment Process (ICAAP) scenarios

Approved a Debt Issuance programme and a Tier 1 capital instrument distribution

Approved the Group tax strategy

Approved the submission and subsequent withdrawal of a preliminary non-binding proposal to the Royal Bank of Scotland Group PLC in relation to its Williams & Glynn operations

Approved major capital and investment expenditure

Approved and recommended to shareholders the reappointment of the External Auditor

Approved and recommended to shareholders a final dividend for FY2017

Customer focus

Monitored progress with the digitally enabled omni-channel strategy and the customer journey programme

Reviewed progress of the PPI complaints remediation programme

Monitored Conduct Framework progress and outcomes

Received updates on the actions to address customer vulnerability in financial services

Risk management

Approved and received interim updates on the RAS

Approved the enhanced RMF

Agreed and monitored principal and emerging risks

Reviewed internal control systems

Monitored the IRB and Credit IFRS 9 programme and related matters and approved the submission of the Group's IRB application to the PRA

Considered the outcome of an independent review of PPI control frameworks

Approved the Scheme triennial valuation

Approved Group insurance renewal including a Directors and Officers Liability Insurance Policy

Governance

Approved Senior Independent Non-Executive Director and Board committee appointments

Considered the Board and committee structure, size and composition

Approved the Board and committee charters and division of roles of Chairman and Chief Executive Officer

Approved revisions to the External Directorship Policy Standard

Considered the outputs of the external Board Effectiveness Review and agreed actions to be taken

Approved Non-Executive Director fees

Considered Non-Executive Directors' independence

Reviewed the Register of Directors' Conflicts of Interests

Recommended the re-election by shareholders of Directors at the Annual General Meeting

Regulatory

Approved the Group's recovery plan in the event of a significant deterioration in financial stability

Approved the Pillar 3 Disclosures Report

Reviewed compliance with the new Financial Services Compensation Scheme rules

Received a presentation from the PRA on its Periodic Summary Meeting letter

Considered the PRA's annual assessment of the Conduct Indemnity Fund

Kept informed of regulatory changes

Stakeholders

Agreed and received updates on the stakeholder engagement strategy

Received investor relations updates

Approved results announcements

Received briefings on AGM arrangements

Received briefings on shareholder engagement feedback

Approved the small holding sale facility

People, culture and values

Approved a revised Board inclusion and diversity policy statement

Reviewed succession planning and talent management

Reviewed the results from the 'MyVoice' colleague engagement survey

Approved the outcomes of a strategic reward review, which included pension scheme reforms

Reviewed health and safety updates

Approved the Modern Slavery Act statement

Supported the launch of the new Values and Behaviours and Great Leadership framework

Corporate governance report

Deep dives and Board briefings

The Board has a programme of 'deep dive' sessions focusing on thematic updates aligned to the strategic priorities and core capabilities which give Directors the opportunity to engage with management in a more informal way outside of the structure of a Board meeting to gain insight on topics of interest or focus for the Board. Additionally the Board receives briefings on regulatory and corporate governance change. Listed below are the 'deep dive' topics and Board briefings during the year.

Deep dives

Mortgage market and performance
UK banking landscape and strategic update
Small and medium business segments
Brand
Customer journey programme
Current account market

Board briefings

IRB and IFRS 9
Credit models
Anti-bribery and corruption risk

Stakeholder engagement

Directors, either collectively or individually, undertook site visits and met with customers and representatives from our wider communities. Site visits provide an opportunity to get closer to business operations, current issues and customer service in an operational environment. This provides insight into customer experiences and allows Directors to connect with management and colleagues alike. In April 2017, the Board visited Studio B, our new innovation lab in London which has been designed to inspire a new way of thinking that could shape the future of banking. It also visited the new flagship Customer Banking Centre in Edinburgh in July 2017, which has a modern design and facilities to reflect the new way in which the Group interacts with and serves its customers. In June, Directors met the winners of our annual Spirit of the Community Awards which are described in more detail on page 32.

Effectiveness

Board size and composition

The Board comprises a Non-Executive Chairman, three Executive Directors and eight independent Non-Executive Directors. The size of the Board is considered to be suitable in the context of a highly complex commercial and regulatory operating environment with the appropriate combination of Executive and Non-Executive Directors such that no individual or small group of individuals can dominate the Board's decision making. The names of the Directors together with their full biographical details, including the skills and experience they each bring to the Board, are on pages 55 to 59. Further details on the composition of the Board and independence of the Non-Executive Directors are provided in the Governance and Nomination Committee report on page 77.

Time commitments

The Board recognises that it is vital that Directors should be able to dedicate sufficient time to the Company to effectively discharge their responsibilities. The time commitment is considered by the Board on appointment and kept under review. The letters of appointment of the Chairman and of each of the Non-Executive Directors set out the minimum time commitment for their roles and that they undertake to allocate sufficient time to the Company as is necessary for the effective discharge of their duties.

The Chairman is expected to commit at least 60 days per year on Company business, the Deputy Chairman 45 days per year and Non-Executive Directors at least 35 days. Time commitment increases for other Board roles such as the Senior Independent Non-Executive Director and committee Chairs and for involvement in a committee as a member.

As described within the relevant sections of this Corporate governance report, the Non-Executive Directors' preparation for and attendance at Board and committee meetings is only part of their role.

The other significant commitments of the Chairman and Non-Executive Directors are disclosed to the Board before appointment, with an indication of time involved. During the year, the Governance and Nomination Committee kept under review the number of external directorships held by each Director and considered the limits on the number of directorships which Directors may hold as a result of PRA Rulebook 'General Organisational Requirements 5.4' (having regard to General Organisational Requirements 5.5 and 5.6) and FCA Handbook Senior Management Arrangements, Systems and Controls (SYSC) 4.3A.5R (having regard to SYSC 4.3A.6R and 4.3A.7R). Details of the Chairman's other significant commitments are set out on page 55. Details of the Non-Executive Directors' other significant commitments are set out on pages 55 to 58. Any changes to the Non-Executive Directors' time commitments were reported by the Governance and Nomination Committee to the Board. The Board is satisfied that each Non-Executive Director is able to devote sufficient time to their role.

Executive Directors are encouraged to take non-executive positions in other companies and organisations to broaden their experience. The appointment to such positions is subject to the approval of the Board which considers, in particular, the time commitment required.

Board changes

Richard Gregory, Senior Independent Non-Executive Director, retired from the Board on 10 January 2017.

Further details about the Group's approach to succession planning and diversity can be found in the Governance and Nomination Committee report on page 77. Changes to committee memberships are set out on pages 76, 81 and 90.

Board independence

It is the Company's policy that at least half the Board should be independent Non-Executive Directors. The Board assesses the independence of Directors on an annual basis following a review by the Governance and Nomination Committee. The Board considers each of its current Non-Executive Directors to be independent in character and judgement. The Chairman was considered independent on appointment. Further information is given in the Governance and Nomination Committee report on page 77.

Conflicts of interest

Pursuant to the Companies Act 2006, the Directors have a statutory duty to avoid situations in which they have or can have a direct or indirect interest in the Company, unless that interest is first authorised by the other Directors. This duty is in addition to the existing duty that a Director owes to the Company to disclose to the Board any transaction or arrangement under consideration by the Company. Prior to appointment, potential conflicts of interest are disclosed and assessed to ensure that there are no matters which would prevent the incoming Director from taking the appointment, and during their tenure Directors are asked to consult with the Company Secretary and the Chairman before taking up any external appointment or responsibilities. Any changes to the commitments of Directors are reported to the Governance and Nomination Committee and the Board. Directors are reminded, at each Board meeting, of their duty to report any actual or potential conflict as soon as they become aware of any such events. If any actual or potential conflict arises, the relevant Director will excuse himself/herself from any meeting or discussions where the potential conflicts are considered and all relevant material will be restricted including Board papers and minutes. A Director with a potential or actual conflict will not be permitted to form part of the quorum or vote upon the matter giving rise to the conflict. Directors do not participate in decisions concerning their own remuneration or interest. All potential conflicts authorised by the Board are recorded in a Register of Directors' Conflicts of Interests which is reviewed by the Board annually.

Board induction

The Chairman ensures that each newly appointed Director receives a full and formal induction on joining the Board which is tailored to reflect a Director's skills, experience and Board role.

The Company Secretary designs and facilitates the induction programme having consulted with the Chairman and having regard to the particular needs of the new Director. Progress is reported to the Chairman and reviewed regularly by the Chairman with each Director.

The aim of the induction programme is to quickly provide a new Director with an understanding of how the Group works and the key opportunities and challenges that it faces to enable them to contribute fully in Board and Committee meetings and covers at least the following:

- the Group and its strategy;
- key business drivers of performance and the competitive environment and regulatory landscape in which the Group operates;
- major strategic and investment programmes and priorities;
- the key current and emerging risk issues and challenges for the business and risk appetite;
- the organisational culture and capabilities, the role of the Board and its committees, and the Company's corporate governance practices; and
- training on the role and responsibilities of a Director, including statutory duties.

The induction programme is delivered through a combination of: one-to-one briefings with the Chairman, Company Secretary, current Directors and members of the Executive Leadership Team; site visits to some of the Group's customer facing and operational areas; and reading materials including archive Board and committee papers and other key corporate governance documents. Meetings are also arranged with other selected senior managers, including the Group Director Internal Audit, and with external stakeholders including the External Auditor.

Directors joining the Board to perform a specific role or holding a senior management function role, such as a committee Chair, are provided with additional in-depth training including meeting with the outgoing role holder or committee Chair where possible and completing a documented handover. Particular attention is given to the tailored components of the programme where a Director is appointed from outside the financial services sector or where a Director has not previously served on a UK listed company board. Directors who take on or change role during the year participate in an induction programme tailored to their new role.

As described on page 68 the Board has in place a professional development and training programme which ensures that Director development continues after the initial induction programme has been completed.

Professional development and training

Continuing professional development is an important aspect of a Director's role. Skills and knowledge need to be kept up to date to ensure the effectiveness of the Board as a whole and allow every Director to contribute fully in Board and committee meetings. During the year the Board Development Programme was refreshed so as to provide a more structured approach. The Board Development Programme includes components covering: Board 'deep dive' sessions (details on page 66); stakeholder engagement (see page 66); opportunities for wider stakeholder engagement in the community in which the Group operates; seminars, courses and roundtables to provide external insights on topical issues, technical briefings and peer group debates; and Board briefings (see page 66).

The Chairman reviews with each Non-Executive Director their individual training and development need and progress at regular one:one meetings.

The Company Secretary maintains a training and development log for each Director.

Board performance evaluation

During 2017, the Board engaged an external company, Advanced Boardroom Excellence, to facilitate the 2017 assessment of the effectiveness of the Board and of its committees. Advanced Boardroom Excellence is an independent consultancy with extensive experience undertaking evaluations for publicly listed companies and with no other connection to the Group. The review was led by Helen Pitcher, the Chairman of Advanced Boardroom Excellence, and took place between March and July 2017.

The key conclusion of the evaluation was that the Board and committees operate effectively with a high degree of integrity and appropriate challenge and support. Significant progress has been made since the last external Board evaluation in 2015 before listing. Indeed the Board was recognised as having operated effectively to complete a successful demerger and IPO. The key theme from the review was therefore evolutionary development of the Board recognising the changes to both Board and Board Committee composition during 2016, the integration of new members which continued through 2017 and the transition to an independent publicly listed company.

2017 review process

The Board performance evaluation was coordinated by the Company Secretary and Fiona MacLeod, a Non-Executive Director on the Governance and Nomination Committee, and overseen by the Governance and Nomination Committee.

The Governance and Nomination Committee, with the support of the Board, agreed the themes to be assessed: use of Board time and efficiency of meetings; quality of the information received by the Board; the Board as a team; succession planning, induction and training; and depth of engagement on areas including strategy, risk and customer related topics. The evaluation was conducted against the Financial Reporting Council's (FRC) best practice framework 'Guidance on Board Effectiveness March 2011' which is publicly available at www.frc.org.uk

The 2017 process included various elements.

2017 review process

- Briefing between Advanced Boardroom Excellence, the Company Secretary and Fiona MacLeod during March to agree the scope, process and timetable for the review
- Structured one:one meetings between Helen Pitcher and all Directors, in addition to senior leaders who regularly interface with the Board and Board committees
- Observation of meetings of the Board, Audit Committee and Risk Committee
- Facilitated roundtable discussions with the Governance and Nomination Committee and with the Remuneration Committee
- Review of the Board and Board committee charters, papers and other key governance documentation
- Draft discussion document discussed with the Governance and Nomination Committee in May
- Presentation and facilitated discussion of key evaluation outcomes, led by Advanced Boardroom Excellence
- Presentation by Advanced Boardroom Excellence to the Chair of each Board committee
- Production of a final report of findings and recommendations
- Agreement by the Board of the key areas of focus and continuous improvement actions for the future development of Board effectiveness

The approach was designed to facilitate and encourage open and constructive dialogue and the exchange of ideas and viewpoints between the reviewer and participants. As such, a tailored discussion guide was used to structure the one:one meetings held with each Director, the Company Secretary, Group General Counsel, Group Chief Risk Officer, Group Human Resources Director and Group Director Internal Audit. In the one:one meetings participants were asked for their views on the elements of Board effectiveness identified by the FRC.

While a formal assessment of each individual Director was not sought due to the relatively short period the current Board composition had been in place, the process elicited a number of useful insights which were shared by the Chairman with each Non-Executive Director in his regular one:one meetings. A more formal assessment of individual Directors will be addressed in future years.

Due to evolving corporate governance best practice and regulatory requirements impacting the remit of governance and nomination committees and remuneration committees, facilitated roundtable discussions were held with the Chair and members of the Governance and Nomination Committee and of the Remuneration Committee. This approach enabled the committees to openly discuss how their areas of focus could evolve over the next 12–24 months and what should be the principal areas of committee activity and priorities.

The information gathered during the individual meetings, Board and committee observations, documentation review and roundtable discussions was independently reviewed by Helen Pitcher to produce an analysis of strengths, challenges, development opportunities and recommendations which was set out in a draft discussion document reviewed by the Governance and Nomination Committee. This was followed by a facilitated discussion with the Board at which Helen Pitcher presented the key outcomes of the evaluation and the Board agreed the key areas of focus and priority actions for the future development of Board effectiveness.

In addition a report on the evaluation of each principal Board committee was produced and discussed with the Chair of each committee. The Senior Independent Non-Executive Director received a report on the Chairman which was shared with the Chairman individually and with the Non-Executive Directors without the Chairman being present.

Principal findings

The conclusions of the 2017 review were positive and have confirmed that the Board and its committees operate effectively. A benchmark provided by Advanced Boardroom Excellence against a FTSE 100 comparator group (the Company is currently in the FTSE 250) showed a good balance of strengths and areas to further develop. The Board was found to be detailed in its governance, committed to its continuous improvement and development and showed a desire to achieve best practice on all fronts. The review recognised that the Board comprises a group of accomplished individuals. With a number of relatively new members at Executive Leadership Team and Non-Executive Director level there is a clear focus on further consolidating and building its own dynamic to become an even more integrated and effective team. It was recognised that the team dynamic had been well demonstrated at the successful IPO.

The four key areas for the future development of the Board's effectiveness were:

- *Board oversight* – Increase the opportunities for engaging the full Board in evolving the Group's strategy including developing the knowledge and insight of the whole Board and encouraging Directors to bring external insights;
- *Board development and engagement* – As the Board evolves it continues to focus on the development of the Board itself as a cohesive unit able to continue to challenge consistently and effectively while maximising the diversity of contribution, expertise and knowledge on the Board;
- *Leadership role of the Board* – Provide for greater engagement of the Board with broader stakeholder communities, including customers, in a more proactive and consistent way; and
- *Board planning* – Continue to develop an efficient, effective and balanced governance support process including creating capacity for the Board to undertake reflective challenge and debate on strategic performance.

Corporate governance report

Continuous improvement actions

The Board performance evaluation report from Advanced Boardroom Excellence sets out a series of recommendations that have been carefully considered by the Board. The Board has agreed a suite of priority actions aligned to the key areas for the future development of the Board's effectiveness. Pleasingly a number of these actions had already been discussed and in some cases instigated by the Chairman and Chief Executive Officer. It was positive to see these recommendations reinforced by external expert evaluation. The priority actions agreed by the Board include:

- *ensuring the already robust strategy process allows greater time for input, debate, challenge and discussion at the Board* – prior to the evaluation the Chairman and Chief Executive Officer had agreed a full programme of Board engagement in relation to the FY2018-FY2022 strategic planning process. The Board performance evaluation added some helpful suggestions around seeking an even broader suite of external insights;
- *reviewing the Board's role in the process of both creating and monitoring culture and values to develop a programme of effective feedback to the Board* – the Board is very engaged around the culture and values of the organisation. As agreed by the Board the Group Human Resources Director is working with the Governance and Nomination Committee and the wider Board to ensure a deep rooted and sustained Board role in culture and values going forward;
- *ensuring that work on executive succession and pipeline is integrated into the activities of the Governance and Nomination Committee and more widely shared with the Board* – to this end the Governance and Nomination Committee has identified succession planning, including the Committee's role in executive and senior management succession planning, as a further priority area of focus for 2018. The Board will review the senior talent and diversity, succession and development plans on an annual basis;
- *mapping in conjunction with Non-Executive Directors, a programme of external input* to strengthen the debate and discussion on the key areas of the business strategy and transformation;
- *considering the development opportunities for the Board both from a business and Board dynamics perspective* – the Board annual calendar will be refreshed to include more opportunities for the Board members to spend informal time together. The Chairman will continue to focus on further enhancing the strong Board culture and positive and constructive relations between the Directors as a collective and between the Board and the Executive Leadership Team;
- *focusing specifically on further developing the Board members into a coherent, collective, innovative strategic oversight team* – the Board agenda has been restructured as recommended by Advanced Boardroom Excellence to provide more agenda space for effective debate and challenge at Board meetings on topics such as strategy, culture and stakeholder, including colleague, engagement; and
- *providing the broader executive team with the opportunity to align with the Board more closely* – the Chairman will encourage all Non-Executive Directors to have more one:one time with the members of the Executive Leadership Team (not limited to those members who are Executive Directors on the Board) with progress to be discussed during the Chairman's regular scheduled one:one meetings with each Non-Executive Director and recorded on their individual training and development plan.

Follow up

The Chairman and Board very much regard the Board performance evaluation as an opportunity for continuous improvement, not a one-off event.

The Governance and Nomination Committee, with the support of the Company Secretary, prepared a detailed action plan incorporating the priority actions agreed by the Board and addressing the other recommendations agreed by the Board to be taken forward.

The Governance and Nomination Committee will coordinate the implementation of the actions which will be fully owned across the Board and all Board committees.

Information and support

The Board has processes in place to ensure that it is supplied in a timely manner with information in a form and of a quality to enable it to effectively discharge its duties. The Chairman, through the Company Secretary, is responsible for ensuring communication flows between the Board and its committees with the support of the Executive Directors and management, and ensures that this information is of high quality in terms of its currency, clarity, accuracy, appropriateness and comprehensiveness. All Directors have access to the advice of the Company Secretary in relation to the discharge of their duties and matters of governance. Directors are able to seek clarification or further detail from management where necessary. The Company Secretary is also responsible for facilitating communications with shareholders, as appropriate, and ensuring due regard is paid to their interests. All Directors are provided with sufficient resources to undertake their duties. In appropriate circumstances, Directors may obtain, at the Group's expense, independent professional advice where they judge it necessary to discharge their responsibilities as Directors. The appointment and removal of the Company Secretary is a matter reserved for the Board as a whole.

Service contracts and letters of appointment

Details of Executive service contracts and letters of appointment of the Board are set out on pages 105 and 106 of the Directors' remuneration report.

Internal control

Board responsibility

The Board is responsible for the Group's systems of internal control. The internal control framework is designed to facilitate effective and efficient operations, ensure a high quality of internal and external reporting, and ensure compliance with applicable laws and regulations. The Directors and management are committed to maintaining a robust control framework as the foundation for the delivery of effective risk management. Owing to the limitations inherent in any internal control framework, the controls have been designed to manage and mitigate, rather than eliminate, the risk of failure to achieve the Group's business objectives and can provide only reasonable, not absolute, assurance against material misstatement or loss. The Directors acknowledge their responsibilities in relation to the Group's internal control framework and for reviewing its effectiveness.

The Board confirms that throughout the year ended 30 September 2017 and up to the date of approval of this Annual Report and Accounts, there have been rigorous processes in place to identify, evaluate and manage the principal risks faced by the Group, including those that would threaten its business model, future performance, solvency or liquidity, the likelihood of a risk occurring and the costs of control in accordance with the Guidance on Risk Management, Internal Control and Related Financial and Business Reporting published by the FRC.

In order to assist in the identification and management of the principal risks, the Board has established an RMF which is integrated into the Group's overall framework for risk governance and has developed a system of regular reports from management. The Board has authorised the Risk Committee to oversee the Group's compliance with the Board's approved RAS, RMF and risk culture. Further details can be found in the Risk report on pages 127 to 175.

Reviews by the Board

The effectiveness of the risk management and internal control systems is reviewed regularly by the Risk Committee and the Audit Committee, including an annual review. The Risk Committee is responsible for providing oversight and advice to the Board in relation to current and potential future risk exposures. The Audit Committee assists the Board in discharging its responsibilities with regard to external and internal audit activities and controls including reviewing audit reports, internal controls and risk management systems.

The Group's risk management and internal control systems are regularly reviewed by the Board and are consistent with the guidance on Risk Management, Internal Control and Related Financial and Business Reporting issued by the FRC and compliant with the requirements of the Capital Requirements Directive IV (CRD IV). They have been in place for the year under review and up to the date of the approval of the Annual Report and Accounts.

Control effectiveness

A review of the effectiveness of controls is regularly undertaken across the Group, providing an assessment and statement on the effectiveness of the Group's control environment. This provides assurance to the Risk Committee that no new material control issues have been identified and that robust management actions are in place to address specific known gaps.

Overall assessment

Over the past year, the Group has further enhanced the RMF, simplifying and improving the risk categories and impact classification. The control environment remains stable with the 2017 Control Effectiveness Statement providing assurance that ineffective controls are escalated appropriately and have adequate action plans in place.

The Risk Committee, in conjunction with the Audit Committee, concluded that the Group's risk management and internal control framework in relation to the Group's risk profile and strategy was effective and adequate, and was recommended to and approved by the Board.

Bribery and corruption

In compliance with the Bribery Act 2010, the Group has in place risk assessments, policies and guidelines on interacting with customers, suppliers and agents, including specific policies for gifts and hospitality. Certain Senior Managers are required to assess money laundering risks and the adequacy of related internal controls within their areas of responsibility on an ongoing basis. Formal anti-bribery and corruption training is required for all colleagues, the Executive Leadership Team and Directors.

Remuneration

The statement by the Chair of the Remuneration Committee and the Directors' annual report on remuneration are set out on pages 94 to 122.

Corporate governance report

Shareholder relationships

The Board recognises the need for a programme of engagement which offers all shareholders opportunities to receive information from the Company and enables them to share their views with the Board. In addition, the Board regularly receives feedback on shareholder sentiment and sell side analyst views of the Group and the wider industry.

The Board is committed to ensuring that there are effective channels of communication with the Company's shareholders. The Group's website enables access to documents and communications as soon as they are published, including recordings of webcasts and other analyst presentations.

Relationships with institutional investors

Engagement with institutional investors (both existing and potential investors) took place throughout the year, in order to update the market on our progress against the Group's long-term strategy and recent financial performance. Investor roadshows were held in key geographic locations reflecting the nature of the Company's institutional ownership and were attended by an appropriate mix of Directors and included the Chairman, the Deputy Chairman and Senior Independent Non-Executive Director and the Chief Executive Officer.

The Board receives regular feedback on share price performance, investor and analyst views and changes to the shareholder register via regular monthly reports, a quarterly detailed investor relations update and *ad hoc* intelligence.

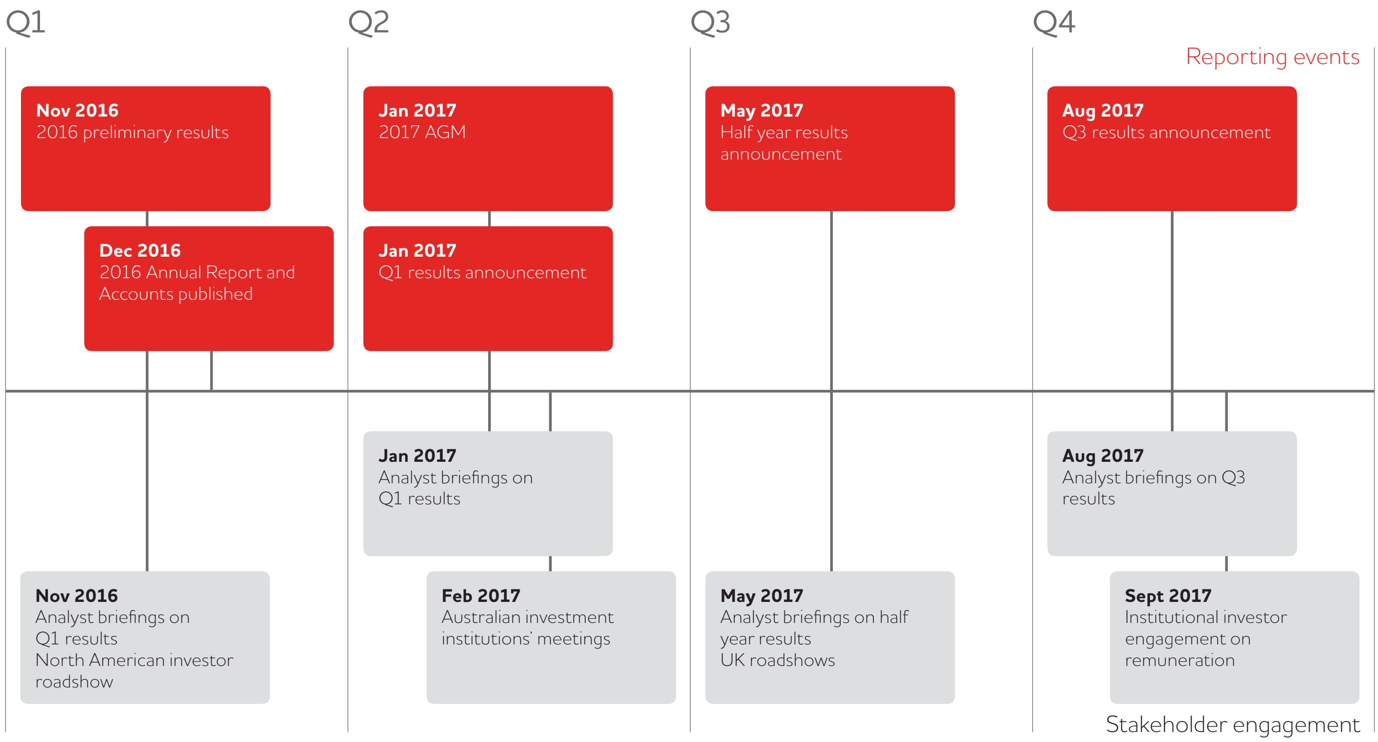
Relationships with retail shareholders

The Company Secretary oversees communication with retail shareholders and provides feedback to the Board and appropriate committees to ensure the views of retail shareholders are received and considered.

The Group's Registrar, Computershare, provides a dedicated shareholder service at www.investorcentre.co.uk in the UK and www.investorcentre.com.au in Australia through which shareholders can manage their shareholding online, receive Company communications and cast proxy votes for forthcoming general meetings.

Small holding sale facility

In May 2017, the Company announced the launch of a sale facility for eligible holders (including shareholders and CDI holders) for small holdings, defined in the Company's Articles of Association as a holding of shares with an aggregate market value of less than A$500 based on the closing price of a CHESS Depository Interest (CDI) on the Australian Securities Exchange (ASX). This facility provided eligible shareholders with an easy and cost-effective way to sell all of their shares and enabled the Group to reduce the ongoing costs associated with administering the security registers. The sale facility closed on 28 June 2017 at which point 5,187,747 shares were sold pursuant to the facility which had been held by 139,846 eligible holders representing 0.59% of the total issued share capital of the Company at the time.



The annual general meeting

Shareholders are invited to attend the Company's 2018 annual general meeting (AGM), to be held at 10am (GMT) on Wednesday 31 January 2018 at the offices of Pinsent Masons LLP, 30 Crown Place, Earl Street, London, EC2A 4ES, United Kingdom, when they will have the opportunity to engage directly with Directors, who will be available to answer any shareholder questions. Facilities are also available for shareholders to cast their votes electronically, or by post. All resolutions at the 2018 AGM will be voted on a poll. The procedure for voting on a poll follows best practice and allows the Company to count all votes rather than just those of the shareholders attending the meeting.

The resolutions to be proposed at the AGM, together with explanatory notes, are set out in a separate Notice of AGM which accompanies this Annual Report and Accounts and is on the Company's website (www.cybg.com). The Notice of AGM is circulated to all shareholders at least 20 working days before such meetings and it is the Company's policy not to combine resolutions. As recommended by the Code, all resolutions to be proposed at the 2018 AGM will be voted on separately and the voting results will include all votes cast for, against and those withheld, together with all proxies lodged before the meeting. A vote withheld will not be a vote in law and will not be used in calculating the votes for or against a resolution. Details of the proxy votes cast will be made available on the Company's website as soon as is reasonably practicable after the meeting, by means of an announcement on the securities exchanges to which the Company is listed and on the Company's website www.cybg.com. In the opinion of the Board, where the situation arises that a significant proportion of votes have been cast against a resolution at any general meeting, the Company will explain, when announcing the results of voting, what action it intends to take to understand the reasons behind the result of the vote.

Governance and Nomination Committee report

“The Committee has evolved its role and remains committed to being at the forefront of best corporate governance practice.”

Dear shareholder,

As Chairman of the Board and Chairman of the Governance and Nomination Committee, I am pleased to present the report on the Committee’s activity during 2017.

The Committee’s role is to regularly review the structure, size and composition of the Board having regard to the balance of skills, experience, knowledge, independence and diversity on the Board. It is also responsible for developing and maintaining a formal, rigorous and transparent procedure for identifying and nominating for approval by the Board, candidates to fill Board and committee vacancies when they arise. The Committee also: reviews the succession plans at Board and Executive level; leads the process for the periodic evaluation of the performance and effectiveness of the Board, committees and individual Directors; and makes recommendations to the Board to ensure that the Group’s corporate governance arrangements are consistent with best practice and good corporate governance standards.

During 2017, the Committee spent considerable time overseeing the annual performance evaluation of the Board and its committees which this year was externally facilitated by Advanced Boardroom Excellence. I am grateful to Fiona MacLeod who led the process on behalf of the Committee and the Board. The evaluation approach, process followed, principal areas of development and priority actions agreed by the Board are described on pages 68 to 70 of the Corporate governance report. I am pleased to confirm that the key conclusion of the evaluation was that the Board and its committees operate effectively with significant progress made since the last external Board evaluation which was undertaken in 2015 in advance of the demerger and IPO. Since the completion of the review the Governance and Nomination Committee has overseen the preparation and implementation of a detailed action plan incorporating the priority actions agreed by the Board and has kept the Board informed of progress.

As part of the annual performance evaluation, the Governance and Nomination Committee held a facilitated roundtable session with Advanced Boardroom Excellence to discuss openly how the Committee wanted to evolve its role consistent with best practice for listed company governance and nomination committees. Following the IPO, the focus of the Committee in 2016 and early 2017 was principally on succession planning and refreshing capability and composition of the Board and its committees. Having taken time to both fully reflect and to look ahead, the Committee has now agreed its principal areas of activity and priorities for 2018 as follows:

- evaluation of the skills, knowledge and experience on the Board particularly with regard to longer-term requirements and to inform future Board composition;
- succession planning, including the Committee's role in executive and senior management succession planning, which is an area of growing shareholder and regulatory interest;
- developing the Committee's and Board's role in the areas of talent management and leadership development;
- agreeing the Committee's and Board's role in supporting management with the cultural transformation and diversity and inclusion agendas; and
- improving Director training and development.

In the year ahead, the Committee will continue to monitor the needs of the Board, its committees and the longer-term leadership of the business by ensuring that succession plans align to, and keep pace with, the strategic goals of the Group. The Committee will continue to oversee the effectiveness of the corporate governance arrangements, particularly the impacts of corporate governance reforms, and will continue to monitor the implementation of the actions agreed by the Board following the performance evaluation of the Board and of its committees.

Jim Pettigrew
Chair, Governance and Nomination Committee

Governance and Nomination Committee report

Membership and meetings

The current members of the Committee are:

Jim Pettigrew, Chair

David Bennett

Fiona MacLeod

The Committee is chaired by the Chairman of the Board and the members of the Committee are Independent Non-Executive Directors, in accordance with the provisions of the Code. If a matter were to concern the Chairman, then he would leave the meeting and the remaining members would elect one of their number to take the Chair, unless the Chairman had designated a member to do so.

The Chief Executive Officer attends meetings at the invitation of the Committee. The Group Human Resources Director also attends meetings at the invitation of the Committee, particularly when it is considering Executive succession planning matters.

Members of the Committee took no part in any discussions concerning their own membership of the Board or appointment as a Chair of a committee.

Committee attendance

The core activities of the Committee were carried out in four scheduled meetings of the Committee. One additional *ad hoc* meeting was arranged for decisions required outside scheduled meetings. The table below shows the Committee members during the year to 30 September 2017 and their attendance at scheduled Committee meetings.

	Number of scheduled Committee meetings eligible to attend	Number of scheduled Committee meetings attended
Committee Chair		
Jim Pettigrew	4	4
Committee members		
David Bennett	4	4
Fiona MacLeod[(1)]	4	4
Former Committee members		
Richard Gregory[(2)]	1	1

(1) Fiona MacLeod was appointed as a Committee member on 30 December 2016.
(2) Richard Gregory retired as a Committee member on 10 January 2017.

Committee role and responsibilities

During the year, the Committee revised its Charter which sets out the role and responsibilities of the Committee. The Charter of the Committee can be found on the Company's website www.cybg.com/about-us/corporate-governance/

Committee performance evaluation

The independent, externally facilitated Board Performance Evaluation carried out during the year included an assessment of the Committee's effectiveness. The review identified that the Committee Charter reflected best practice and that the responsibilities of the Committee set out in the Charter were consistent with the Code. A key finding was that the Committee needs to reflect on its responsibilities and to set its objectives and priorities for the year and agree the processes by which it will fulfil its responsibilities. The Committee has now agreed its priorities, as set out on page 75, and is developing a work plan to address these priorities in addition to its wider Charter responsibilities. The Committee's calendar of meetings has been refreshed to allow for better planning and to ensure the Committee's workload is spread across the calendar year.

Matters considered and actions taken by the Committee

The significant matters addressed by the Committee during the year ended 30 September 2017 and in evaluating the 2017 Annual Report and Accounts are described in the following pages.

Role of the Committee	Key matters considered and actions completed

Board and Board committee composition
Membership of the Board and the current and future composition of its committees
	– Reviewed the structure, size and composition of the Board and Board committees including skills, experience, independence, knowledge and diversity and considered the longer-term succession of Board and committee members relative to tenure, mix and diversity of skills and the Group's strategy, future challenges and opportunities; reported the outcome and recommendations to the Board;
	– Reviewed the time commitment including external appointments of serving Directors;
	– Undertook the annual review of the Conflicts of Interests Register; and
	– When considering the recruitment of a new Director, the Committee adopts a formal, rigorous and transparent procedure with due regard to diversity, including gender. Before commencing the recruitment process, the Committee evaluates the balance of skills, knowledge, experience, independence and diversity on the Board and, in light of this evaluation, prepares a description of the role and capabilities required. In identifying suitable candidates, the Committee:
	  – uses open advertising or the services of external advisers to facilitate the search;
	  – considers candidates from different genders and a wide range of backgrounds;
	  – considers candidates on merit and against objective criteria ensuring that appointees have sufficient time to devote to the position, in light of other potential significant positions; and
	  – engages from time to time with the Group's major shareholders in future skills requirements and ideas for potential candidates.

Skills and independence	– Assessed the independence of Non-Executive Directors having regard to both the Code requirements on independence and factors such as length of tenure and the ability of Non-Executive Directors to objectively challenge the Executive, free from relationships or circumstances which are likely to affect, or could appear to affect, the Director's judgement. The Committee also took account of any relationships that had been disclosed and authorised by the Board. Based on the assessment for 2017 the Committee is satisfied that, throughout the year, all Non-Executive Directors remained independent as to both character and judgement and that Jim Pettigrew, the Board Chairman, was considered independent on appointment. At least half the Board comprised independent Non-Executive Directors; and – Recommended to the Board the re-election of all Directors.
Executive succession planning and talent management	– Had an update from and discussion with the Group Human Resources Director on the succession plan for the Executive Leadership Team and their direct reports; and – Had an update from and discussion with the Group Human Resources Director on the Group's talent management framework and talent pool and the opportunities for Board engagement in talent management and leadership development.
Diversity and inclusion	– The Board recognises the value of achieving diversity on the Board and throughout the Group. Although new appointments are based on merit, careful consideration is given to the benefits of improving and complementing the diversity, skills, experience and knowledge of the Board. The Board recognises and is committed to creating the conditions that foster talent for women to achieve their full potential by building strong female representation at Board level, Executive Leadership Team level and throughout the Group. During the year the Committee reviewed and recommended to the Board an updated Board Inclusion and Diversity Policy Statement to include a target of 33% female representation on the Board by 2020, achieved through the natural cycle of Board renewal. It is also the Board's intention to broaden diversity on the Board beyond gender diversity alone, to reflect the communities in which the Group operates and serves. As at 30 September 2017, there were three female Directors (25%) on the Board.

Governance and Nomination Committee report

Role of the Committee	Key matters considered and actions completed
Board and Board committee effectiveness review	– Oversaw the annual performance evaluation of the Board and its committees which was externally facilitated by Advanced Boardroom Excellence. The evaluation approach, process followed, principal areas of development and priority actions agreed by the Board are described on pages 68 to 70 of the Corporate governance report; – Oversaw the preparation and implementation of a detailed action plan incorporating the priority actions agreed by the Board, actions of an administrative nature and actions specific to a Board committee; kept the Board informed of progress; and – Undertook an assessment of the effectiveness of the externally facilitated independent performance evaluation of the Board.
Governance	– Participated in a facilitated roundtable session with Advanced Boardroom Excellence to openly discuss the evolving corporate governance best practice and regulatory requirements impacting the remit of the Governance and Nomination Committee; – Discussed and agreed how the Committee's areas of focus could evolve over the next 12–24 months and what the principal areas of Committee activity and priorities should be; – Received an update on proposed corporate governance reforms; and – Reviewed and agreed an External Directorship Policy for adoption by the Board to govern the number of non-executive directorships an incoming or current Director is permitted to hold in the context of ensuring Directors are able to commit sufficient time to their role with the Group to discharge their responsibilities effectively.

Audit Committee report

“The Audit Committee has fulfilled its responsibilities to ensure the integrity and quality of the Group’s financial reporting.”

Dear shareholder,

As Chair of the Audit Committee, I am pleased to present the report from the Committee for the year ended 30 September 2017. I became the Chair of the Committee on 23 November 2016, having been a member since 12 September 2016. I would like to thank David Bennett, my predecessor as Interim Chair, for his invaluable guidance and insight to me as incoming Chair.

Highlights in 2017

During the year, the Audit Committee has fulfilled its responsibilities and met its key objectives, by overseeing financial reporting, including the adequacy of related disclosures as well as reviewing internal controls and the effectiveness of both internal and external audit. The Committee is comprised of independent Non-Executive Directors.

The Committee continued to exercise its responsibilities for ensuring the integrity and quality of the Group’s financial reporting and spent considerable time reviewing the Group’s financial results. It questioned management robustly on a number of key accounting judgements relevant to the financial statements, including a focus on impairment losses on loans and advances, PPI redress provision and other conduct matters, deferred tax assets, retirement benefit obligations and fair value of financial instruments (full details are contained on pages 82 to 84 of this Report). The Committee has focused closely on the analysis underpinning the ongoing Going Concern test, the longer-term Viability Assessment, and in particular, the presentation of the Annual Report and Accounts in a way that makes them Fair, Balanced and Understandable.

The Group continues to enhance its control environment. The Committee, utilising its independent perspective, challenged constructively the operation of the Group’s Three Lines of Defence model in relation to the Group’s internal controls which is essential to ensure risks are appropriately managed and mitigated. The Committee has worked closely with the Risk Committee in this process.

The Committee continued to oversee the performance and effectiveness of internal and external audit, the main independent assurance mechanisms that serve to protect shareholders’ interests.

Audit Committee report

The Group Director Internal Audit provided regular updates to the Committee on enhancements made during the year to the Internal Audit function, following on from Deloitte LLP's external quality assessment of the Internal Audit Function in 2016. These included a refresh of the Internal Audit strategy to align to the Group's strategy and clearly link the Internal Audit work to the key drivers of success for the Group.

Having considered feedback from stakeholders, peer benchmarking analysis, results of quality assessments and the Internal Audit reports provided to the Committee, it was concluded that Internal Audit activities were effective.

The Committee closely monitored the external audit process and the performance of the External Auditor, EY, through an annual effectiveness review against four themes in line with the FRC guidance: judgement; mindset and culture; skills, character and knowledge; and an assessment of quality control. The Committee considered the review and concluded in terms of the themes assessed that the external audit process was effective.

Committee performance evaluation
The independent, externally facilitated Board Performance Evaluation carried out during the year included an assessment of the Committee's effectiveness. Overall, the Committee was assessed as effective. Further details are provided in this report.

Looking ahead
The report sets out the areas the Committee focused on in 2017. Many of these areas will again be areas of focus for the Committee in 2018. In particular the Committee will monitor the application of the Three Lines of Defence Model, assess the Internal Audit oversight of the IRB project, and continue to provide oversight of the implementation of the new financial instruments accounting standard IFRS 9, which will be effective for the Group in the reporting period beginning 1 October 2018.

Tim Wade
Chair, Audit Committee

Membership and meetings

The current members of the Committee are:

Tim Wade, Chair

Clive Adamson

David Bennett

David Browne

Dr Teresa Robson-Capps

The Committee comprises five Independent Non-Executive Directors. Tim Wade, Chair, has recent and relevant accounting and audit experience for the purposes of the Code, having held a number of senior finance roles. The other Committee members have significant current or recent experience in the financial services and banking industries (details of which are contained within the biographies section on pages 55 to 58). This depth of experience enables the Committee to deal effectively with the matters within its remit and to challenge management and auditors when required.

In addition to the Committee members, the Chairman, Chief Executive Officer, Chief Financial Officer, Group Head of Finance, Group Chief Risk Officer, Company Secretary, Group General Counsel, Group Director Internal Audit and the External Auditor are invited to attend Committee meetings. The Chair is also a member of the Risk Committee.

Private sessions are held with the External Auditor and Group Director Internal Audit at alternate Committee meetings to provide additional opportunity for open dialogue and feedback without management being present. The Chair of the Committee also meets with the Group Director Internal Audit and the Senior Statutory Auditor outside the formal Committee process at regular intervals throughout the year.

Alignment with Risk Committee

The Committee recognises the common interest in issues relevant to both the Risk Committee and Audit Committee and in particular the responsibilities of both in relation to the effectiveness of internal control. Joint discussions by both committees for the financial year ended 30 September 2017 included: progress made towards the implementation of IFRS 9; the Company's fraud and money laundering controls; assurance plans from the Three Lines of Defence; the Viability Statement; and bonus risk adjustments and metrics to be recommended to the Remuneration Committee. To support the coordination of information between the committees, the Chairs of each of the Audit and Risk Committees are members of both committees. The Audit Committee and Risk Committee also hold at least one joint meeting per year.

Committee attendance

The core activities of the Committee were carried out in six scheduled meetings of the Committee. Two additional *ad hoc* meetings were arranged for decisions required outside scheduled meetings. The table below shows the Committee members during the year ended 30 September 2017 and their attendance at scheduled Committee meetings.

	Number of scheduled Committee meetings eligible to attend	Number of scheduled Committee meetings attended
Committee Chair		
Tim Wade	6	6
Committee members		
Clive Adamson	6	6
David Bennett	6	6
David Browne	6	6
Dr Teresa Robson-Capps	6	5(1)
Former Committee members		
Richard Gregory (2)	2	2

(1) Unable to attend the meeting due to a prior business commitment.
(2) Richard Gregory retired as a Committee member on 10 January 2017.

Committee role and responsibilities

During the year, the Committee revised its Charter which sets out the role and responsibilities of the Committee. The Charter of the Committee can be found on the Company's website www.cybg.com/about-us/corporate-governance/.

Committee performance evaluation

The Committee's performance was reviewed as part of the independent, externally facilitated Board Performance Evaluation during the year which included an assessment of the Committee's effectiveness. Overall, the Committee was assessed as effective. The key area for development related to ensuring that the Charters for the Audit and Risk committees were reviewed to mitigate duplications and overlaps. This was an action already identified by both committees.

As part of a handover to Tim Wade on his appointment as Chair of the Committee, the new Chair set out his priorities for the Committee and these priorities have been incorporated into the Committee's annual work plan and informed the Committee's agenda throughout the coming year.

Audit Committee report

Matters considered and actions taken by the Committee

The significant matters addressed by the Committee during the financial year ended 30 September 2017 and in evaluating the 2017 Annual Report and Accounts are described in the following pages.

Role of the Committee	Key matters considered and actions completed
Accounting, tax and financial reporting	
To review the appropriateness of the Company's financial statements, including the content of the Interim Financial Report, Annual Report and Accounts, and related Preliminary Results Announcements, Interim and quarterly results announcements and supporting analyst presentations.	– Understood the process for the production of the reports under the remit of the Chief Financial Officer and the level of involvement of cross-functional subject matter experts, including monitoring the procedures in place to ensure that all contributors attested to the completeness, accuracy and appropriateness of the disclosures provided.
Accounting policies and practices To review the critical accounting policies, disclosure obligations and changes in accounting requirements.	– Reviewed with both management and the External Auditor critical accounting estimates and judgements, significant accounting policies and disclosures for the Group's financial statements during the year; and – Received regular updates from the Group Accounting Policy team and External Auditor on key developments in financial reporting requirements. In particular, deep dives were presented on the Group's readiness to implement IFRS 9 to be adopted by the Group from 1 October 2018.
Significant issues and areas of judgement To consider where necessary, the actions, estimates and judgements of management.	
Impairment losses on loans and advances The Group's loans and advances are subject to impairment losses, which are measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. The process of calculating the collective loan loss provision requires the use of significant estimates and judgements over the following: estimating the probability of default and estimates of future recoveries in Base Models; Model Risk Reserves; and the use of overlays.	– Reviewed regular reports from management in relation to impairment provisioning, with the key focus being on collective provisioning for SME lending where the judgemental element is most significant; – Reviewed and challenged the inputs and resulting output of the base models, with a particular focus on probabilities of default and the estimate of future recoveries; – Reviewed and challenged the level of overlays included within the collective provision and the rationale behind the requirement for overlays to be held that augment the collective provisioning modelled output; and – Agreed that the judgements were appropriate at 30 September 2017. The disclosures relating to impairment provisions are set out in note 3.6 to the financial statements and in the Risk report from page 137.

Role of the Committee	Key matters considered and actions completed
PPI redress provision and other conduct related matters The level of provisions required for both redress and administration in relation to past conduct related matters requires assumptions to be made that are based upon a combination of historical data and management judgement. These judgements are inherently complex as they involve making estimates based on multiple factors that incorporate expectations of future customer behaviour, the impact of regulatory rule making and the application of precedent from the Financial Ombudsman Service.	– Reviewed and challenged the assumptions made by management when determining the level of provisions required for PPI and other conduct related matters; – Reviewed in detail proposals in relation to PPI and other conduct scenarios (including potential redress and administrative costs) presented by management which reflected alternative potential outcomes before concluding on the £190m provision increase recorded in March 2017 and the £403m increase recorded in September 2017. Under the terms of the Conduct Indemnity Deed in place with NAB, the impact of this on the Group income statement was £58m; – Considered the continued impact of Plevin together with PS17/3 issued in March 2017 relating to the August 2019 time bar for PPI complaints. Based upon the most recent information the Committee concluded that the assumptions used by management were supportable and that the PPI provisions recorded at 30 September 2017 were appropriate; and – Based upon the most recent information the Committee concluded that management assumptions were supportable and that the other related conduct provisions recorded at 30 September 2017 were appropriate. The disclosures relating to provisions for conduct matters and the impact of the Conduct Indemnity Deed are set out in note 3.14.
Deferred tax assets The largest elements of the Group's deferred tax asset are historic losses and capital allowances. In determining that the deferred tax asset balance remains on the balance sheet, management has exercised judgement over the forecast future profitability of the Group; and the number of years over which to take account of future profits, i.e. the period over which profits can be reliably estimated.	– Reviewed the recoverability of deferred tax assets throughout the year; – Considered the judgements made by management over the forecast future profitability of the Group and the time horizon over which the use of tax losses was foreseeable in light of the continuing and progressively tightening restrictions on their use; and – Agreed that the recognition of a deferred tax asset balance of £154m at 30 September 2017 was appropriate. The disclosures relating the Group's deferred tax asset position as at 30 September 2017 are set out in note 3.11.
Retirement benefit obligations The actuarial valuation of the Group's defined benefit scheme liabilities involves making several financial and demographic assumptions, including: discount rate; future inflation rates; and future mortality rates.	– Reviewed the discount and inflation rate assumptions proposed by management at 30 September 2017 against a benchmark range provided by the external adviser and concurred with these key assumptions; and – Considered the mortality assumptions which were reflective of the position reported at the recent Triennial Review by the Scheme actuary. The disclosures relating the Group's retirement benefit obligations at 30 September 2017 are set out in note 3.16.

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Audit Committee report

Role of the Committee	Key matters considered and actions completed
Fair value of financial instruments Significant management judgement is required for Level 3 measurements, as one or more inputs are unobservable. The most significant Level 3 asset is the Fair Value Loan Portfolio, where management exercises significant judgement over future expectation of credit losses, through the application of a Credit Risk Adjustment (CRA).	– Reviewed the judgement made by management and concurred with the level of CRA applied at 30 September 2017. The disclosures relating the Group's fair value loan portfolio and fair value measurements at 30 September 2017 are set out in notes 3.3 and 3.18 respectively.

The Committee considered management's review of the disclosed critical accounting estimates and judgements. The Committee concluded that, with the exception of the consideration of the carrying value of the Company's investment in Clydesdale Bank PLC which was not a critical estimate or judgement as at 30 September 2017 as there was no evidence that the asset was impaired, no changes were required to these in the 2017 Annual Report and Accounts.

The Committee considered whether critical estimates and judgements were involved in a number of other areas, including the effective interest rate method of accounting (Note 2.2) and the capitalisation and impairment of intangible assets (Note 3.10). The Committee concluded that the impact of the sensitivity of judgement in these areas was low and consequently they were not critical estimates or judgements.

Going concern	– Reviewed and challenged the going concern assessment undertaken by management including evidence of the Group's capital, liquidity and funding position and confirmed to the Board that it was appropriate for the Group's financial statements to be prepared on a going concern basis.
Long-term viability	– Reviewed and challenged the viability assessment (including the three year time horizon selected) undertaken by management in the 2017 Annual Report and Accounts. The Committee considered the process to support the viability statement in conjunction with an assessment of principal risks and strategy/business model disclosures, taking into account the assessment by the Risk Committee of stress testing results and risk appetite. The Committee recommended the draft viability statement (as set out on page 125) to the Board for approval.
Assessment of the fair, balanced and understandable reporting	– Considered, at the request of the Board, the comprehensive review process which supports the Board and Committee in reaching its conclusion whether the 2017 Annual Report and Accounts was fair, balanced and understandable and whether it provided the necessary information for shareholders to assess the Group's performance, business model and strategy. The process which enabled the Committee to reach this conclusion included: – the production of the 2017 Annual Report and Accounts which was managed by the Chief Financial Officer, with overall governance and coordination provided by a cross-functional team of senior management led by the Group Head of Finance; – cross-functional support to drafting the 2017 Annual Report and Accounts, which included input from Finance, Risk, Legal and Governance, Investor Relations, HR and the wider business; – a robust review process of inputs into the 2017 Annual Report and Accounts by all contributors to ensure disclosures were balanced, accurate and verified, and further comprehensive reviews were conducted by senior management; – a review by the Company Secretary of all Board and Committee minutes to ensure all significant matters discussed at meetings were appropriately disclosed in the 2017 Annual Report and Accounts as required; – a formal review by the Committee of the draft 2017 Annual Report and Accounts in advance of final sign-off; and – a final review by the Board of Directors. – After careful review and consideration of all relevant information, including principal risks, the Committee was satisfied that, taken as a whole, the 2017 Annual Report and Accounts is fair, balanced and understandable and has affirmed that view to the Board. – This process was also undertaken in respect of all the Group's financial reporting during the year to ensure that, taken as a whole, based on the information supplied to it and challenged by the Committee, they were fair, balanced and understandable, and advised the Board to that effect.

Role of the Committee	Key matters considered and actions completed
Regulatory compliance Oversight of the Group's compliance with all necessary regulatory reporting.	– Reviewed the integrity of the Pillar 3 Disclosures and recommended approval by the Board; – Considered the findings from Internal Audit's review of COREP reporting as requested by the PRA as part of an industry-wide exercise to examine the quality of COREP reporting across a number of banks and building societies; and – Oversight of significant management judgement in the regulatory returns to the Group's regulators, the PRA, BoE and FCA.
Internal controls and RMF Details of the internal controls and risk management systems for the Group's financial reporting process are provided within the Corporate governance report on page 71 and in the Risk report on pages 127-175.	– Reviewed in line with the Internal Audit plan, the output of Internal Audit reports (including thematic and focused reviews of prudential, credit, conduct and strategic change risks) to confirm the effectiveness of the Group's internal control and risk management systems; and – Considered the findings of the External Auditor in connection with the Group's control environment.
Monitoring the effectiveness of the Group's whistleblower framework The Chair of the Committee is the Whistleblower Champion in accordance with the Senior Managers Regime with responsibility for the integrity, independence and effectiveness of the Group's policies and procedures on whistleblowing and the Committee has oversight of the whistleblower policy standard and framework.	– Considered periodic whistleblower framework reports covering the Group's whistleblowing arrangements, including monitoring the trends in reported and substantiated whistleblowing cases; – Obtained assurance on the completion of training by colleagues to raise awareness across the organisation of the whistleblower framework; – Agreed the transfer of responsibility of the whistleblowing policy standard and framework from Internal Audit to Regulatory and Compliance Risk, with Internal Audit undertaking periodic assurance over its effectiveness and operation; and – Had oversight of updates to the whistleblowing policy standard to include slavery and human trafficking concerns as a result of the Modern Slavery Act 2015 and to reflect the requirements set out in the FCA's Senior Management Arrangements, Systems and Controls Sourcebook, the PRA Rulebook – General Organisational Requirements and the Employment Rights Act 1996.
Fraud and anti-money laundering	– In conjunction with the activities of the Risk Committee, reviewed management's processes for identifying and responding to the risk of fraud and money laundering. Specifically, this involved understanding and overseeing the adequacy of Internal Audit coverage of fraud and money laundering controls and External Audit coverage of fraud risks and controls relating to financial reporting; and – Considered any instances in which control weaknesses, fraud or misconduct were highlighted and management's response in conjunction with any associated control deficiencies.

As a result, the Committee, in conjunction with the Risk Committee, is satisfied that internal controls for financial reporting and risk management systems were appropriate and fit for purpose throughout the year.

Audit Committee report

Role of the Committee	Key matters considered and actions completed
Independence and assurance **Internal audit** *Monitoring the role and effectiveness of the Internal Audit function including the role of the Group Director Internal Audit*	– Approved revisions to the Internal Audit Charter which sets out the role and responsibilities of the function in relation to recommendations made by Deloitte LLP in their external quality assessment (EQA) of the Internal Audit Function in 2016 (the EQA is to take place at least once every five years) and updated guidance in accordance with the Institute of Internal Auditors. The Internal Audit Charter can be found on the Company's website at www.cybg.com/about-us/corporate-governance/; – Approved the audit plan and monitored progress to deliver the plan and material changes to it on a quarterly basis; – Reviewed the outcomes of Internal Audit's work, the actions agreed with management to address any issues raised and the status of previously agreed actions; – Regular interactions with the Group Director Internal Audit during the year, including private sessions with the members of the Committee and specific workshops with Internal Audit and senior management to discuss audit planning and priorities; – Assessed the annual performance of the Group Director Internal Audit. The Group Director Internal Audit continued to report directly to the Chair of the Committee, with a secondary reporting line to the Chief Executive Officer for administrative purposes; – Following the EQA in 2016, the Committee tracked the progress made during the year of the implementation by the Group Director Internal Audit of certain recommendations raised in the assessment to further enhance the Internal Audit function; and – Reviewed the results of internal quality assurance reviews on the effectiveness of the Internal Audit function.
The Internal Audit function was sufficiently resourced and skilled to operate as a standalone entity	– Monitored the adequacy of Internal Audit resources, including the financial budget and capability to draw on external specialists when appropriate. This included a dedicated peer benchmarking exercise conducted during the year.
External audit *Responsible for overseeing the relationship with the External Auditor*	– Approved the annual audit plan, approved the engagement letter and agreed the auditor's remuneration. The Committee was authorised by shareholders at the 2017 AGM to agree the remuneration of the External Auditors; – Reviewed the findings of the external audit including key judgements and the level of challenge provided by the External Auditor; – Reviewed the External Auditor's representation letter; and – Reviewed management's responses to control findings, non-compliance and any other findings identified by external audit.
Assessed the performance of the External Auditor	– The Committee considered the effectiveness of the audit process and the External Auditor performance as part of an annual performance review. The assessment focused on the areas of judgement; mindset and culture; skills, character and knowledge; with an overarching assessment of quality control.

Role of the Committee	Key matters considered and actions completed
External Auditor independence and objectivity, and remuneration for audit and non-audit services	– Both the Board and the External Auditor have safeguards in place to protect the independence and objectivity of the External Auditor. The Committee approved during the year revisions to the External Auditor Policy Standard ('Policy Standard') to align it to the Group's Policy Management Framework (aligned with the RMF in September 2017) and the FRC's Revised Ethical Standard 2016; – The Policy Standard details the nature of the services that the External Auditor may not undertake and specifies that non-audit services may not be pre-approved and are subject to prior approval from the Committee or a delegate. In certain cases, the External Auditor may be selected over another service provider due to their detailed knowledge and understanding of the Group's operations. Any allowable non-audit service with a value above £100,000 requires approval from the Chair of the Committee. The Policy Standard also specifies that the overall fee for non-audit services be continually monitored and should not exceed 70% of the average audit fee over the prior three-year period; – The total amount paid to the External Auditor in 2017 was £1,766k (2016: £1,697k). Payments by the Group for both audit and non-audit services provided in 2017 and 2016 are further detailed in note 2.4 to the financial statements; and – The Policy Standard also regulates the appointment of former audit colleagues to senior finance positions in the Group. This policy is reviewed at least annually and was refreshed during 2017.
Following the Committee's review of the effectiveness of the external audit process and the assessment of the External Auditor's independence and objectivity, it has recommended to the Board the reappointment of EY as the Group's External Auditor for recommendation to and approval by shareholders at the 2018 AGM.	
The External Auditor, the Senior Statutory Auditor and The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014	– EY has been the External Auditor for Clydesdale Bank PLC and other Group entities since January 2005. EY was appointed as the Company's External Auditor on 14 January 2016 following an audit tender, shortly before the Company became the holding company of the Group and for the initial period post the demerger and IPO in February 2016, however, the Committee recommended that this be kept under review; – The Group has no current retendering plans. The Committee undertook a competitive tender of the audit of the Group in early 2015. In applying the CMA's requirements, the next mandatory tender would be in respect of the 2026 financial year; – During the year, Steven Robb succeeded George Reid as the Senior Statutory Auditor and EY will continue to practice the rotation of the Senior Statutory Auditor responsible for the Group audit at least every five years, and all other audit partners and audit senior management will be required to rotate at least every seven years; – The Committee continues to follow developments in the reform of the external audit regulations and the UK and European requirements on publicly listed banking groups; and – The Committee confirms that the Group has complied during the period of financial review and to the date of this report with The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014, which relates to the frequency and governance of tenders for the appointment of the External Auditor and the setting of a policy on the provision of non-audit services.

Risk Committee report

“The Risk Committee has developed its role in supporting a strong and effective risk culture which drives customer centricity.”

Dear shareholder,

As Chair of the Risk Committee, I am pleased to present the report from the Committee for the year ended 30 September 2017. I became the Chair of the Committee on 11 January 2017, having been a member since 1 July 2016. I would like to thank Richard Gregory, my predecessor as Chair, for imparting his knowledge and insight to me as incoming Chair.

Highlights in 2017

During the year, there have been a number of key priorities upon which the Committee has focused to enhance both its effectiveness and role. In particular, the Committee has assessed how best it can support a strong and effective risk culture which drives customer centricity.

The Committee has continued to direct the enhancement of the Group's RAS and associated metrics to better align with the strategic planning process, with particular focus on defining the risk appetite for conduct risk and operational resilience. It continued to consider stress and scenario analysis to provide comfort on the Group's ability to mitigate potential risks.

The Committee developed its view and understanding of top and emerging enterprise-wide risks as agreed by the Executive Leadership Team and the Board, which represent the most significant risks to the achievement of the Group's current business plan and strategy and/or could result in material financial, reputational or regulatory impact. The Group continues to operate in an environment subject to considerable change and during the year the Committee has been proactive in its review, oversight and challenge of risks arising from headwinds such as the recent political events, specifically the outcomes of the UK general election and the commencement of Brexit negotiations following the EU referendum and wider geo-political risks which have led to increased economic and political uncertainty. In addition, there has been focus on a number of high profile cyber security breaches during the last few years at other UK corporates such as the recent WannaCry incident in May 2017, given the importance of digital capability to the Group's strategic focus and enhancing the Group's enabled omni-channel offering to customers. The potential impact to the Group's business from various mandatory regulatory developments such as fulfilling the requirements of the General Data Protection Regulation (GDPR), Payment Services Directive 2 (PSD2), MiFID II; ring fencing and any changes due to regulatory capital requirements as a result of the BCBS are also topical and subject to ongoing consideration by the Committee.

Following his appointment in September 2016, the new Group Chief Risk Officer, Mark Thundercliffe reviewed the Group's RMF and Three Lines of Defence Model and the Committee monitored the enhancement and embedding of these arrangements.

The following report sets out the principal risks and areas of emerging risk the Committee evaluated over the year. More details on the wider risk profile and the RMF that the Committee oversees can be found in the Risk overview within the Strategic report on pages 18 to 19 and in the Risk report on pages 127 to 175.

Committee performance evaluation
The independent, externally facilitated Board performance evaluation carried out during the year included an assessment of the Committee's effectiveness. Overall, the Committee was assessed as effective. Further details are provided in the Committee report.

Looking ahead
The Group has made significant advances this year towards its delivery on executing its three-year strategic plan to establish itself as the UK's leading full service challenger bank. In support of the Group's strategy, the Committee will closely scrutinise developments and any impact on the RAS.

Clive Adamson
Chair, Risk Committee

Risk Committee report

Membership and meetings

The current members of the Committee are:

Clive Adamson, Chair

David Bennett

David Browne

Paul Coby

Fiona MacLeod

Tim Wade

The Committee comprises six Independent Non-Executive Directors who have a variety of industry backgrounds, including banking and financial services. Membership of the Committee has been designed so that there is a deep understanding of the risk management, banking and financial sector expertise it needs to fulfil its responsibilities. Paul Coby and Fiona MacLeod joined the Committee on 30 December 2016 bringing valuable insights into IT risk and strategic change, risk and control, respectively. In addition to the Committee members, the Chairman, Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, Group Chief Risk Officer, Company Secretary, Group General Counsel, and Group Director Internal Audit are invited to attend Committee meetings. The Chair is also a member of the Audit Committee.

Committee attendance

The core activities of the Committee were carried out in six scheduled meetings of the Committee. Two additional *ad hoc* meetings were arranged for decisions required outside scheduled meetings. The table below shows the Committee members during the year ended 30 September 2017 and their attendance at scheduled Committee meetings.

	Number of scheduled Committee meetings eligible to attend	Number of scheduled Committee meetings attended
Committee Chair		
Clive Adamson	6	6
Committee members		
David Bennett	6	6
David Browne	6	6
Paul Coby(1)	4	4
Fiona MacLeod(2)	4	4
Tim Wade	6	5(3)
Former Committee members		
Richard Gregory(4)	2	2

(1) Paul Coby was appointed as a Committee member on 30 December 2016
(2) Fiona MacLeod was appointed as a Committee member on 30 December 2016
(3) Unable to attend the meeting due to a prior business commitment
(4) Richard Gregory retired as a Committee member on 10 January 2017

Committee role and responsibilities

During the year, the Committee revised its Charter which sets out the role and responsibilities of the Committee. The Charter of the Committee can be found on the Company's website www.cybg.com/about-us/corporate-governance/.

Committee performance evaluation

The Committee's performance was reviewed as part of the independent, externally facilitated Board performance evaluation during the year which included an assessment of the Committee's effectiveness. Overall, the Committee was assessed as effective. In common with the Audit Committee, the key area for development related to ensuring that the Charters for the Risk and Audit Committees were reviewed to mitigate duplications and overlaps. This was an action already identified by both Committees.

Following Clive Adamson's appointment as Chair of the Committee, he set out his priorities for the Risk Committee and these priorities have been incorporated into the Committee's annual work plan and will inform the Committee's agenda throughout the coming year.

Matters considered and actions taken by the Committee

The significant matters addressed by the Committee during the financial year ended 30 September 2017 and in evaluating the 2017 Annual Report and Accounts are described in the following pages.

Role of the Committee	Key matters considered and actions completed
Enhancing the RAS and stress testing *Reviewing and approving the Group's risk appetite*	– Conducted six-monthly reviews and recommended any updates to the Board for approval of the RAS taking into consideration the strategic objectives and target business model of the Group as well as the environment in which it operates; – Reviewed regular reports of performance against each RAS measure, and assessed and confirmed the adequacy of management actions in relation to actual or potential breaches of Red and Amber RAS thresholds; – Fully refreshed the statements of appetite and limit settings for the material sources of risk during the year; and – Requested and reviewed deep-dive analysis on a variety of risk matters including: 'B' post implementation review, customer funding gap, and IT.
Reviewing the ICAAP and ILAAP and recommending approval to the Board	– Reviewed and monitored the capital, funding and liquidity profile through the ICAAP and ILAAP processes.
Embedding the risk framework and governance *Providing oversight and reviewing the application of the Group's risk management, compliance and control systems*	– Reviewed and approved proposals to enhance the RMF; – Reviewed and approved an updated Policy Management Framework which provides the overarching principles and minimum control requirements that operate across the Group to mitigate risks to within the Group's risk appetite; – Received updates in relation to the Group's IRB application to the PRA and ongoing compliance; – Considered an annual review of the Group's anti-money laundering and counter-terrorist policy, systems and controls; and – Reviewed the policies and procedures for preventing and detecting fraud and bribery.
Supporting an effective risk culture Ensuring that all colleagues operate in line with the Group's risk focused culture	– Continually assessed risk culture, including considering risk events and undertaking root cause analysis; – Developed financial risk measures for bonus and long term incentive plan (LTIP) with the Remuneration Committee for 2018; – Recommended the levels of alignment of remuneration to risk performance; and – Considered any risk adjustments to be taken into account by the Remuneration Committee when making remuneration decisions for 2017 and 2018.
Risk management Overseeing the risk profile and risk management of the Group within the Board approved RAS	– Reviewed and challenged regular reports from the Group Chief Risk Officer that considered matters of concern on the material sources of top and emerging risks to the Group (see the following pages) and outlined the remedial activities initiated to ensure that the risk was brought within risk appetite; – Reviewed and challenged regular reports from the Chief Financial Officer to manage the risks related to Funding, Liquidity and Capital; – Approved the annual Three Lines of Defence Oversight and Assurance Plans and received regular updates on the adequacy and effectiveness of the application of the risk and control framework; – Received updates on the output of assurance activities from the Three Lines of Defence regarding internal control processes for risk management; – Carried out an assessment of the Viability Statement in the draft 2017 Annual Report and Accounts and advised the Board and Audit Committee to that effect; and – Alongside other risk categories, the Committee oversaw Conduct Remediation Programmes ensuring that they deliver the right outcomes for our customers.

Risk Committee report

As part of the RMF, during the year the Committee maintained oversight of the following identified principal risks and associated top and emerging risks:

Principal risk	Examples of Risk Committee consideration
Credit risk The risk of loss of principal or interest stemming from a borrower's failure to meet contracted obligations to the Group in accordance with the terms agreed. Credit risk is evident at both a portfolio and transactional level.	– The Committee reviewed regularly the performance of the credit risk portfolio, including segmentations alongside changes in the economic environment to ensure that concentration risks were minimised. An area of particular focus and attention is the Group's mortgage portfolio spread and the level of concentration of mortgage lending. **Emerging risk – *Macroeconomic environment***. The impact of the sustained low interest environment places increased pressure on NIM and conversely, a sharp rise in interest rates leads to an increased risk of default rates and credit losses. **Emerging risk – *Consumer credit***. Maintaining awareness of the risk of significant unforeseen credit losses occurring within a short time period which has the potential to have a detrimental impact on earnings and profitability.
Balance sheet and Prudential regulation risks This covers a number of categories of risk which, combined, affect the manner in which the Group can support its customers in a safe and sound manner	– The Committee monitored closely the Group's funding position giving due consideration to any additional risks arising from increased market uncertainty following changes in the macroeconomic environment, including the triggering of Article 50 and subsequent Brexit negotiations which continue to create significant economic uncertainty for the UK; and – At each meeting the Committee considered a report from the Treasurer which provided an update on the Group's exposure to balance sheet and prudential regulation risks.
Regulatory and compliance risks This consists of regulatory strategy and change risk, regulatory relationship risk and the risk of failing to understand and comply with relevant laws, regulations, licence conditions, supervisory requirements, industry codes of conduct and voluntary initiatives.	– The Committee obtained frequent briefings from management on forthcoming regulatory developments and upstream risk, to allow members to consider and oversee the implications of these on the Group's strategic objectives and operations, systems and controls; – Regular updates were received by the Committee from the Group Chief Risk Officer on progress made towards achieving IRB accreditation; and – The Committee reviewed regular reports detailing how regulatory changes were being integrated into business strategic execution (see emerging risks below). **Emerging risk – *Regulatory capital requirements*** – Changes to regulatory capital requirements due to the BCBS consultation on changes to the standardised approaches for calculating credit risk and operational risk. **Emerging risk – *Banking reform, ring fencing and resolution*** – Regulatory authorities in the UK and Europe have proposed reforms to certain aspects of banking sector regulation including ring fencing requirements and MiFID II. **Emerging risk – *Use of data*** – The EU Commissions General Data Protection Regulation (GDPR) is to be introduced from 25 May 2018 meaning the Group will be subject to increased regulatory burden when processing customer, colleague and other data and may be subject to increased sanctions for breach.
Conduct risk Defined as the risk of treating customers unfairly and/or delivering inappropriate outcomes resulting in regulatory fines, compensation, redress costs and/or reputational damage.	– Through the execution of the Group Conduct Strategy, the Committee oversaw the pro-active review of the business for potential conduct issues; – The Committee monitored progress to remediate key legacy conduct issues throughout the year, including PPI and other remediation programmes; – The Committee received regular updates on the implementation and effective execution of the Group Conduct Strategy including the bi-annual Conduct Framework assessment, This included review of product governance outcomes, obtaining assurance that product design and execution continued to deliver fair outcomes to customers; and – The Committee oversaw performance against Conduct Risk Appetite including the introduction of additional and enhanced Conduct-related RAS measures and approved a new Conduct Risk Policy Statement.

Principal risk	Examples of Risk Committee consideration
Operational risk The risk of loss resulting from inadequate or failed internal processes and systems or from external events.	– The Committee reviewed the current and target approaches to change management to ensure that the Operational risk elements inherent in the Group's strategic plans were being effectively mitigated. This included the oversight of the effectiveness of actions to exit remaining TSAs with NAB. **Emerging risk – *Geopolitical uncertainty.*** The outcome of the EU referendum and subsequent triggering of Article 50 has created a period of economic uncertainty for the UK.
Financial crime risk The risk that the Group's products and services will be used to facilitate financial crime against the Group, its customers or third parties.	– The Committee maintained oversight of the effectiveness of the Financial Crime Framework for monitoring, management and mitigation of financial crime and considered reports on the strength of the Group's cybercrime defence strategy. – **Emerging risk – *Cybercrime*.** There is a risk that the Group is unable to keep pace with the increased threat of cybercrime that digital expansion presents.
Strategic, business and financial performance risk The risk of significant loss, loss of earnings and/or damage arising from business decisions that impact the long-term interests of stakeholders or from an inability to adapt to external developments.	– The Committee reviewed a consolidated report outlining the triggers and exposure to strategic risk by the Group Chief Risk Officer. **Emerging risk – *Payment Services Directive 2 (PSD2)*** – A directive of the European Parliament, the rules of which will apply from 13 January 2018, which aims to further develop a better integrated internal market for electronic payments within the EU, and which the Group will be required to comply with.
People risk The risk of not having sufficiently skilled and motivated colleagues who are clear on their responsibilities and accountabilities and who behave in an ethical way.	– The Committee provided oversight of people risks which included the ability to manage change, the availability of management resources against plan, and the culture embedded across the Group.

Further details on the Group's approach to risk appetite, risk culture, the RMF, and significant and emerging risks can be found in the Risk report beginning on page 127.

Statement by the Chair of the Remuneration Committee

“The Committee continues to ensure the Group’s remuneration arrangements support delivery of its strategic priorities for 2018 and onwards.”

Dear shareholder,

As Chair of the Remuneration Committee, I am pleased to present the Group’s Directors’ remuneration report, including details of the Directors’ and Non-Executive Directors’ pay, for the year ended 30 September 2017.

Our Directors’ remuneration policy was approved by shareholders in 2017 and no changes to the policy are proposed for 2018. This statement and the accompanying report demonstrate the framework in which decisions have been made, the outcomes for the 2017 performance year and how the Committee plans to approach the year ahead.

2017 review

Overall, 2017 has been a very strong year and the Group has maintained momentum in delivering against its strategic priorities. These priorities and commitments remain unchanged, providing sustainable customer growth, efficiency and capital optimisation delivered by a strong customer-focused culture, all within a framework of prudent risk management and governance. This purpose is once again reflected in our remuneration arrangements and is supported by the implementation of our remuneration policy for 2018 and onwards.

Underlying profit is up 33% year on year and 15% ahead of the target. Underlying CIR has improved by 7% from 74% to 67% notwithstanding the additional costs associated with our first full year since the IPO.

Overall underlying costs for the year of £675m were below our target of £690m–£700m. Balance sheet growth continued based on a prudent risk appetite with customer loans increasing by 6.0% as mortgage balances increased by 7.5% and core SME balances grew by 5.9%.

Following the success of the demerger and IPO, we embarked on a programme of significant transformation. That activity has been far reaching and had a personal impact on many colleagues. 2017 saw our colleague engagement fall to 72%, a decrease of 7%. When compared with a score of 79% last year, the results show a decline across a number of categories. When we compare ourselves to other organisations going through similar levels of transformation (known as the Transitional Companies norm), our engagement is more in line with this norm and significantly ahead on half of the survey categories. In fact despite the overall decline, many of our scores remain strong.

As detailed in the Annual report on remuneration, the substantial majority of both financial and non-financial targets set by the Committee for the 2017 bonus were exceeded. However, as the customer metric (NPS) and colleague engagement scores underperformed the Committee exercised their discretion to reduce the element of bonus linked to business performance and therefore determined that a bonus of 82% of salary be paid to the Chief Executive Officer (CEO), Chief Financial Officer (CFO) and Chief Operating Officer (COO).

The Group has also devoted significant effort into enhancing its credibility and relationships with key external stakeholders across the business, regulatory and government spectrum.

Considerations for the year ahead

The Committee will continue to operate within the existing approved Directors' remuneration policy in 2018 and will continue to focus on ensuring the remuneration policy remains in line with the market and compliant with regulatory requirements. Our continuing strategy will align the interests of the Executive Directors and shareholders. Given the continuing uncertainty over the exit of the UK from the EU, the unexpected outcome of the June general election for the UK Government and the relatively high inflation figures in comparison with previous years, the Committee will also focus on ensuring the Group is able to attract, retain and motivate key talent at all levels of the organisation, in a challenging market.

Working within the policy framework, the Committee has undertaken a review of the Group's remuneration arrangements and in particular the performance measures of our incentive plans to ensure they are aligned with the Group's business strategy and reward for the delivery of key strategic objectives.

Executive Directors salaries

It is the Committee's intent that Executive Director salary increases remain aligned to those applied to colleagues generally across the Group. However, as per our remuneration policy, the committee reserves the right to provide increases that are greater than those applied across the Group where there is a strong rationale to do so.

As last year, the CEO and COO salaries will remain unchanged in 2018. The CFOs salary will increase by 8.75% to £500,000 from 1 October 2017. This change reflects the new status of the role as a FTSE 250 PLC CFO and the importance of the role in driving the performance of the business.

Pay and employment conditions of other colleagues in the Group were taken into account when considering these outcomes. Building an improved colleague proposition across CYBG has been a key area of focus in 2017 and improvements have included consolidated pay increases, enhanced defined contribution pension provision and the introduction of a flexible benefits account worth up to 5% (capped at £2,500) of salary from 1 January 2018 for all colleagues below Executive Director.

Variable pay

The Committee will set appropriate and stretching annual variable reward targets for the year ahead based on the Group's key financial, risk, customer and culture objectives. The Remuneration Committee is committed to providing transparency in decision making in respect of the Group's incentive plans. It will disclose targets and measures; together with information relating to performance against those targets within the Annual report on remuneration for the relevant year, except to the extent that the Board deem these to be commercially sensitive, in which case it will disclose this information once it is deemed not to be sensitive.

The new LTIP award for our executives, awarded in respect of performance in the financial year ended 30 September 2017, is subject to a three-year performance period (1 October 2017 to 30 September 2020) and a three to seven year deferral period. This ensures a significant proportion of Executive Directors' remuneration continues to be deferred. This, together with the fact that a large proportion of short-term incentive is deferred and delivered in shares, ensures that Executive Directors' remuneration is aligned with the achievement of our long-term strategy and the long-term interests of shareholders. Details of the performance measures and targets for the LTIP award to be granted in respect of 2017 are provided on page 111.

Details of the performance measures for the 2018 annual incentive (bonus) are detailed on page 108. However, for reasons of commercial sensitivity, the specific targets for each measure will not be disclosed until the end of the 2018 performance period, when performance against the targets will also be disclosed.

Consideration of shareholders' views

Shareholders have an essential role to play in guiding responsible pay practices. The Committee received feedback from our major shareholders ahead of the 2017 AGM, and took account of these views when formulating the final development of our policy, which was reflected in the high levels of support for resolutions relating to remuneration.

On behalf of the Board, I am pleased to recommend this statement to shareholders, ahead of the 2018 AGM.

Adrian Grace
Chair, Remuneration Committee

This report has been prepared in accordance with Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 as amended in 2013, the provisions of the UK Corporate Governance Code (the 'Code') and the Listing Rules.

On behalf of the Board

Adrian Grace
Chair, Remuneration Committee

20 November 2017

Directors' remuneration report

Remuneration Committee

Purpose and membership of the Remuneration Committee

The Committee is responsible to the Board for overseeing the Directors' remuneration policy ensuring that the Group complies with its regulatory requirements and is able to recruit, retain and motivate its senior colleagues and reward their individual contribution to the Group in line with the Group's risk appetite. Under the Committee's Charter the key roles and responsibilities of the Committee are to:

- develop the Group's remuneration strategy and policy for all colleagues, including Executive Directors, for approval by the Board;
- ensure the Directors' remuneration policy has regard to the risk appetite of the Group and aligns with its long-term success;
- ensure there are measures in place to avoid potential conflicts of interest in the design of incentive arrangements to ensure the interests of customers, colleagues, shareholders and other stakeholders are aligned;
- submit the Directors' remuneration policy, at least every three years, to a binding vote of the Group's shareholders, consider and, where appropriate, respond to feedback received from shareholders through that process;
- determine the overall parameters for variable pay arrangements for colleagues, members of the Executive Leadership Team and Executive Directors;
- determine the remuneration in respect of the Chairman and members of the Executive Leadership Team;
- consider, and approve, the list of Material Risk Takers (MRTs);
- monitor the remuneration arrangements of all MRTs in line with the PRA Remuneration Code; and
- approve annually the formal Group's PRA Remuneration Policy Statement (RPS) required under the PRA Remuneration Code.

The Committee reports to the Board on its activities and makes recommendations, where required by charter, all of which have been accepted during the year.

Remuneration Committee membership in 2017

All members of the Committee were independent Non-Executive Directors who serve on the Committee for a minimum three-year term and a maximum of six years. The Committee is chaired by Adrian Grace and it held five scheduled meetings during the financial year. Three *ad hoc* meetings were arranged for decisions required outside scheduled meetings.

The table below shows the Committee members during the year to 30 September 2017 and their attendance at scheduled Committee meetings.

	Number of scheduled Committee meetings eligible to attend	Number of scheduled Committee meetings attended
Committee Chair		
Adrian Grace	5	5
Committee members		
David Bennett	5	5
David Browne	5	5
Jim Pettigrew	5	5

By invitation other attendees will include: the Chief Executive Officer; the Group Human Resources Director; the Head of Reward and Pensions and the Chief Financial Officer, except when issues relating to their own remuneration are being discussed. PricewaterhouseCoopers (PwC) LLP (the Committee's independent remuneration adviser) also attend meetings where invited. The Company Secretary attends meetings to record minutes.

In addition, representatives from the Risk Committee may attend where appropriate to provide the Remuneration Committee with detailed risk assessments.

Committee performance evaluation

The Committee's performance was reviewed as part of the independent, externally facilitated Board performance evaluation during the year which included an assessment of the Committee's effectiveness. Overall the Committee was assessed as effective.

The key areas for development related to continuing to evolve its role consistent with best practice for listed company remuneration committees particularly by refreshing the approach to setting out the Committee's objectives and priorities for the year to ensure its responsibilities are addressed in the most effective manner and formalising the reporting to the Committee from the Risk Committee.

Key matters considered by the Committee during 2017

During the year, the Committee considered, among other matters, the following:

Role of the Committee	Key matters considered	Actions taken
Fixed and variable pay issues	– 2017 short and long-term incentive arrangements	– Considered and approved 2017 discretionary incentives, performance measures and structures for delivery
	– 2017 total remuneration outcomes	– Approved variable remuneration awards for Executive Directors, other senior management, MRT and all colleagues for 2017 financial year – Approved the release of deferred bonus awards
	– Legacy NAB awards	– Considered approach to legacy NAB awards and recommended no change
	– All colleague 2017 pay mandate	– Considered all colleague pay and executive pay arrangements. Recommended change to CFO base salary
	– Chairman's fee	– Considered external market insight and recommended no change
	– MRT termination and commencement awards	– Considered all commencement awards and termination payments – Delegated authority to approve awards and release payments below a de minimis level to Group Human Resources Director and CEO
Governance, risk and other matters	– MRTs	– Reviewed and approved changes and confirmed MRT throughout the year
	– Regulatory developments	– Considered regulatory remuneration requirements and approved compliance review
	– Remuneration policy	– Approved the CYBG remuneration policy ahead of the AGM
	– 2016 risk adjustments	– Approved the Group's approach to risk and control adjustments for incentive arrangements and periodic review thereof – Formalised role of Board Risk Committee and Board Audit Committee
	– 2016 performance assessment (CEO, CFO, COO & LT)	– Reviewed Executive Director and senior leadership team individual scorecards
	– Scheme rules and terms of the DEP & LTIP	– Approved the terms of the DEP and LTIP plans for 2017 and 2018
	– Annual remuneration disclosures	– Approved the submission of the remuneration policy statement to the PRA and FCA – Approved the 2017 Directors' remuneration report including Pillar 3 requirements
	– Investors and regulator feedback	– Considered investor feedback and AGM outcomes and any impact on future structure of Executive Directors' remuneration

Remuneration Committee continued

Role of the Committee	Key matters considered	Actions taken
	– Pension arrangements	– Considered the closure of the Group's defined benefit pension scheme to future accrual and approved retirement arrangements for COO.
	– Remuneration Committee adviser review	– Considered performance of PwC LLP and confirmed continued engagement.
	– Terms and conditions for Executive Leadership Team	– Approved changes to contract terms for notice periods.
	– Remuneration Committee effectiveness	– Considered independent assessment of Committee effectiveness and approved recommendations.

Advisers to the Committee

Following a selection process carried out by the Remuneration Committee prior to the IPO of the Group, the Committee engaged the services of PwC as independent remuneration adviser. During the financial year, PwC advised the Committee on all aspects of the Directors' remuneration policy for members of the Executive Leadership Team. PwC also provide professional services in the ordinary course of business including assurance, advisory, tax and legal advice. The Committee is notified of other remuneration work that is undertaken by PwC. In addition, there are processes in place to ensure no conflict of interest exists in the provisions of these services.

PwC is a member of the Remuneration Consultants Group, whose voluntary code of conduct is designed to ensure objective and independent advice is given to remuneration committees. Fees of £139,000 excluding VAT (2016: £93,000 in respect of the eight-month period from the IPO to the year end) were paid based on time spent on advice provided to the Remuneration Committee in respect of Directors' remuneration for the financial year.

Statement of voting at general meeting

Prior to the IPO, the Group's sole shareholder was NAB and there is therefore no prior historic voting information prior to this date. The proposals in relation to the Group's remuneration policy and the remuneration offered to the Executive Directors in 2017 were detailed within the Directors' remuneration report for 2016 and were voted on at the AGM on 31 January 2017. The shareholder votes submitted at the meeting, either directly, by mail or by proxy, were as follows:

	Votes for		Votes against		Votes withheld
	Number of shares	% of votes	Number of shares	% of votes	Number of shares
Directors' remuneration policy	594,488,715	99.23%	4,592,820	0.77%	1,524,064
Directors' remuneration report	588,279,591	98.89%	6,602,277	1.11%	5,719,654
CYBG Long Term Incentive Plan	592,635,707	98.93%	6,437,433	1.07%	1,510,537
CYBG Deferred Equity Plan	596,602,161	99.59%	2,430,299	0.41%	1,546,891

Directors' remuneration policy – abridged

At a glance – Executive Directors' remuneration structure in 2018 summary

For the 2018 performance year the annual incentive award (bonus) will be up to 100 percent of base salary, with measures described on page 108. Executive Directors will also be eligible to receive an LTIP award of up to 100 percent of base salary in respect of the 2018 performance year. The level of LTIP vesting will be based on performance measured over the 2019-2021 period, with targets disclosed in next year's annual report. In combination, bonus and LTIP will not exceed the regulatory 2:1 ratio between variable to fixed pay.

2018 2019 2020 2021 2022 2023 2024 2025 2026 2027	Implementation for 2018
Base salary	– David Duffy – £1,000,000 (unchanged from 2017). – Ian Smith – £500,000 (increased for 2018). – Debbie Crosbie – £450,000 (unchanged from 2017).
Benefits and allowances	– Benefits and allowances include pension, car, medical cover life assurance arrangements and where applicable relocation. – David Duffy – £236,000 (Accommodation allowance ceased 2017). – Ian Smith – £105,000 (increases relative to salary). – Debbie Crosbie – £91,000 (Pension cash allowance for 2018).
FY18 Annual incentive (bonus) Performance period (2018); Awarded (50% in shares 50% cash) (2019); Vesting (2022); Potential share deferral and phased vesting (2023–2027)	– Maximum 100% of base salary and linked to the delivery of 2018 business strategy. – At least 50% delivered in shares. – Delivered in December after the year end. – Part of the bonus may be deferred to ensure that, in combination with the LTIP award, regulatory requirements for deferral are met.
FY18 Long term incentive plan (LTIP) Awarded (2019); Performance period (2019–2021); Vesting (2022); Deferral and phased vesting (2023–2027)	– Maximum of 100% of base salary and linked to the delivery of business strategy over the years 2019 to 2021. – It is expected that awards will be granted in December following the year end. – Award deferred for a total of seven years, with vesting in equal tranches over years three to seven.

→ Award subject to 12 month holding period in line with regulatory requirements.

Policy and principles

The current Directors' remuneration policy approved by shareholders at the AGM on 31 January 2017 remains in force. The Committee will consider the remuneration policy annually to ensure that it remains aligned with business needs and is appropriately positioned relative to the market. There is no intention to revise the policy more frequently than every three years, unless amendments to the policy are required in the interim, in which case appropriate shareholder approval will be sought.

An abridged version of the policy which includes the remuneration tables for Executive and Non-Executive Directors is included in the following pages for reference. This does not replace or override the full approved policy which is available on pages 106–115 of the 2016 Annual Report and Accounts available at: www.cybg.com/investor-centre/annual-reports/

Details on how the policy will be applied in 2018 are included on pages 108 to 109 of the report. In applying this policy the Group remuneration approach remains to:

– provide competitive, transparent and fair rewards, benefits and conditions;
– reward achievement of short- and long-term individual objectives and business strategy;
– align the interests of colleagues and shareholders through colleague share ownership;
– deliver outcomes over short- and long-term horizons with appropriate performance and risk adjustments, ensuring performance assurance principles are applied;
– support the RMF with regard for the risk appetite of the Group; and
– attract, recognise, motivate and retain high performers.

Remuneration arrangements are fully compliant with, and will be operated in line with, all regulatory requirements, including the PRA Remuneration Code and are in line with UK listed financial services sector best practice.

Directors' remuneration policy – abridged continued

Our peer group companies
The CYBG comparator peer group was reviewed by the Committee and is defined as other UK-based banks and wider financial services firms of a comparable size, divisional heads in larger UK banks and other FTSE companies reflecting our market capitalisation.

Elements of package – fixed remuneration
The policy in relation to each element of Executive Directors' remuneration is set out in the following tables.

Base salary

Purpose and link to strategy	Recruit, reward, retain and recognise leadership position and responsibility for delivering strategy.
Operation	Base salaries are paid in 12 equal monthly instalments during the year and are reviewed annually. Any changes are effective from 1 January. When determining and reviewing base salaries, the Committee considers: – Group and individual performance; – the skills, experience and responsibilities of the Executive Director and their market value; – the scope and size of the role; – base salary increases for colleagues throughout the Group; and – external benchmarks data for peer banks, the divisional heads of larger UK banks and FTSE data reflecting our market capitalisation.
Maximum potential	The Committee will seek to limit pay increases for Executive Directors, where there is no change in role, to those applied to colleagues generally across the Group. However, where an Executive Director is relatively new in role the Committee reserves flexibility to provide increases that are greater than those applied across the Group to bring the individual's salary into line with the market and reflect the gaining of experience.
Other colleagues	The approach takes into account affordability, economic factors, external market data, business and personal performance.

Pension

Purpose and link to strategy	Recruit, reward, retain key talent and contribute towards individuals funding for retirement.
Operation	Executive Directors are entitled to participate in the Group defined contribution pension scheme or may receive a cash allowance in *lieu* of some, or all, of the employer pension contribution. The Group's defined benefit pension scheme is only available to existing members.
Maximum potential	The maximum cash allowance for Executive Directors will be set at 20% of an Executive Director's base salary. Contributions to the Group's defined benefit pension scheme are capped by reference to the Scheme earnings cap. Only one Executive Director was a member of the Group's defined benefit scheme during 2017 and they ceased to accrue benefits from 31 July 2017 in line with other colleagues.
Other colleagues	All new colleagues are automatically enrolled in the Group's defined contribution pension scheme. The defined benefit scheme closed to new entrants in 2004 and closed to the future accrual of benefits for the majority of colleagues from 31 July 2017.

Benefits

Purpose and link to strategy	To provide benefits consistent with role.
Operation	The Group provides a range of benefits which can include private medical insurance, health assessments, life assurance and car allowance/car. The Committee retains the discretion to provide additional benefits as may be reasonably required. These may include relocation benefits such as (but not limited to) accommodation, family relocation support and taxable travel. The Executive Directors are entitled to a maximum of 30 days holiday in addition to applicable bank/public holidays.
Maximum potential	The CEO has a cap of £250,000 on his benefits, including pension contributions and any cash allowance in lieu of pension contributions. For the other Executive Directors, the maximum value of benefits is set by the nature of the benefits and the cost of providing them.
Other colleagues	The Group provides a range of benefits based on colleagues' roles, which include private medical insurance, health assessments, life assurance and car allowance/car. Colleagues receive between 25 and 30 days' holiday annually depending on their role.

Elements of package – variable remuneration

Bonus	
Purpose and link to strategy	The annual bonus is designed to reward Group and personal performance in line with strategic objectives.
Operation	Annual bonuses are discretionary and are based on Group and individual performance within the year. The measures, their weighting and targets are set annually with awards determined by the Committee at the end of the financial year. The annual bonus may be delivered in cash and shares, which, in combination with the LTIP awards and any relevant awards under the all-employee Share Incentive Plan (SIP) will be structured in line with the requirements on the deferral of variable pay under the PRA Remuneration Code. The equity-based element of the award will be made as rights to CYBG shares or other instruments, which are released at the end of the required holding period. The mechanism for making these awards will be the Deferred Equity Plan (DEP). The amount and deferral period for bonus will be determined in line with regulatory requirements and to the extent that the LTIP award does not fully meet the deferral requirements. Dividends or dividend equivalents accrued on deferred annual bonus shares are paid on vesting, subject to the extent permitted under the relevant remuneration regulations. Discretion may be exercised by the Committee to ensure that the bonus outcomes are a fair and accurate reflection of the business and individual performance and consider any risk-related issues (but may not exceed the maximum opportunity). The Group can, in specific circumstances, apply malus and/or clawback to all or part of any bonus award.
Maximum potential	Taken together with the LTIP awards, total variable remuneration is limited by the 2:1 ratio of variable pay to fixed pay, subject to the LTIP award being at least half of the total variable pay award.
Performance conditions	Performance measures are set by the Committee each year and are set out in the Annual report on remuneration, normally this would be: – 80% of the annual bonus opportunity for Executive Directors is based on performance of the Group against key financial and non-financial measures; and – 20% is based on personal performance and behaviours. When determining the outcome of the performance measures, the Remuneration Committee will seek the advice of the Risk Committee to ensure all relevant risk factors are identified and the bonus pool and/or individual awards adjusted accordingly. Specific measures, targets and weightings will be set by the Remuneration Committee annually and disclosed on a retrospective basis.
Other colleagues	All colleagues within the Group are in a single Group-wide scheme with target opportunities ranging from 8% to 50% of base salary depending on role. Awards will be funded from a bonus pool reflecting the same financial and non-financial measures that apply to Executive Directors. When determining the outcome of the performance measures the Remuneration Committee will seek the advice of the Risk Committee to ensure all relevant risk factors are identified and the bonus pool and/or individual awards are adjusted accordingly.

Directors' remuneration policy – abridged continued

Long Term Incentive Plan (LTIP)	
Purpose and link to strategy	Delivery of the Group's strategy and growth in shareholder value.
Operation	Awards are based on a three-year performance period reflecting a basket of business and shareholder measures aligned with strategic goals. Awards will vest a minimum of three years after being awarded, or longer, for example where required by the PRA Remuneration Code. Where a period of deferral extends beyond three years, awards will only be subject to service requirements for the first three years, thereafter awards will only be subject to forfeiture for reasons of gross misconduct or malus. The value of awards for the purposes of determining total variable remuneration will be in line with the rules set by the Regulator. The Committee, in its absolute discretion, will determine the level of the LTIP awards made under the LTIP after taking account of the Executive Director's individual performance and business performance. Any LTIP award, when combined with any deferred element of the annual bonus, will meet the deferral requirements under the PRA Remuneration Code. Malus and clawback also apply to the whole of the LTIP award in line with the requirements of the PRA Remuneration Code. Awards are made as conditional rights to CYBG shares, or other instruments, which will be released at the end of the holding period or later where required under the PRA's Remuneration Code. Dividends or dividend equivalents accrue on the LTIP awards and, to the extent that the award vests, are paid on vesting, subject to the extent permitted under the relevant financial services remuneration regulations.
Maximum potential	Taken together with the bonus award, the total variable remuneration is limited by the agreed 2:1 ratio of variable pay to fixed pay, subject to the LTIP award being at least half of the total variable pay award.
Performance conditions	Service and performance conditions must be met over a three-year period. Measures aligned with strategic goals are proposed for future LTIP awards, including the 2016 awards to be made following the AGM: – Sustainable Customer Growth; – Efficiency; – Capital Optimisation; and – Prudent Risk Management and Governance. The weighting of metrics will be determined before each award and those for the 2017 award are set out in the Annual report on remuneration, with 25% of the maximum vesting for each measure for threshold performance. The measures reflect a balanced approach between financial and non-financial. The Committee has discretion to vary the weighting of performance metrics, or to substitute the metrics over the life of this Directors' remuneration policy. Shareholders will be consulted should the metrics themselves be varied. In determining the outcome, the Remuneration Committee will seek the advice of the Risk Committee to ensure all relevant risk factors are identified and the level of vesting adjusted accordingly.
Other colleagues	Members of the Executive Leadership Team and other senior managers are eligible to participate in the LTIP with awards made solely at the discretion of the Committee.

Shareholding requirement	
Purpose and link to strategy	To align Executive Directors' interests with those of shareholders
Operation Executive Directors	Executive Directors are expected to build up a specified holding of CYBG shares equivalent to a percentage of salary. 60% of the shares vesting (after settling tax and National Insurance liabilities) from CYBG share plans must be retained until the shareholding requirements are met. **Executive Director** / **Shareholding requirement (% of salary)** CEO: 200% CFO and COO: 150% When assessing an Executive Director's shareholding against the requirement, vested awards which are held as rights rather than shares will be included based on the anticipated net number of shares that would be released to the Executive Director at the end of the holding period.
Other colleagues	Additionally, members of the Executive Leadership Team are expected to build up a holding of CYBG shares equivalent to 100% of salary. 50% of the shares vesting (after settling tax and NIC liabilities) from CYBG share plans must be retained until the shareholding requirement is met.

Executive Director	Shareholding requirement (% of salary)
CEO	200%
CFO and COO	150%

Performance measures

The Committee selected the short- and long-term performance measures to ensure an appropriate balance between short and long term strategic goals and aligning the interests of Executive Directors with shareholders. Targets are set each year having regard to the strategic plan and consensus forecasts. Measures and targets for both the bonus plan and LTIP are aligned to the strategic plan and have been approved by the Board.

The Committee may apply discretion, in exceptional circumstances (for example, if there is a major corporate event), to amend or vary targets or the weighting of performance metrics (measures), or to substitute the metrics over the life of this Directors' remuneration policy if these are no longer appropriate to ensure alignment with strategy and any risks within the business. The Committee will consult with the Group's risk management and control functions to ensure changes are appropriate and do not inadvertently encourage irresponsible or inappropriate behaviour. The Committee will consult with shareholders in advance of any change to performance metrics.

The Committee retains discretion to adjust outcomes to ensure these are consistent with corporate performance. The Committee proposes to use the measures described in the Policy Table for the 2016 LTIP award to be made after the AGM and future awards, but will reassess these annually based on the Group's performance and strategy. In determining the 2016 measures, the Committee consulted with major shareholders.

Risk adjustments, malus and clawback

For MRTs, which include the Executive Directors, bonus and LTIP awards may be reduced before they are released (malus) or may be subject to clawback where the Committee determines that an adjustment should apply. Clawback may be applied up to seven years from the award date, or 10 years for those holding a senior management function where an investigation has commenced.

Malus may be applied where: there is evidence of colleague misbehaviour, misconduct, material error, where a colleague participated in conduct which resulted in losses for the Group or they failed to meet appropriate standards; any material failure of risk management at a Group, business area, division or business unit level; if the financial results at a Group, division or business unit level are restated; if the financial results for a given year do not support the level of variable remuneration awarded; or any other circumstances where the Committee consider adjustments should be made. The Committee is supported in this by the Board Risk and Audit Committees and the CYBG Risk function.

Clawback may be applicable where there is reasonable evidence of colleague misbehaviour or material error, or there is material failure of risk management at a Group, business area, division or business unit level.

Other CYBG share plans

The Executive Directors are invited to participate in all-employee share plans on the same basis as other Group colleagues. These plans encourage share ownership, aligning colleagues' interests with those of shareholders and allowing them to benefit from the long-term success of the Group.

The CYBG Share Incentive Plan (SIP) provides for the purchase of shares, in line with HMRC participation level rules, on a monthly basis from gross pay and is also the vehicle used to allow for awards of free or matching shares.

Each Executive Director received 256 free shares following the demerger and the CFO participates in the monthly purchase of shares through the SIP.

If operated in the future, Executive Directors will also be eligible to participate in all employee share plans operated by the Group.

Directors' remuneration policy – abridged continued

Legacy arrangements
Awards granted under the NAB Share Plans were retained by colleagues of the Group following the demerger and IPO on 8 February 2016. Awards remain subject to their existing terms and performance conditions, with service requirements based on employment by Clydesdale Bank PLC.

Detailed below are the rights under the NAB LTIP held by the COO. Neither the CEO, nor the CFO received any NAB LTIP awards.

Debbie Crosbie's NAB LTIP awards	Vesting date	Release date (1)	Performance period (if applicable)	NAB performance rights
FY2013 LTIP	20 Dec 17	20 Jun 18	11 Nov 13 to 11 Nov 17(2)	10,161
FY2014 LTIP	21 Dec 18	21 Jun 19	10 Nov 14 to 10 Nov 18(2)	13,380

(1) Reflects the end of the six months post vesting holding period.
(2) Awards that do not vest at the end of the first performance period will be retested after 12 months.

The level of vesting for these awards is determined by the NAB Board, and in 2017 the NAB Board determined that the 2012 NAB LTIP should be lapsed in full.

The 2013 and 2014 LTIP awards are due to be released in June 2018 and June 2019 respectively, and are based on NAB's relative TSR performance with half measured against the S&P/ASX Top 50 Index peer group and half against a selection of financial companies in the ASX Top 200 peer group. Awards that do not vest at the end of the first performance period will be retested after 12 months.

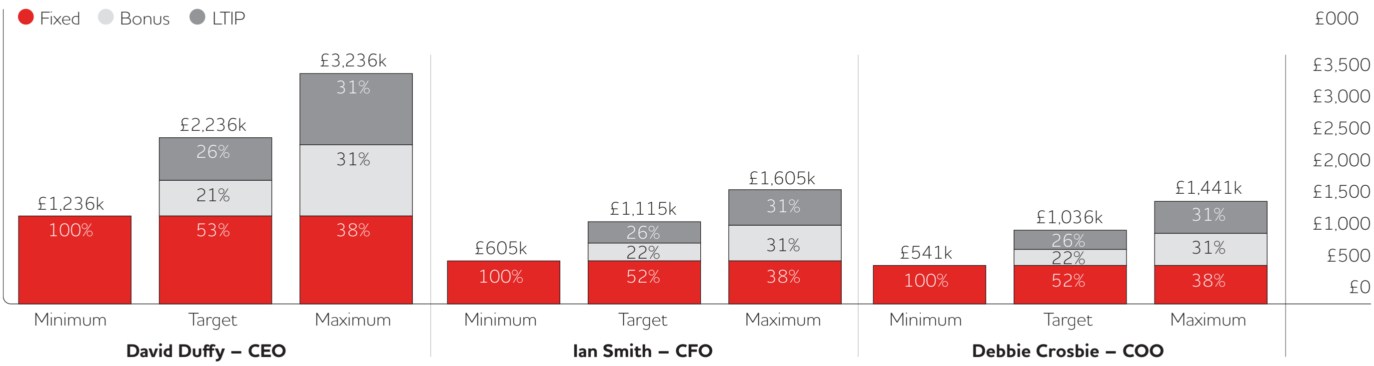
The final decision on the level of vesting will be taken by the NAB Board, with value at the date of vesting included in the Directors single table figure in the year they vest.

Illustration of the application of remuneration policy
The chart below illustrates the potential remuneration of the Executive Directors based on the policy in the following three scenarios:

- minimum remuneration based on fixed elements of package only (salary, pension, benefits);
- target outcome assumes the actual bonus award is 50% of the maximum opportunity with 60% of the LTIP vesting; and
- maximum outcome which assumes the actual bonus award is 100% of the maximum opportunity and 100% vesting of the LTIP.

The amounts do not allow for share price appreciation and do not include dividends or payments in *lieu* of dividends. Salary figures are as at 1 October 2017 and in line with policy the maximum bonus and LTIP awards are 100% of base salary.

Potential 2018 remuneration outcomes



Service contracts and policy on payments for loss of office

Standard provision	Provision	Details
Election	All Executive Directors are subject to annual re-election.	
Notice periods within Executive Directors' service contracts	12 months notice from Company. 12 months notice from Executive Directors.	Executive Directors may be required to work during the notice period, unless determined otherwise.
Confidentiality	Six-month post-termination restrictive covenants	Executive Directors are subject to a confidentiality undertaking without limitation in time, as well as to six-month post-termination restrictive covenants covering: non-competition; non-solicitation of and non-dealing with clients; non-interference with suppliers or contractors and non-solicitation of colleagues.
Compensation for loss of office	Payment in *lieu* of notice of no more than 12 months' salary	Payable monthly and subject to an obligation on the Executive Director to mitigate their loss such that payments will either reduce or cease completely if the Executive Director obtains alternative employment. In the event of redundancy, the Executive Director shall be entitled to receive statutory redundancy pay, together with outplacement and legal support.
Treatment of annual bonus on termination	With the exception of good leavers, where participants leave before 1 December they will not be eligible for an award.	The Committee has discretion to reduce the entitlement of a 'good leaver' in line with performance and the reason for leaving.
Treatment of unvested deferred bonus on termination	With the exception of good leavers awards lapse where participants leave in the three years following the award being made.	Awards to good leavers will be retained in full, with no change to vesting or release dates. With the exception of gross misconduct and malus, service provisions end three years from the date of award.
Treatment of unvested LTIP awards on termination	With the exception of good leavers awards lapse where participants leave in the three years following the award being made.	Awards to good leavers will be prorated, unless the Committee decides otherwise, to reflect the period worked in the three years following the award. The award will vest, unless the Committee decides otherwise, on the normal vesting date to the extent that any performance condition has been met. With the exception of gross misconduct and malus, service provisions end three years from the date of award.
Outside appointments	Executive Directors may accept outside appointments in other listed companies with Executive Directors retaining any fees received.	The Chair is required to approve appointments in advance. Agreement from the Board must be sought before Executive Directors accept any additional Non-Executive roles outside of CYBG. Procedures are in place to ensure that regulatory limits on the number of directorships held are complied with. Details of the directorships held can be found in the biographies section of the Corporate governance report.

Directors' remuneration policy – abridged continued

The Committee retains the discretion to determine whether an Executive Director is to be treated as a good leaver. Unless determined otherwise, an Executive Director will be treated as a good leaver in cases where their employment ends due to death, injury, ill-health, disability, redundancy, retirement, or the company being transferred out of the CYBG Group and any other reason (except for dishonesty, fraud, misconduct or dismissal). The Committee reserves the right to make additional payments where such payments are made in good faith and are required to discharge legal obligations or are due to the breach of such obligations.

The notice periods and dates of their service contracts are shown below.

Executive Directors	Notice period	Date of service contract
Debbie Crosbie	12 months	24 November 2015
David Duffy	12 months	25 November 2015
Ian Smith	12 months	3 December 2015

Considerations of employment conditions elsewhere in the Group

Pay and employment conditions generally in the Group are considered when setting Executive Directors' remuneration. The Committee are provided with regular updates on overall pay and conditions, including negotiated pay increases for the broader colleague population, has oversight of significant changes in the provision of benefits (including pension provisions) and approves the colleague bonus pool.

During the year the Committee considered the following in relation to colleagues below the Executive Directors:

- remuneration packages of Executive Leadership Team members;
- design of the annual bonus plan for Executive Leadership Team and all colleagues;
- measures and targets for the 2017 annual bonus pool;
- salary increases for all colleagues;
- policy in relation to pension plans and the closure of the defined benefit pension plan to future accrual;
- design of the 2017 LTIP and awards to members of the Executive Leadership Team and other Group senior colleagues (based on role); and
- commencement and termination payments made to MRTs.

The Committee does not specifically invite colleagues to comment on the Directors' remuneration policy but any comments made by colleagues are taken into account. Consideration is given to feedback provided by colleagues through the annual engagement survey.

Chairman and Non-Executive Directors' remuneration policy abridged

The table below sets out the Non-Executive Directors' remuneration policy which applies to the Chairman and Non-Executive Directors.

Non-Executive Directors are engaged through letters of appointment which are for an initial period of three years, subject to three-months notice by the Non-Executive Directors or the Group. The Chairman has six months notice. All Non-Executive Directors are subject to annual re-election by shareholders at each AGM and are subject to early termination without compensation if he or she is not reappointed at a meeting of shareholders.

Non-Executive Directors' packages	
Purpose and link to strategy	To ensure the Group is able to engage and retain highly skilled and experienced individuals.
Operation	Fees paid to the Chairman are determined by the Remuneration Committee, while the fees paid to the Non-Executive Directors are set by the Board annually. The fees reflect a base fee with additional fees payable for being members of, or chairing, Board committees and a separate fee is payable to the Senior Independent Director and Deputy Chairman. Non-Executive Directors are appointed for an initial three-year term and will normally serve two terms, exceptionally three. The fees are set at a rate that reflects the value to the Group and expected time commitment given the added regulatory complexity within the financial services sector. In exceptional circumstances, incremental fees may be paid for additional duties and time commitment, to reflect increased workload. From time to time, new Board committees may be established and/or responsibilities distributed between committees, at which point fees for committee membership and Chair may be reviewed. The Chairman and Non-Executive Directors are reimbursed for expenses incurred in performing their duties and any tax arising on such reimbursed expenses is paid by the Group. For individuals based outside of the UK this will include travel to and from the UK. Non-Executive Directors and the Chairman do not participate in any variable remuneration or benefits arrangements.
Maximum potential	The maximum aggregate value of fees payable to the Chairman and the Non-Executive Directors is capped at £2.5m under the Articles of Association.
Performance conditions	There are no performance conditions attached to the fees payable to the Chairman or Non-Executive Directors.

The dates of Non-Executive Directors' letters of appointment are shown below:

Non-Executive Directors	
Clive Adamson	19 May 2016
David Bennett	23 November 2015
David Browne	11 November 2015
Paul Coby	19 May 2016
Adrian Grace	11 November 2015
Fiona MacLeod	8 September 2016
Jim Pettigrew	11 November 2015
Teresa Robson-Capps	11 November 2015
Tim Wade	8 September 2016

Annual report on remuneration

Implementation of the policy in 2018
The following sets out how the Directors' remuneration policy will be applied in 2018:

The remuneration policy will be operated as set out above. In particular:

- the targets for the 2018 annual bonus are considered to be commercially sensitive at this time but will be disclosed along with measures and weightings on a retrospective basis;
- details of the LTIP award for 2017 are set out in the Annual report on remuneration including how they are aligned with our strategic priorities of delivering sustainable customer growth, improving efficiency and capital optimisation and link to our risk and compliance and customer-focused culture objectives;
- salary change for the CFO is intended from the 1 October 2017 reflecting his role since the IPO;
- the annual bonus for Executive Directors for the performance year 2018 will be capped at 100% of base salary;
- the LTIP for Executive Directors for the performance year 2018 will be capped at 100% of base salary;
- Non-Executive Directors fees in 2018 may be reviewed as the Group progresses with its strategic priorities and to reflect any changes in the nature of a Non-Executive Director's role and responsibilities;
- to comply with remuneration regulation changes effective for 2018 the deferral of awards has been extended to between three and seven years; and
- in addition, dividends will not accrue on bonus and LTIP awards made in relation to FY2018 (in line with regulatory requirements). However, the number of deferred bonus shares/LTIP awards granted may be based on a share price discounted by reference to the expected dividend yield over the vesting period.

Base salary	
David Duffy	£1,000,000
Ian Smith	£500,000
Debbie Crosbie	£450,000

Benefits and allowances (including pension)	
David Duffy	£236,000
Ian Smith	£105,000
Debbie Crosbie	£91,000

FY2018 annual bonus	
Opportunity	100% of base salary. In line with policy 80% of the award is based on the performance of the Group against key financial and non-financial measures and 20% is based on personal performance and behaviours. The overall design of the 2018 plan remains unchanged from last year.
Performance measures and targets	The Committee has determined that for 2018 the annual bonus will be based on the following: – underlying financial measures with a weighting of 77% including: - underlying profit before tax (underpin); - customer lending growth; - total costs; - CIR; and - RoTE. – non-financial measures with a weighting of 23% including: - CYBG Retail net promoter score (CB, YB and B); - adoption of our digital channels; and - colleague engagement linked to our annual survey. The Board considers that the targets which apply to these measures are commercially sensitive and as such these will be disclosed alongside the level of payout in next year's implementation report.

FY2017 long-term incentives

Opportunity	100% of base salary.
Performance measures and targets	The Remuneration Committee has again set performance measures based on delivering the company's strategic objectives and containing measures linked to sustainable customer growth, efficiency, capital optimisation, risk and compliance and customer-focused culture. These measures, and their respective targets, are consistent with the strategic plan. The Remuneration Committee has determined that 60% vesting is justified for target performance and 25% is justified for threshold performance.
Vesting terms	The performance period will be the three years commencing 1 October 2017. An assessment of personal performance in the financial year preceding the date of the grant will be taken into account before awards are made. The anticipated date of grant is November 2017. To the extent that the performance conditions are met, awards will vest equally from the third anniversary of the date of grant to the seventh such anniversary. At each vesting date the resultant number of shares (post taxation) will be subject to a twelve-month retention period.

Executive Directors – single total figure of remuneration (audited)

The table below sets out the single total figure of remuneration and breakdown for each Executive Director in respect of the financial year to 30 September.

	David Duffy		Ian Smith		Debbie Crosbie	
£000s	**2017**	2016	**2017**	2016	**2017**	2016
Salary	**1,000**	1,000	**460**	460	**450**	450
Benefits and allowances	**56**	67	**11**	9	**10**	10
Pension and pension allowance [(1)]	**180**	180	**87**	87	**100**	100
Total fixed remuneration	**1,236**	1,247	**558**	556	**560**	560
Annual bonus [(2)]	**820**	800	**377**	368	**369**	360
LTIP vesting in year [(3)]	**–**	–	**–**	–	**–**	–
Other awards [(4)]	**–**	1	**–**	1	**–**	1
Total remuneration	**2,056**	2,048	**935**	925	**929**	921

(1) David Duffy and Ian Smith have both opted out of the Group's defined contribution pension scheme and received a cash allowance in lieu of the Group's pension contributions. Debbie Crosbie was a member of the defined benefit plan until 30 July 17 and then opted out of the Group's defined contribution pension scheme and received a cash allowance. Her pension figure includes both elements with the defined benefits element reflecting the HMRC noted below.

(2) Includes the cash, upfront retained and deferred bonus elements.

(3) No CYBG PLC LTIP awards or legacy NAB LTIP awards vested during 2016 or 2017.

(4) Each of the Executive Directors also received £500 of free shares in March 2016.

Former Executive Directors and payments to past Directors (audited)

No Executive Directors left during the year. Richard Sawyer resigned as an Executive Director on 2 February 2016 when CYBG PLC demerged from NAB and no additional remuneration or fees were paid in 2017 by the Group or NAB for his services to the Group.

Executive Directors payments for loss of office (audited)

No payments were made during the year.

Total pension entitlements (audited)

David Duffy and Ian Smith have both opted out of the Group's defined contribution pension plans and receive cash allowances in lieu of pension contributions. Debbie Crosbie participated in the Group's defined benefit scheme until 31 July 2017, when the plan was closed to future accrual, based on her salary up to the earnings cap (£150,600 from October 2016 to April 2017 and £154,200 from April 2017 to July 2017). In addition, Debbie Crosbie received a cash allowance of 17.6% of her salary above the earnings cap, up to 31 July 2017 and an allowance of 18% on her full salary from 1 August 2017.

Annual report on remuneration continued

Details of the pension accrued in the Group's defined benefit pension scheme by Debbie Crosbie in respect of qualifying services are shown below. The value of the pension is calculated using the HMRC method. The remainder of the pension value is delivered as a cash allowance.

Values relating to DB scheme	Accrued pension at year end £000	Normal retirement date	Additional value of pension on early retirement £000	Pension value in the year from DB scheme £000	Pension value in year from cash allowance £000	Total £000
Debbie Crosbie	40	30 March 2035	–	43	57	**100**

Taxable benefits (audited)

- Executive Directors receive private medical cover, health assessment and life assurance.
- The CEO receives a car cash allowance of £30,000 p.a. and the other Executive Directors receive an allowance of £6,840 p.a.
- To support the CEO's relocation from Ireland to Glasgow, the CEO received an allowance of £35,000 p.a. which was payable until May 2017.

Annual bonus (audited)

The following annual bonus awards were made in respect of the 2017 financial year; these were agreed by the Committee having reviewed the Group's results. Details of the targets used to determine annual bonus in respect of the 2017 financial year and the extent to which they were satisfied are shown in the table below.

These figures are included in the single figure table on the previous page.

2017 saw a strong performance from the Group, with significant change as a result of the transformation programme and a focus on building a high-performing, customer-centric organisation with strong productivity and efficiency. In our first full year as CYBG we have demonstrated good progress in delivering against the key performance measures set by the Committee:

- underlying profit before tax up by 33% on last year and 15% ahead of target;
- underlying RoTE increased to 7.5%;
- underlying CIR improved by 7% from 74% to 67%;
- underlying costs for the year of £675m were below our target range of £690m to £700m.
- while our engagement score fell by 7% from last year it benchmarks well when compared to organisations going through similar levels of transformation;

The table below sets out the performance of the Group element for determining Executive Directors' bonus awards.

Executive Directors Underlying performance measures		Weighting	Threshold	Target	Stretch	Actual	**Award as % salary(2)**
Sustainable returns	PBT(1)	22.0%	£240m	£267m	£293m	£293m	**22%**
	Customer lending growth	18.4%	3.5%	4.5%	6.0%	6.0%	**18%**
	NPS	7.3%	20%	22.5%	25%	12.0%	**0%**
	Digital adoption	7.3%	35%	39%	43%	38.2%	**3%**
Efficiency	Total costs	5%	£700m	£696m	£690m	£675m	**5%**
	CIR	5%	72%	69%	65%	67%	**4%**
Capital optimisation	RoTE	10%	5.8%	6.4%	7.0%	7.1%	**10%**
Customer-focused culture	Colleague engagement	5%	72%	77%	82%	72%	**2%**
		80.0%					**64%**

(1) The underlying PBT excludes exceptional items which have reduced the statutory PBT by £25m (a reconciliation of underlying profit before tax to statutory profit before tax is provided in the Financial results section). The bulk of this reduction is driven by a combination of legacy conduct issues in respect of PPI, other conduct matters, separation costs and restructuring expenses. The underlying PBT was not adjusted by the incremental year-on-year change in the prudent valuation adjustment (PVA) figure for 2017. The PVA figure reduced by £3m year on year from £7m in 2016 to £4m in 2017. No upward adjustment to underlying PBT has been considered.

(2) To reflect the under performance of NPS and Colleague Engagement the Committee reduced the arithmetic out turn of 64.3% to 62% for calculating Executive Directors' bonus awards.

The Committee determined the personal award for each Executive Director should be at the maximum as set out below. This reflects the Committee's assessment of a strong performance against every category of their personal score card and the demonstration of the required behaviours for their role, together with the pivotal role the Executive Directors played in the successful delivery of our strategy in our second year as a standalone PLC.

Executive Director	Personal award % salary	Group award % salary	Total award % salary	Total award
David Duffy	20%	62%	82%	£820,000
Ian Smith	20%	62%	82%	£377,000
Debbie Crosbie	20%	62%	82%	£369,000

In assessing the Group's performance, the Committee reviewed a report from the Chair of the Risk Committee on any risk issues within the business and determined that no adjustments were required to the bonus pool or to individual bonus awards for Executive Directors.

Deferral of bonus (audited)

In line with regulatory requirements, a portion of the bonus award is subject to deferral to the extent to which the required deferral is not fully met by the LTIP award. Half of the upfront and deferred elements are also subject to a six-month retention period. As such the Executive Directors awards were made as follows.

	David Duffy	Ian Smith	Debbie Crosbie
Upfront cash	£284,000	£130,600	£127,800
Upfront shares (1)	£284,000	£130,600	£127,800
Deferred shares (2)	£252,000	£115,800	£113,400
Total	£820,000	£377,000	£369,000

(1) Awarded as conditional rights to CYBG PLC shares which will be released at the end of the six-month retention period.
(2) Awarded as conditional rights to CYBG PLC shares or other instruments with vesting after 12 months in line with regulatory requirements after taking account of the LTIP award. Half will be released on vesting with half subject to an additional 12-month retention period.
Once deferred bonus awards are subject to continued service until released, the Group can, in specific circumstances, apply malus and/or clawback to all or part of any bonus award.

LTIP awards

LTIP awards to be granted in relation to 2017

The following awards were made to Executive Directors to reflect their performance in 2017 and align their interests with those of shareholders.

2017 LTIP award	Percentage of salary (1)	Face value of award	Type of interest awarded	End of performance period	Percentage receivable for threshold performance (2)	Percentage receivable for target performance (3)
David Duffy	100%	£1,000,000	Conditional rights to CYBG PLC shares	30 Sep 2020	21%	67%
Ian Smith	100%	£460,000				
Debbie Crosbie	100%	£450,000				

(1) The award is based on a percentage of salary as at 30 September 2017.
(2) 21% reflects 9 of the measures vesting at 25% for threshold performance and 2 vesting at 0%.
(3) 67% reflects 9 of the measures vesting at 60% for target performance and 2 vesting at 100% for target performance.

The award will vest based on the performance over the 2018 to 2020 financial years as set out below. These objectives are designed to deliver sustainable growth over the next three years and as such deliver returns to shareholders. Outcomes will be disclosed on a retrospective basis at the end of the performance period.

Annual report on remuneration continued

2017 LTIP Underlying performance measures		Weighting	Threshold	Target	Stretch
Sustainable customer growth	Retail NPS	8.33%	21	24	27
	Customer lending growth	8.33%	4%	5%	6%
	Digital adoption	8.33%	50%	52.5%	55.0%
Efficiency	CIR(2)	20.00%	58%	55%	52%
	RoTE(2)(3)(5)	20.00%	10%	11%	12%
	IRB accreditation(1)	10.00%		Achieved	
Risk and compliance	Bad and doubtful debt/average loans(1)	6.67%	–	<30bps	–
	Cumulative operational risk losses(4)	6.67%	<£30m	<£25m	<£20m
	Complaints per 1000	6.67%	3.7	3.5	3.3
Customer-focused culture	Colleague engagement	2.50%	72	77	82
	Senior leadership diversity	2.50%	38%	40%	42%

(1) IRB accreditation (based on the full roll out) and bad and doubtful debt/average loans are all or nothing measures with 100% vesting if achieved for these elements.
(2) CIR and RoTE are targeted on an underlying basis.
(3) Three-year average.
(4) Cumulative figure for 2017, 2018 and 2019.
(5) CET1 ratio has been removed as a measure for 2017, but will underpin RoTE. CET1 must achieve >12% before the RoTE element is assessed.

In line with regulator changes to deferral periods, LTIP awards to Executive Directors will be released over three to seven years from the date of grant.

Past LTIP awards

2015 demerger LTIP award (audited)

Following the demerger from NAB an award was made to recognise the Executive Director's contribution to the success of the demerger, with performance measured against a cumulative underlying PBT target over 2016 to 2018. Details of the PBT targets will be disclosed after the end of the performance period once these are no longer commercially sensitive. The PBT outcome will be adjusted by the incremental year-on-year change in the prudent valuation adjustment figure during this period.

2015 demerger LTIP	Percentage of salary(1)	Face value of award	Number of shares awarded(2)	Type of interest awarded	End of performance period	Percentage receivable for below target performance	Percentage receivable for target performance
David Duffy	150%	£1,500,000	768,560	Conditional rights to CYBG PLC shares	30 Sep 2018	0%	100%
Ian Smith	100%	£450,000	230,568				
Debbie Crosbie	100%	£450,000	230,568				

(1) The award was based on a multiple of salary as at 30 September 2015.
(2) The award price of £1.9517 was calculated based on the average middle-market share price over the three days before grant.

2016 LTIP awards

Following the approval of the remuneration policy at the AGM, the following awards were made to Executive Directors to reflect their performance in 2016 and align their interests with those of shareholders.

2016 LTIP award	Percentage of salary(1)	Face value of award	Number of shares awarded(2)	Type of interest awarded	End of performance period	Percentage receivable for threshold performance(3)	Percentage receivable for target performance(4)
David Duffy	100%	£1,000,000	375,897	Conditional rights to CYBG PLC shares	30 Sep 2019	20%	68%
Ian Smith	100%	£460,000	172,912				
Debbie Crosbie	100%	£450,000	169,153				

(1) The award is based on a percentage of salary as at 30 September 2016.
(2) The award price of £2.6603 was calculated based on the average middle-market share price over the three days before grant.
(3) 20% reflects 80% of the measures vesting at 25% for threshold performance and 20% vesting at 0%.
(4) 68% reflects 80% of the measures vesting at 60% for target performance and 20% vesting at 100% for target performance.

The award was granted on 9 March 2017 and will vest based on the performance over the 2017 to 2019 financial years as set out below. These objectives are designed to deliver sustainable growth over the next three years and as such deliver returns to shareholders. Outcomes will be disclosed on a retrospective basis at the end of the performance period.

Performance over the period will be assessed against the following measures:

2016 LTIP measures		Weighting	Threshold	Target	Maximum
Sustainable customer growth	Clydesdale and Yorkshire Bank NPS	10%	22.5%	25%	27.5%
	Digital adoption	10%	45%	50%	55%
Efficiency	CIR(2)	25%	60%	57.5%	55%
Capital optimisation	CET1 ratio(1)(2)	10%	n/a	>12%	n/a
	RoTE(2)	30%	8%	9%	10%
	IRB accreditation for mortgage book(1)	5%	n/a	Achieved	n/a
Prudent risk management and governance	Bad and doubtful debt/average loans(1)(3)	5%	n/a	<25bps	n/a
	Cumulative operational risk losses(4)	5%	<£25m	<£20m	<£15m

(1) CET1 ratio, IRB accreditation for mortgage book and bad and doubtful debt/average loans are all or nothing measures with 100% vesting if achieved for these elements.
(2) CIR and RoTE are targeted on an underlying basis.
(3) Three-year average.
(4) Cumulative figure for 2017, 2018 and 2019.

Annual report on remuneration continued

Non-Executive Directors (audited)

The table below sets out the single total figure of remuneration and breakdown for each Non-Executive Director for the year ending 30 September 2017.

	Fees		Benefits		Total	
	2017 £000	2016 £000	**2017 £000**	2016 £000	**2017 £000**	2016 £000
Clive Adamson	**104**	23	**–**	–	**104**	23
David Bennett(1)	**190**	183	**–**	–	**190**	183
David Browne(1)	**100**	137	**–**	–	**100**	137
Paul Coby	**78**	23	**–**	–	**78**	23
Adrian Grace(1)	**100**	118	**–**	–	**100**	118
Fiona MacLeod	**81**	4	**–**	–	**81**	4
Jim Pettigrew(1)	**365**	495	**–**	–	**365**	495
Dr Teresa Robson-Capps(1)	**80**	102	**–**	–	**80**	102
Tim Wade	**107**	5	**–**	–	**107**	5
Richard Gregory(1)(2)	**45**	225	**–**	–	**45**	225
Total	**1,250**	1,315	**–**	–	**1,250**	1,315

(1) Fees in 2016 include those in respect of increased duties during the demerger.
(2) Richard Gregory retired from the Board on 10 January 2017.

Non-Executive Directors' annual fees

The following fees are payable to Non-Executive Directors in line with the rates approved by the Board in November 2015 and reaffirmed by the Board in September 2017. The Non-Executive Directors are reimbursed for expenses they incur in performing their duties. Any tax arising on such reimbursed expenses is paid by the Group.

Chairman	£350,000
Non-Executive Director	£70,000
Deputy Chairman	£60,000
Senior Independent Director	£30,000
Chair Audit Committee	£30,000
Chair Risk Committee	£30,000
Chair Remuneration Committee	£30,000
Member Audit Committee	£10,000
Member Risk Committee	£10,000
Member Remuneration Committee	£10,000
Chair Governance and Nomination Committee	£5,000
Member Governance and Nomination Committee	£5,000

Non-Executive Directors' fees in 2018 may be reviewed as the Group progresses with its strategic priorities and to reflect any changes in the nature of a Non-Executive Director's role and responsibilities.

Former Non-Executive Directors and payments to past Non-Executive Directors (audited)
Richard Gregory retired from the Board on 10 January 2017. No additional fees were paid by the Group for his services to the Group.

Non-Executive Directors payments for loss of office (audited)
No payments were made during the year.

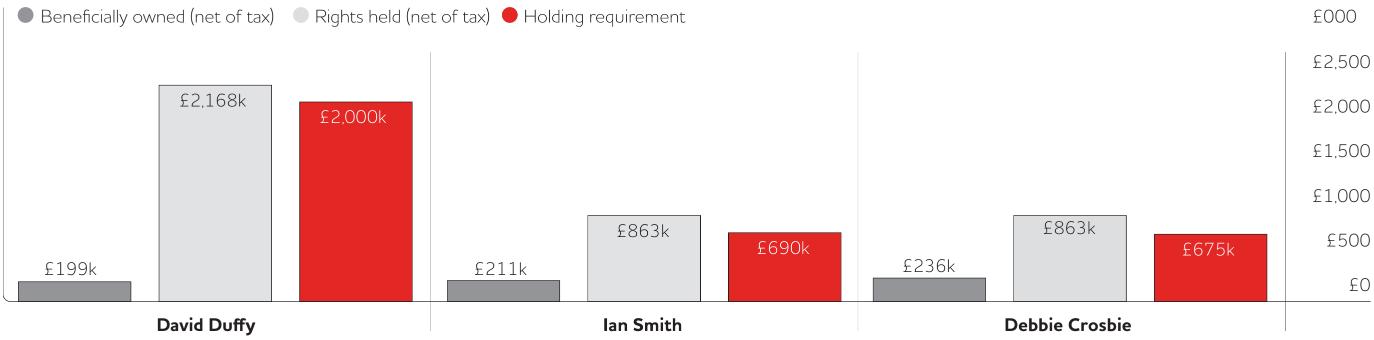
Statement of Directors' shareholding and share interests (audited)
Executive Directors are required to build up a holding of the Group's shares to the value of 150% of base salary (200% for the CEO). To support this, Executive Directors are required to retain 60% of the net shares received from variable pay awards after the payment of tax and National Insurance until the shareholding requirement is met.

Detailed below are the current beneficial holdings of ordinary shares for each Executive Director, together with details of their vested and unvested awards under the CYBG PLC share plans.

Director	Ordinary shares(1)(2)	Vested awards(3)	Unvested awards(4)	Vested LTIP awards	Unvested LTIP awards(5)(6)	Maximum total shares and awards	Expected value pre tax £000	Expected value net of tax(7) £000
David Duffy	123,747	–	78,299	–	1,144,457	1,346,503	4,091	2,168
Ian Smith	96,356	34,408	36,086	–	403,480	535,922	1,628	863
Debbie Crosbie	100,736	46,113	35,296	–	399,721	535,753	1,628	863

(1) Ordinary shares beneficially owned, including any shares held via the CYBG PLC Share Incentive Plan and holdings of connected persons. Ian Smith joined the partnership scheme in April 2017 and purchased 320 shares by 30 September 2017.
(2) Includes CHESS Depositary Interests (CDIs) which represent interests in ordinary shares beneficially owned by David Duffy (4,080) and Ian Smith (4,502). Values are based on 30 September 2017 closing price of AUS$5.14 (300.8p) and the average exchange rate on the day (AUS$:GBP 0.5853).
(3) Gross number of conditional rights awards which have vested but not yet been released as shares.
(4) Unvested awards are subject to continued employment with no business performance conditions.
(5) Unvested awards are subject to continued employment and the achievement of business performance conditions. This applies to the gross number of shares under the 2015 demerger LTIP award which have not yet vested and are subject to business performance conditions and continued employment.
(6) The unvested 2015 demerger LTIP and 2016 LTIP awards have been included at 100% of their face value in line with current accounting assumptions. Values are based on the 30 September 2017 closing price of 303.80 pence.
(7) Assumes 47% is deducted from vested and unvested rights to reflect the tax and national insurance due on the release of shares.

The chart below shows the Executive Directors' current share holdings and net number of shares they would receive if all the unreleased rights (vested and unvested) shown above vested in full against their shareholding requirements applicable for Executive Directors:



Annual report on remuneration continued

For the purpose of assessing the Executive Directors' holdings against the shareholding requirements at 30 September 2017 unvested awards are excluded.

Director	Base salary	Requirement as % of base salary	Shares and vested rights[1]	Expected value net of tax[2]	Shareholding requirement met?
David Duffy	£1,000,000	200%	123,747	199,250	No
Ian Smith	£460,000	150%	130,764	210,548	No
Debbie Crosbie	£450,000	150%	146,849	236,447	No

(1) Includes vested awards over CYBG PLC shares which have not yet been released.
(2) Values are based on the 30 September 2017 closing price of 303.80 pence, with 47% deducted from vested rights to reflect the tax and National Insurance due on the release of shares.

One Executive Director (Ian Smith) purchases shares via the Share Incentive Plan and currently purchases £150 worth of shares per month.

Non-Executive Directors' shareholding (audited)
The beneficial interests of the Non-Executive Directors and their connected persons who held office at 30 September 2017 in the shares of the Group and as at 30 September 2016 are shown below:

Non-Executive Directors	Ordinary shares beneficially owned at 30 September 2016 or date of appointment if later	Ordinary shares beneficially owned at 30 September 2017 (or date of cessation if earlier)
Clive Adamson	–	–
David Bennett	16,334	16,334
David Browne	5,000	5,000
Paul Coby	–	–
Adrian Grace	16,220	16,220
Fiona MacLeod	–	7,000
Jim Pettigrew	50,000	50,000
Dr Teresa Robson-Capps	–	–
Tim Wade	–	–

None of the Non-Executive Directors holds any awards under the CYBG PLC share plans.

None of the Non-Executive Directors, or their connected persons, bought or sold shares between 30 September 2017 and the date of this report.

Executive Directors' shareholdings under each of the Group's share plans
The Group operates four share plans which were approved prior to the demerger, namely:

- Deferred Equity Plan (DEP);
- Long Term Incentive Plan (LTIP);
- Share Incentive Plan (SIP); and
- Save As You Earn Plan (SAYE).

As CYBG PLC is no longer part of the NAB Group, no details of outstanding NAB awards are included within this section.

Deferred Equity Plan (DEP)

Awards were made to Executive Directors under the DEP following the demerger.

DEP awards	Start of year	Awarded during the year	Vested during the year[1]	Lapsed during the year	Unvested at year end[2]	Date of grant	Grant price[3]	Market value at date of grant[3] £000	Notes
David Duffy	768,560	–	–	–	768,560	11 Feb 16	195.17	1,500	2015 demerger LTIP
	–	78,299	–	–	78,299	09 Mar 17	266.03	208	2016 deferred bonus
	–	375,897	–	–	375,897	09 Mar 17	266.03	1,000	2016 LTIP
Ian Smith	34,408	–	34,408	–	–	11 Feb 16	195.17	–	2015 deferred bonus
	230,568	–	–	–	230,568	11 Feb 16	195.17	450	2015 demerger LTIP
	–	36,086	–	–	36,086	09 Mar 17	266.03	96	2016 deferred bonus
	–	172,912	–	–	172,912	09 Mar 17	266.03	460	2016 LTIP
Debbie Crosbie	46,113	–	46,113	–	–	11 Feb 16	195.17	–	2015 deferred bonus
	230,568	–	–	–	230,568	11 Feb 16	195.17	450	2015 demerger LTIP
	–	35,296	–	–	35,296	09 Mar 17	266.03	94	2016 deferred bonus
	–	169,153	–	–	169,153	09 Mar 17	266.03	450	2016 LTIP

(1) The upfront retained bonus award vested on 9 March 2017 when granted.
(2) None of the unvested awards is due to vest in 2017.
(3) The value of awards granted under the DEP was based on the three-day mid-market closing price over the preceding three days.

Long Term Incentive Plan (LTIP)

An award was made on 9 March 2017 in relation to the 2016 LTIP following the approval of the remuneration policy at the AGM.

Share Incentive Plan (SIP)

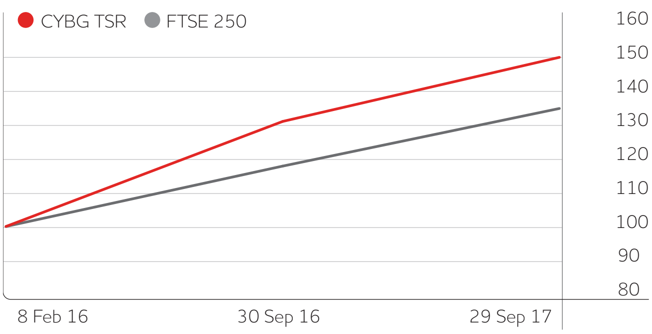
No awards were made to Executive Directors under the SIP during 2017. One Executive Director (Ian Smith) currently participates in the monthly purchase of shares through the SIP.

Save As You Earn plan (SAYE)

No offers under the CYBG PLC SAYE plan have been made.

Total Shareholder Return (TSR) performance

The graph below shows the value of £100 invested in the Group's shares since listing, compared with the FTSE 250 Index. The graph shows the TSR generated by both the movement in share value and the reinvestment over the same period of dividend income. The Committee considers the FTSE 250 as representative of the current market capitalisation of the Group.



Source: PwC

Annual report on remuneration continued

CEO historic remuneration

The table below sets out the total remuneration delivered to the Chief Executive Officer over 2017:

Chief Executive Officer	2017	2016
Total single figure (£000)	**2,056**	2,048
Annual short term incentive payment level achieved (% of maximum opportunity)	**82%**	80%
Long-term incentive vesting level achieved (% of maximum opportunity)(1)	**–**	–

(1) No CYBG LTIP awards vested during 2016 or 2017.

Relative importance of spend on pay

The table below sets out the relative importance of spend on pay in the 2017 financial year:

Overall spend	Disbursements from profit in 2017 financial year £m	Disbursements from profit in 2016 financial year £m
Dividend(1)	**9**	–
Overall spend on pay including Executive Directors(2)	**166**	280

(1) The Directors have recommended a final dividend in respect of the year ended 30 September 2017 of 1p per ordinary share in the Company (2016: Nil) to be paid on 16 February 2018 subject to approval of shareholders at the 2018 Annual General Meeting.
(2) 2016 and 2017 figures as per note 2.4 of the consolidated financial statements. The 2017 overall spend on pay includes a past service credit of £88m as a result of the closure of the defined benefit pension scheme to future accrual for the majority of members.

Change in the CEO's remuneration compared with colleagues

The table below shows the percentage change in remuneration for the CEO between 2016 and 2017 compared with the percentage change in the average remuneration of colleagues.

Remuneration compared with colleagues	Salary 2016 to 2017	Benefits(3) 2016 to 2017	Bonus 2016 to 2017
CEO(1)	0%	–16%	2.4%
Colleagues(2)	2.6%	0%	5.3%

(1) Reflects annual salary at 30 September and average for respective years.
(2) Reflects average annual FTE salary of colleagues employed at both 30 September 2016 and 30 September 2017 and average bonus awards for 2016 and 2017.
(3) Taxable benefits and other allowances excluding employer pension contributions, with the CEO's accommodation allowance ending part way through the year.

Other remuneration disclosures

Our remuneration policy for all colleagues

The Group has implemented a firm-wide remuneration policy that is designed to attract and retain high-calibre individuals who will promote the delivery of our long-term strategy in line with our business, values and risk appetite. While the levels and elements of the remuneration may differ from that of the Executive Directors, they are based on the same principles, aligning remuneration, which shall not be excessive, and ensuring that variable pay is appropriate, balanced and calibrated for any impact of risk.

Element	Objective	Operation
Base salary	Recruit, reward, retain and recognise scope of role.	Base salaries are reviewed annually and reflect Group and individual performance, skills, experience and the scope of the role.
Benefits	To provide benefits consistent with role.	The Group provides access to a range of benefits which may vary according to seniority.
Pension	To provide benefits consistent with role.	The Group operates a defined contribution pension scheme for all colleagues. The defined benefit scheme closed to new entrants in 2014, with the Scheme closing to future accrual on 31 July 2017 for the majority of colleagues.
Bonus	The annual bonus is designed to reward Group and personal performance in line with strategic objectives.	The Group has a single firm-wide short-term incentive plan. This is discretionary and is based on Group and individual performance within the year. The determination of measures and their weighting are set annually and awards are determined by the Remuneration Committee at the end of the financial year. For MRTs, deferral is applied in line with PRA Remuneration Code. Where that does not apply, colleagues who have a bonus award of £14,000 or more will have part of the award deferred for 12 months.
LTIP	Delivery of the Group's strategy and growth in shareholder value.	In line with Executive Directors, the Group's Executive Leadership Team is able to influence the Group's performance and they are incentivised to do so through eligibility to equity-based compensation. Awards are based on a three-year performance period reflecting a basket of business and shareholder measures aligned with strategic goals. Awards will vest a minimum of three years after being awarded, or longer where required by the PRA Remuneration Code. Awards may be subject to a discount in determining total variable remuneration under the rules set by the European Banking Authority.
Other share plans	Offers opportunity to acquire shares in CYBG PLC	As well as the DEP and LTIP, the Group operates: – a SIP under which colleagues may purchase Partnership Shares and the Group may offer free shares; and – the Group may in the future offer a SAYE plan.
Commencement, retention and guaranteed awards	Buy-out of unvested equity from a previous employer	The amount, timing and performance hurdles are based on those being forfeited and satisfactory evidence. Guaranteed incentives or bonus are not provided to existing colleagues.

Total reward consists of both fixed and variable components:

- fixed remuneration provided as cash and benefits (including employer pension); and
- variable remuneration reflects both individual and business performance.

Other remuneration disclosures continued

The mix of fixed and variable reward is balanced to ensure that fixed remuneration provides a sufficient level of remuneration so that the variable reward components can be fully flexible, including the possibility of paying no variable reward. The remuneration mix at target is based on market information and practices. In any year, the actual mix may vary from target, given the overlay of business performance and individual performance.

All variable pay awards to MRTs are subject to malus and clawback in line with regulatory requirements.

Control functions
Colleagues engaged in control functions (*i.e.* Risk, Internal Audit and Compliance colleagues) are critical to effective management of risk across the Group. Independence from the business for these colleagues is assured through:

- setting the reward mix so that variable reward is not significant enough to encourage inappropriate behaviours while remaining competitive with the external market; and
- scorecards which are specific to the function.

The Committee reviews remuneration structures for control function colleagues.

Risk adjustment
In addition to the Committee's review of risks that impact on the level of the bonus pool and the application of malus and clawback as outlined above, individual bonus awards are also subject to meeting all compliance requirements and awards made can be reduced to nil where these are not met, or where colleagues are subject to disciplinary sanction.

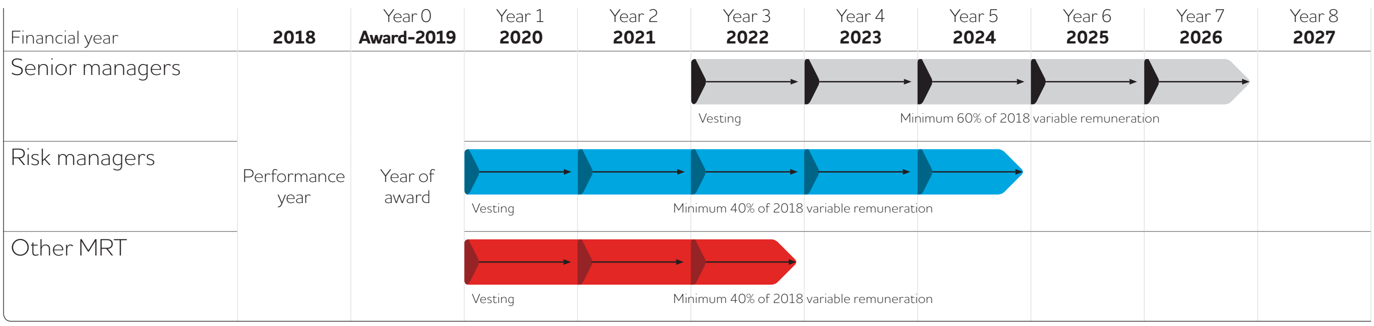
Deferral arrangements
Variable rewards (bonus, LTIP and retention awards) are subject to deferral and retention for all MRTs in line with UK regulation:

- at least 60% of total variable reward will be deferred where the total variable reward is £500,000 or more; and
- at least 40% of total variable reward will be deferred where the MRT does not meet *de minimus* conditions.

The period of deferral ranges from one to three years to three to seven years depending on role in line with UK legislation.

The tables below set out the deferral arrangements for those roles classed as MRTs under Articles 2, 3 and 4 of the European Banking Authority Guidelines. These have been grouped under the three classifications within Strengthening Individual Accountability in Banking:

- Senior Manager Function (SMF) roles under the Senior Manager Regime. This includes Executive Directors, SMF Non-Executive Directors (Chairman, Senior Independent NED and the Chairman of Remuneration, Risk, Audit and Nomination Committees) and other SMF leadership team members and senior managers.
- Risk Manager roles which includes (but not exclusively) leadership team members not classified as SMF, the senior management responsible for material business units, for management of specific risk categories such as liquidity, operational or interest rate risk, and for control functions who are responsible for the day-to-day management of the business, its risks, or its control functions.
- Other MRT which are roles considered to have material impact on the risk profile of the Group.



Award subject to additional holding period in line with regulatory requirements.

Remuneration of MRTs for 2017

This section discloses the remuneration awards made by the Group to 157 MRTs (2016: 149) in respect of the 2017 performance year. Additional information summarising the Group's decision-making policies for remuneration are also provided. These disclosures deliver the requirements of Capital Requirements Regulation (CRR) Article 450.

The following groups of individuals have been identified as meeting the criteria for MRTs including those who may have a material impact on the Group's risk profile:

- senior management, Executive Board Directors, members of the Executive Leadership Team;
- Non-Executive Directors; and
- other individuals whose activities could have an impact on the Group's risk profile.

Aggregate remuneration of MRTs by business area	Banking[1]	Independent control functions[2]	Corporate functions[3]	Total
Number of MRTs	45	81	31	157
Total fixed remuneration (£m)	5.6	12.1	4.7	22.4

(1) Includes colleagues in the Customer Banking Division and the Customer Banking Director.
(2) Includes Executive Directors, Non-Executive Directors and colleagues within Risk, Internal Audit and Compliance functions.
(3) Includes Human Resources, Finance, Marketing, Products and other corporate functions.

Total value of MRTs remuneration awards	Senior management £m[1]	Other MRTs £m[2]	Total £m
Number of MRTs	24	133	157
Fixed remuneration[3]	6.6	15.8	22.4
Variable remuneration (cash)	1.3	2.4	3.7
Variable remuneration (shares)	1.3	1.1	2.4
Deferred remuneration (cash)[4]	–	–	–
Deferred remuneration (shares)[5]	0.8	0.9	1.7
Long-term incentive (shares)[5][6]	4.4	2.3	6.7
Total variable remuneration[7]	7.8	6.7	14.5
Total remuneration	14.4	22.5	36.9

(1) Includes the Executive Directors, members of the Executive Leadership Team and those holding a Senior Management Function under the Senior Management Regime.
(2) Includes Non-Executive Directors, colleagues identified as MRTs under the FCA/PRA criteria and any colleagues who the Group consider to have responsibility and accountability for activities that could have a material impact on the Group's business risk profile or credit exposure and colleagues in independent Risk, Internal Audit and Compliance function roles.
(3) Excludes termination awards made under the Group redundancy policy together with PILON and any pension augmentation.
(4) Deferred bonuses awarded in cash.
(5) All awards are made as conditional rights to the Group's shares.
(6) Reflects the face value of the 2017 LTIP award to be made.
(7) Includes current year commencement awards awarded in 2017.

Deferred remuneration	Senior management £m	Other MRTs £m	Total £m
Deferred remuneration at 30 September 2017[1]			
Outstanding vested	2.4	1.7	4.0
Outstanding unvested	9.1	3.0	12.1
Awarded during the financial year[2]	5.6	2.9	8.5
Released/paid out during the financial year[3]	1.1	0.7	1.8
Reduced through performance adjustments[4]	–	–	–

(1) Value at date of award. Figures including 2015 and 2016 deferred awards (LTIP, Bonus and commencement) plus 2017 awards.
(2) Includes 2016 deferred bonus awards, 2016 LTIP and 2017 commencement awards.
(3) Reflects deferred elements of 2015 and 2016 bonuses.
(4) This figure does not include the adjusted value of awards which were forfeited by colleagues upon leaving the Group.

Other remuneration disclosures continued

Other remuneration	Senior management	Other MRTs	Total
Commencement awards (£m)(1)	–	0.7	0.7
Number of beneficiaries	–	5	5
Highest award to single beneficiary (£m)	–	0.4	
Termination awards (£m)(2)	–	1.6	1.6
Number of beneficiaries	–	8	8
Highest award to single beneficiary (£m)	–	0.7	

(1) Current year commencement awards and prior year buyout awards granted in 2017.
(2) Awards made under the Group redundancy policy together with PILON and any pension augmentation.

Remuneration band (€m)(1)	Senior management	Other MRTs	Total
More than €3.5m	–	–	–
€3.0m – €3.5m	1	–	1
€2.5m – €3.0m	–	–	–
€2.0m – €2.5m	–	–	–
€1.5m – €2.0m	–	–	–
€1m – €1.5m	5	–	5
€0.5m – €1.0m	4	3	7
Less than €0.5m	14	130	144

(1) Total remuneration has been calculated including fixed remuneration, allowances, variable remuneration (including 2017 LTIP at face value) in relation to the performance year, and fees for Non-Executive Directors. Variable remuneration includes the annual short-term incentive award in respect of the 2017 financial year. Bands have been converted using a rate of 1 GBP = 1.08401 EUR, consistent with the European Commission's currency converter for September 2017.

Directors' report

Corporate governance report

The Corporate governance report, found on pages 49 to 122, together with this report of which it forms part, fulfils the requirements of the Corporate Governance Statement for the purpose of the FCA's Disclosure and Transparency Rules (DTR).

Company background

The Company was incorporated in England and Wales on 18 May 2015 as a public company limited by shares under the Companies Act 2006 with the name Pianodove PLC. Pianodove PLC changed its name to CYBG PLC on 1 October 2015. The registered office of the Company is at 20 Merrion Way, Leeds, West Yorkshire, LS2 8NZ with the Head Office and principal place of business of the Company being 30 St Vincent Place, Glasgow, G1 2HL.

Directors

The current Directors of the Company and their biographical details are shown on pages 55 to 59. As previously announced, Richard Gregory, Senior Independent Non-Executive Director retired from the Board on 10 January 2017.

Particulars of Directors' emoluments and interests in shares in the Company are given on pages 108 to 118 of the Directors' remuneration report.

During the year, no Director had a material interest in any contract of significance to which the Company or a subsidiary undertaking was a party.

Board composition changes

Changes to the composition of the Board since 1 October 2016, and up to the date of this report, are shown in the table below. Further details of Board changes can be found on page 67 of the Corporate governance report and on page 76 of the Governance and Nomination Committee report.

Name	Role	Date of retirement
Richard Gregory	Senior Independent Non-Executive Director	10 January 2017

Annual general meeting (AGM)

The Company's 2018 AGM will be held at 10am (GMT) on Wednesday 31 January 2018 at the offices of Pinsent Masons LLP, 30 Crown Place, Earl Street, London, EC2A 4ES, United Kingdom. Details of the meeting venue and the resolutions to be proposed, together with explanatory notes, are set out in a separate Notice of AGM which accompanies this Annual Report and Accounts and is published on the Company's website www.cybg.com

The AGM will be webcast live at 10am (GMT) on Wednesday 31 January 2018 on the Company's website www.cybg.com and a recording will also be available shortly after the conclusion of the AGM. Please note that viewing the live webcast does not enable shareholders to ask questions or vote during the AGM.

The webcast may include a question and answer session with shareholders present at the AGM in addition to background shots of those in attendance. Photographs may also be taken at the AGM and used in future Group publications. If you attend the AGM in person, you may be included in the webcast, recording and/or photographs.

Election and re-election of Directors at the forthcoming AGM

Following recommendations from the Governance and Nomination Committee, the Board considers all Directors continue to be effective, committed to their roles and have sufficient time available to discharge their duties.

In accordance with the Code, all Directors will retire and seek re-election at the 2018 AGM.

Directors' indemnities

The Directors have each entered into individual deeds of access, insurance and indemnity with the Group which, among other things and subject to certain exceptions, indemnify the Directors to the maximum extent permitted by law and regulation against liabilities to a person other than the Company or an associated company that they may incur as an officer of the Company and any other subsidiary of the Group. Each such provision constitutes a 'third-party indemnity provision' and a 'qualifying indemnity provision' for the purposes of section 234 to 236 of the Companies Act 2006. These provisions are in force for the benefit of the Directors at the date of this report, and were in force when this report was approved and during the financial year to which this report relates. Such deeds are available for inspection at the Company's registered office.

The Group has an insurance policy in place for the benefit of all trustees, colleagues, Directors, officers, members and partners of the Company while acting in the capacity of a trustee or administrator of employee benefit or pension plans. This policy therefore indemnifies the Directors of Yorkshire and Clydesdale Bank Pension Trustee Limited and YCB DC Trustee Limited (each a 'Trustee Company'), the trustees of two occupational pension schemes operated by the Group, against liability incurred by them in connection with the management and administration of the pension schemes. This insurance policy constitutes a 'pension scheme indemnity provision' and a 'qualifying indemnity provision' for the purposes of sections 235 to 236 of the Companies Act 2006. These provisions are in force for the benefit of the Directors of Trustee Companies at the date of this report, and were in force when this report was approved and during the financial year to which this report relates. Such policy is available for inspection at the Company's registered office.

In addition, the Group had appropriate Directors' and Officers' Liability Insurance cover in place throughout the financial year.

Profits and appropriations

The Group profit before tax for the financial year ended 30 September 2017 amounted to £268m (2016: profit of £77m). The profit attributable to the ordinary shareholders for the year ended 30 September 2017 amounted to £146m (2016: loss of £206m). As at 30 September 2017, the distributable reserves of the Company were £1,002m (2016: £1,003m).

Directors' report

Dividends

The Directors recommend a final dividend of 1p per ordinary share in the Company in respect of the year ended 30 September 2017 (2016: £Nil) which will, subject to approval by shareholders at the 2018 Annual General Meeting, be payable on 16 February 2018.

Amendment to the Articles of Association

The Company may only amend its Articles of Association if its shareholders pass a special resolution to that effect.

Share capital, control and Directors' powers

Shares in the Company are listed on both the London Stock Exchange (LSE) and the ASX (in the form of CHESS Depositary Interests (CDIs)) and therefore, the Company is required to comply with the disclosure requirements of both listing regimes.

Details of the movements in allotted share capital during the year, together with the rights and obligations attaching to the Company's shares, are shown in note 4.1 to the consolidated financial statements.

There are no restrictions on voting rights of securities in the Company. The Notice of AGM specifies deadlines for determining attendance and voting entitlements at the AGM.

Where participants in an employee share incentive plan operated by the Company are the beneficial owners of shares but not the registered owners, the voting rights are normally exercised at the discretion of participants.

With the exception of restrictions on the transfer of ordinary shares under the Company's share incentive plans, while the shares are subject to the rules of the plan, there are no restrictions which exist on the transfer or holding of securities in the Company under its Articles of Association and there are no shares carrying special rights with regards to the control of the Company.

Subject to the Articles of Association and provisions of relevant statutes, the Board may exercise all powers of the Company.

Acquisition of own shares

At the AGM of the Company held on 31 January 2017 a resolution was passed that the Directors were authorised to purchase up to a maximum of 88,153,185 ordinary shares representing approximately 10% of the issued ordinary share capital. A renewal of authority will be sought at the 2018 AGM. Further information is set out in the Notice of AGM.

Political donations

The Group did not give any money for political purposes nor did it make any political donations to political parties or other political organisations, or to any independent election candidates, or incur any political expenditure during the year. At the Annual General Meeting in 2017, shareholders gave authority under Part 14 of the Companies Act to make political donations and incur political expenditure up to a maximum aggregate amount of £100,000. This authorisation was sought for prudence as it is the Group's policy not to make any political donations to political parties or incur political expenditure within the ordinary meaning of those words. Given the wide definition of donations and expenditure within the Companies Act, activities which form part of the regular operations of the Group such as communicating with government at local, national and European level and funding events to which politicians are invited, may be covered.

Financial risk management objectives and policies

Information about internal controls and financial risk management systems in relation to financial reporting and Board review can be found on page 71 of the Corporate governance report.

Information about financial risk management objectives and policies in relation to the use of financial instruments can be found in the Risk report on pages 127 to 175.

Post balance sheet events

There have been no material post balance sheet events.

Information included in the Strategic report

The following information that would otherwise be required to be disclosed in this report and which is incorporated into this report by reference can be found on the following pages of the Strategic report.

Subject matter	Page reference
Future developments	13 to 15
Colleague engagement	30 to 32
Emissions reporting	34 to 35

Equality of employment opportunities

It is the policy of the Group to promote equality of employment opportunities by giving full and fair consideration to applications from people with disabilities. If existing colleagues become disabled, every effort is made to retain them within the workforce wherever reasonable and practicable. The Group also endeavours to provide equal opportunities in the training, promotion and general career development of disabled persons.

Substantial shareholdings

Information provided to the Company pursuant to the FCA's DTR is published on Regulatory Information Services and on the Company's website.

As at 30 September 2017, the following information has been received, in accordance with DTR 5, from holders of notifiable interests in the Company's issued share capital. The information provided below was correct at the date of notification; however, the date received may not have been within the current financial year. It should be noted that these holdings are likely to have changed since the Company was notified. However, notification of any change is not required until the next notifiable threshold is crossed.

	Total number of shares	% of issued capital with rights to vote in all circumstances at general meetings[1]
Perpetual Limited and subsidiaries	83,900,030	9.49%
Cooper Investors Pty Ltd	52,888,470	5.99%
Schroders plc	44,572,549	5.04%
Investors Mutual Limited	45,016,877	6.17%
AMP Life Limited, AMP Capital Investors Limited, Ipac Asset Management Limited, AMP Capital Investors (NZ) Limited	43,908,981	4.97%
JCP Investment Partners Limited	35,251,058	3.99%
BT Investment Management Limited	27,036,329	3.06%

(1) Percentage correct as at 30 September 2017.

Going concern

The Group's Directors have made an assessment of the Group's ability to continue as a going concern and are satisfied that the Group has the resources to continue in business for the foreseeable future.

The Group's use of the going concern basis for preparation of the accounts is discussed in note 1.4 of the Group's consolidated financial statements.

Viability statement

Viability

In accordance with the Code, the Directors have assessed the prospects of the Group over a three-year period to 30 September 2020.

The Directors have determined that a three-year period is an appropriate period over which to perform the assessment. This is the period over which forecasts have a greater level of certainty. The Board monitors a longer-term strategic and financial plan which extends beyond the three-year period. This longer-term strategic and financial plan provides less certainty of outcome, but provides a robust planning tool against which strategic decisions can be made.

In making this assessment the Directors have considered a wide range of information, including the Directors' robust review and challenge of the outcomes of the latest ICAAP and the ILAAP, which assess the Group's future projections of capital adequacy, liquidity and funding. The Board has also considered the results of stress testing which is performed.

Furthermore, the Directors have considered the current state of the balance sheet, principal and emerging risks which could impact the performance of the Group and the Group's strategic and financial plan which includes future projections of profitability alongside capital funding and liquidity in a manner aligned to the ICAAP and ILAAP. The strategic and financial plan makes certain assumptions about the performance of the Group and the economic, market and regulatory environments in which it operates. To support the planning process, downside scenario analysis has been performed to consider how the Group's performance would be affected by changing economic and market conditions throughout the planning period.

Information relevant to this assessment can be found in the following sections of the Annual Report and Accounts:

- a financial summary, including a review of the latest income statement and balance sheet is provided in the Financial results section pages 38 to 48;
- the Group's capital position is included in the balance sheet and prudential regulation risks section of the Risk report pages 154 to 160;
- the Group's liquidity position is described in the balance sheet and prudential regulation risks section of the Risk report pages 160 to 167;
- the Group's principal risks and policies and processes for managing those risks are described in the Strategic report on page 19;
- the Group's business model and strategy are described in the Strategic report pages 10 to 13; and
- the Group's approach to stress testing and reverse stress testing are described in the Risk report on page 135.

Based upon this assessment, the Directors have concluded that there is a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the three years to 30 September 2020.

Disclosure of information under Listing Rule (LR) 9.8.4R

Additional information required to be disclosed by LR9.8.4R, where applicable to the Group, can be found in the following sections of this report:

Subject matter	Page reference
Publication of unaudited financial information	The disclosures within the Risk report (pages 127 to 175) are unaudited unless otherwise stated.
Allotment of equity securities	233
Significant contracts	248

Research and development activities

The Group does not undertake formal research and development activities although it does invest in new platforms and products in each of its business lines in the ordinary course of business. In addition to new products and services the Group also invests in internally generated intangible assets including software and computer systems. Further details can be found in note 3.10 of the Group's consolidated financial statements.

Directors' report

Change of control

The Group is not party to any significant agreements that are subject to change of control provisions in the event of a takeover bid, other than the following:

– A Conduct Indemnity Deed with NAB under which NAB has agreed, subject to certain limitations, to provide CYBG with a capped indemnity in respect of certain historic liabilities relating to relevant conduct matters (as defined therein). The capped indemnity will not automatically cease to apply nor will it automatically terminate upon any takeover. However, prior to any change of control, the parties must cooperate in good faith to facilitate an assessment by the PRA to determine whether the capped indemnity should continue at the same amount or whether it should be terminated in whole or part. Any such assessment will be at the sole discretion of the PRA.

There is a very small number of senior colleagues who are entitled to an enhanced redundancy payment if redundancy arises within the initial period of employment and is a result of a change of control. The Group has share schemes under which change of control may apply, albeit this is not considered to be significant.

Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and the Group and Company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law, they are required to prepare the Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and applicable law and have elected to prepare the parent company financial statements on the same basis. Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Company and of the profit or loss of the Group and Company for that year. In preparing these financial statements the Directors are required to:

– select suitable accounting policies in accordance with International Accounting Standard (IAS) 8: Accounting Policies, Changes in Accounting Estimates and Errors and then apply them consistently;

– present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;

– provide additional disclosures when compliance with the specific requirements of IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the financial performance; and

– state that the Group and Company have complied with IFRSs, subject to any material departures disclosed and explained in the financial statements.

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

Under applicable law and regulations, the Directors are also responsible for preparing a Strategic report, Directors' report, Directors' remuneration report and Corporate governance statement that comply with that law and those regulations.

Responsibility statement of the Directors in respect of the Annual Report and Accounts

The Directors confirm that to the best of our knowledge:

– the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the Group and the undertakings included in the consolidation taken as a whole; and

– the Strategic report includes a fair review of the development and performance of the business and the position of the Company and the Group, together with a description of the principal risks and uncertainties that they face.

The Directors consider the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's and Group's position and performance, business model and strategy.

Independent auditor and audit information

In accordance with section 485 of the Companies Act 2006, a resolution to reappoint Ernst & Young LLP, and to authorise the Audit Committee to agree their remuneration, will be proposed at the next AGM.

The Directors who were members of the Board at the time of approving the Report of the Directors are listed on page 53. Having made enquiries of fellow Directors and of the Group's auditor, each of these Directors confirms that:

– to the best of each Director's knowledge and belief, there is no information relevant to the preparation of their report of which the Group's auditor is unaware; and

– each Director has taken all the steps a Director might reasonably be expected to have taken to be aware of relevant audit information and to establish that the Group's auditor is aware of that information.

On behalf of the Board:

Lorna McMillan
Company Secretary
20 November 2017

CYBG PLC. Registered No. 09595911

RISK REPORT

Risk report

> Effective management of risk is a key capability for a successful financial services provider and is fundamental to the Group's strategy. The Group has continued to advance and strengthen its risk capabilities, evolving in line with industry developments and best practice.

Risk principles

The Group's approach to risk management is based on the principle that risk management capability must be embedded across all areas of the Group to be effective. This overriding principle embodies the following concepts:

- commercial decisions are made on the basis of proactive consideration of risk and the potential impact on customers;
- business managers use the RMF to support decision making involving risk and reward trade-offs; and
- colleagues are responsible for risk management in their day to day activities.

Risk culture

Central to the Group's risk culture is the fair treatment of customers and meeting obligations to stakeholders, including shareholders, regulators and colleagues. The Board and senior management are responsible for setting and clearly communicating a strong risk culture through their actions and words, and proactively addressing any identified areas of weakness or concern.

Culture is shaped by many aspects including tangible components such as: the Group's code of conduct; operating principles; policies; standards; the risk management operating model; and an approved articulation of risk appetite that aligns to, and supports, the strategic objectives of the Group. The Group strives to instil a culture that supports compliance with all relevant laws, codes and policies and builds constructive regulatory relationships.

Initiatives that support appropriate risk culture include: the performance management framework; the formal whistleblowing framework that allows colleagues, in confidence and anonymously, to raise concerns about matters of conduct; and messaging from the CEO and members of the Executive Leadership Team emphasising the importance of risk identification, management and mitigation.

Underpinning the RMF and at the heart of the Group's risk culture, is the concept of personal accountability for risk management at source. This is enabled through a risk management accountability model and a formal delegation framework through which colleagues are able to make risk based decisions.

Risk strategy

The Group has a clearly defined strategy in order to manage and mitigate risk in the daily course of its business. The strategy consists of:

- ensuring all principal and emerging risks are identified and assessed;
- ensuring risk appetite is clearly articulated and influences the Group's strategic plan;
- a clearly defined risk culture which emphasises risk management throughout all areas of the business while maintaining independent oversight;
- ongoing analysis of the environment in which the Group operates to proactively address potential risk issues as they arise; and
- supporting commercial decisions and people with appropriate risk processes, systems and controls.

Risk appetite statement (RAS)

Risk Appetite is defined as the level and types of risk the Group is willing to assume within the boundaries of its risk capacity to achieve its strategic objectives. The RAS articulates and supports communication of the Group's appetite to stakeholders. This is important as it provides the definitive view of risk taking activity the Board is comfortable that the Group undertakes and allows decision makers (including those with delegated authority and also those providing oversight) to exercise judgement with greater confidence and speed.

The RAS aligns to the risks identified and defined in the RMF. The design and structure of the RAS has taken into consideration best practice articulated by the European Central Bank which is aimed at ensuring Boards should be strongly involved in the validation process and monitoring of the RAS.

The Group's RAS is prepared by the Group CRO with consideration of the strategic objectives and business model, as well as the environment in which the Group operates. Monthly reporting to Executive Committees and Board includes details of performance against relevant RAS settings, breaches and trends.

Risk policies and procedures

The policy framework is a key component of the Group's RMF providing structure and governance for the consistent, effective management of policies. In developing the policy framework the Group sets the tone that demonstrates the risk culture expected across the organisation. This aligns with the behavioural expectations for all colleagues which form a core part of our performance management approach. Policy statements and supporting policy standards define the minimum control requirements which must be observed across the Group to manage material sources of risk within risk appetite.

Achievements in 2017

Progressing the IRB journey:

In April 2017 the Group submitted an application to the PRA for permission to adopt the IRB approach for the calculation of Credit Risk Weighted Assets (RWAs). The Group is now in active dialogue with the PRA in relation to the application. The IRB programme is also supporting changes in the Collective Provision calculations required by IFRS 9 which will be adopted on 1 October 2018; the programme is on track to commence parallel-run activities in early FY2018. (For further information on IFRS 9, please refer to page 194).

Transitional Service Agreement (TSA) exits:

Significant progress has been made with the build and implementation of a new Credit Risk Engine, to support the TSA exit strategy and also to support the IRB programme. The new Credit Risk Engine is now well into parallel-run, with successful delivery on schedule.

Investing in risk capabilities:

Following the appointment of the Group Chief Risk Officer (CRO) in September 2016, the Risk Management function has restructured to enable a stronger and more granular focus on specific categories of Risk. In addition, several external appointments have been made which have strengthened the Risk team's capabilities, introduced a broader range of external experience and a variety of succession options.

Supporting sustainable growth and operational resilience:

Progressive change continues to be made to support sustainable growth. This has included actions to influence safe lending growth; enhanced policies and controls around regulatory, prudential and operational disciplines, including implementation of improvements to the Group's resilience framework. These enhancements have enabled the Group's digital strategies as well as providing proactive support to achieve a number of the efficiencies and enhancements to the customer journeys, ensuring the Group provides a continuity of service for critical processes.

Embedding the RMF:

The Group rolled out a revised RMF at the start of FY2017. Across the year there has been a focus on embedding the RMF with actions taken across all three Lines of Defence to align to and enhance practices to ensure the RMF has been progressively adopted into routine risk processes and practices. Risk reporting, for example, to the Executive and Board Risk Committees, has also been improved, to ensure that risk owners in the 1st Line of Defence are monitoring, remediating and reporting their own risks in line with the responsibilities defined within the Senior Managers Regime. Risk reporting has also incorporated an increasingly forward looking perspective with a greater focus on not only principal risks but also on emerging risks through the implementation of a 'Top & Emerging Risks' dashboard.

Risk appetite setting:

The approach to Risk Appetite setting was assessed during the year with a number of improvements now adopted within the Board approved RAS for FY2018. This includes: an increase in the number of measures; greater coverage of all risk categories, particularly covering non-financial risks; and a tiered approach to the monitoring of RAS limits to provide earlier warning of any potential breaches.

Priorities for 2018

IRB journey

The Group will continue to work towards achieving approval to adopt the IRB approach, alongside delivering IFRS 9 implementation.

Digitisation and raising cyber awareness

As the industry and environment in which the Group operates evolves, the Group's digital operations continue to be developed through new systems, enhanced monitoring including threat monitoring for potential cyber attacks or increase in fraud related activity. The Group continues to streamline processes, whilst raising awareness of potential threats to the Group through training and education, stress testing and ongoing assurance reviews of key controls, including the management of third party suppliers.

Transitional Service Agreement (TSA) exits:

Priorities for early FY2018 include actions to fully implement the new Credit Risk Engine, cease the reliance on NAB in relation to the calculation of RWAs and the delivery of the Treasury Management System.

Regulatory change

The Group continues to embrace the changing regulatory environment and will remain fully compliant with all applicable current and future regulations. This includes specific requirements such as the General Data Protection Regulation (GDPR) and the Group has, for example, recently taken steps to enhance capabilities in this area by appointing a Group Data Protection Officer (DPO) as a direct report of the Group CRO.

PSD2 changes start to come into effect in January 2018. In addition to enhanced protection for consumers, PSD2 opens up the competitive landscape and in doing so introduces risk for traditional financial services firms. A specific material risk for the Group is disintermediation by third parties. PSD2 also introduces more stringent regulatory requirements for complaint handling and customer authentication increasing the risk of failure to meet regulatory expectations. The Group is well placed to meet the new requirements and is actively adapting its strategy in light of the increased competition and disintermediation risk.

Risk report

Through 2018 the Group will be taking steps to ensure compliance with 'ring fencing' legislation that will take effect from 1 January 2019. The Group will achieve compliance with the legislation with no material changes to its business operations or corporate structure, and with very little impact on the Group's customers. The Group is aware of material changes that other firms will need to make and will support our customers to understand the impact that changes made by other firms may have on them.

Balance sheet risks
The Group remains focussed on maintaining balance sheet strength with particular attention being paid to regulatory developments including the Countercyclical Capital Buffer (CCyB) and MREL. Underpinning this will be a focus on capital, including capital management and any efficiencies that can be applied. The Group will continue to manage its liquidity requirements and funding profile in a prudent manner.

Risk Management Framework (RMF)
While considerable progress has been made during FY2017, work will continue in this regard through FY2018. There will be a continual review, with external support to incorporate industry benchmarking, with any required revisions to be made quickly, reflecting the ongoing and fast pace of change as new risks emerge and evolve.

Cyber and resilience
In addition to the ongoing assessment of the RMF, specific consideration will be given to the oversight and monitoring of the risks relative to both cyber security and cybercrime and, in turn, the resilience of the Group's systems and processes.

Growth and efficiency
The Group continues to drive growth in the lending portfolios. Appetite settings will be monitored to ensure controlled growth, and regulatory guidance relative to areas such as consumer lending will be considered and addressed. Equally, initiatives to deliver efficiencies and simplification across the Group will be subject to continued risk assessment.

Principal risk categories

See page 19 in the Strategic Report for details on the Group's principal risk categories.

Emerging risks

The Group monitors the environment in which it operates to identify emerging risks that may have an impact on its operations and strategy. The Group currently considers its top emerging risks to be:

Macroeconomic environment
With a customer base that remains predominantly UK based, the Group is exposed to inherent risks arising from increased geopolitical uncertainty, which has the potential to impact the UK macroeconomic outlook. The banking sector may be placed under increasing pressure as it is exposed to risks relative to credit conditions which may impact the financial performance of the Group. The Group's credit portfolios will continue to be monitored closely with appetite adjusted where appropriate and risk sensitivity analysis conducted on an ongoing basis. Regular assessments of strategic plans are undertaken to minimise and negate potential impacts.

The UK vote to leave the EU (Brexit)
The Group continues to monitor developments regarding the UK's withdrawal from the European Union and the potential consequences for our customers, products and operating model. As the period of economic uncertainty and market volatility persists, the Group will continue to monitor and assess the external implications and re-evaluate our mitigating actions as appropriate.

Consumer credit
The Group maintains an awareness of the risk of significant unforeseen credit losses occurring within a short time period which has the potential to have a detrimental impact on earnings and profitability. Credit risk strategies, appetite and tolerance levels are reviewed and approved by the Board and regular monitoring of the credit portfolio, including risk sensitivity analysis and reviews of asset quality metrics, is undertaken to ensure early identification and mitigation of potential risk areas. Early identification and mitigation of risks is an area of considerable regulatory focus and one where the Group is particularly alert to the potential regulatory, economic and customer impacts.

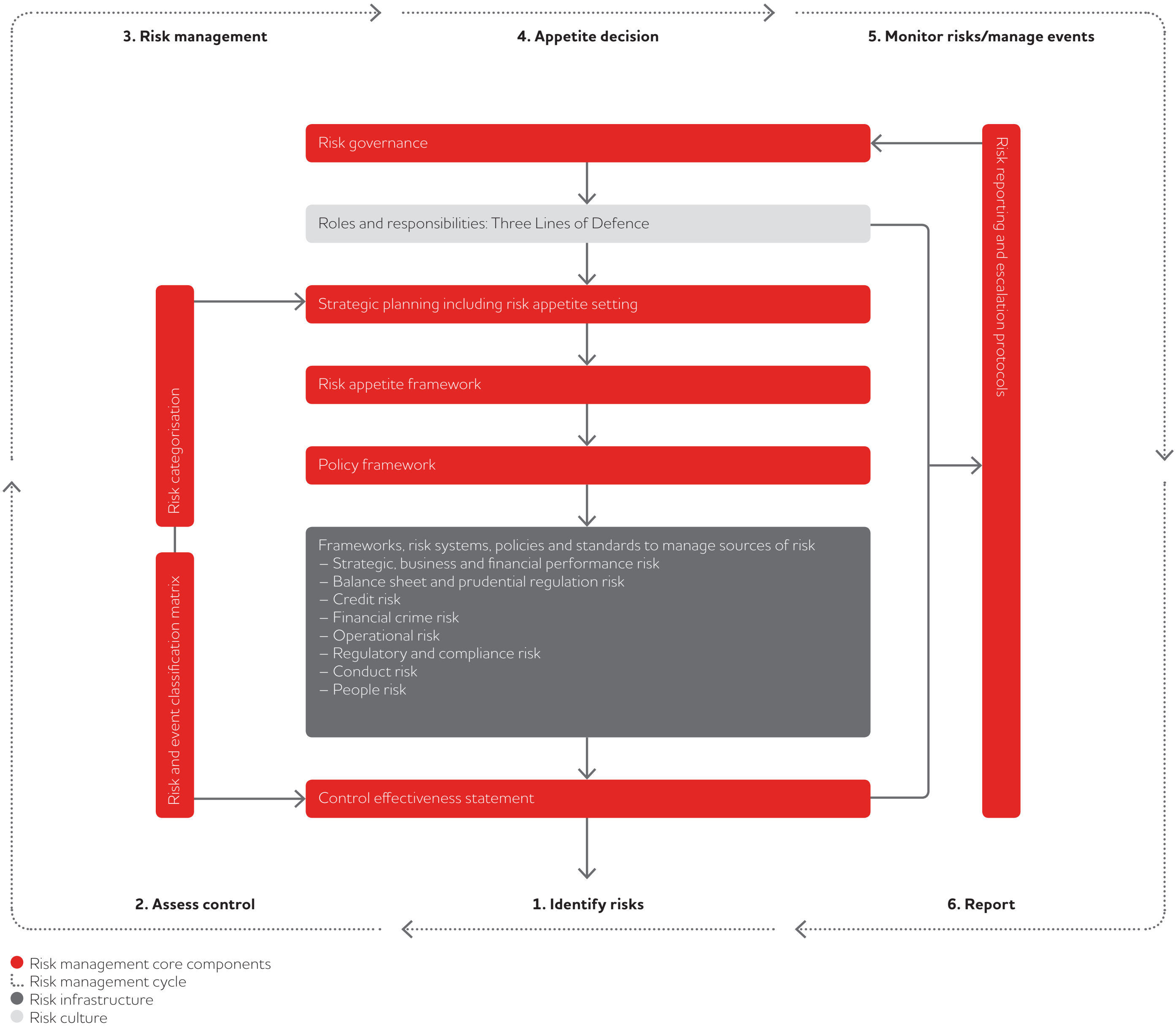
Cyber security and IT
The Group, in line with the industry, is subject to increasing levels of attempted cyber-attack, with criminal groups employing increasingly sophisticated knowledge of financial markets and internal activities/processes, leading to potential reputational and financial detriment. The Group continues to invest in and enhance its information security capabilities, monitoring the external/internal threat landscape and the changing risk profile of the business.

Financial crime (including cybercrime)
The Group is exposed to the risk of its products and services being used to facilitate crime against its customers, third parties or the Group itself. The management of Financial Crime remains a key area of regulatory focus and the Group continues to enhance its framework for monitoring, management and mitigation of financial crime.

Regulatory change
The Group, in common with the financial services industry as a whole, continues to face a significant agenda of regulatory and legislative change, including those pertaining to taxes. Compliance with the developing regulation remains a key focus. The Group continues to monitor the emerging requirements and ensure it is well placed to respond with effective regulatory change management. Specific forthcoming changes, such as Open Banking and PSD2, bring both risk and opportunity to the competitive environment in which the Group operates. Senior management is considering the strategic impacts of these changes for the Group (for further detail on key regulatory changes impacting the Group please see page 17).

Risk Management Framework (RMF)

The Group identifies and manages risk using the RMF (see diagram below), which is the totality of systems, structures, policies, processes and people that identify, measure, evaluate, control, mitigate, monitor and report all internal and external sources of material risk.



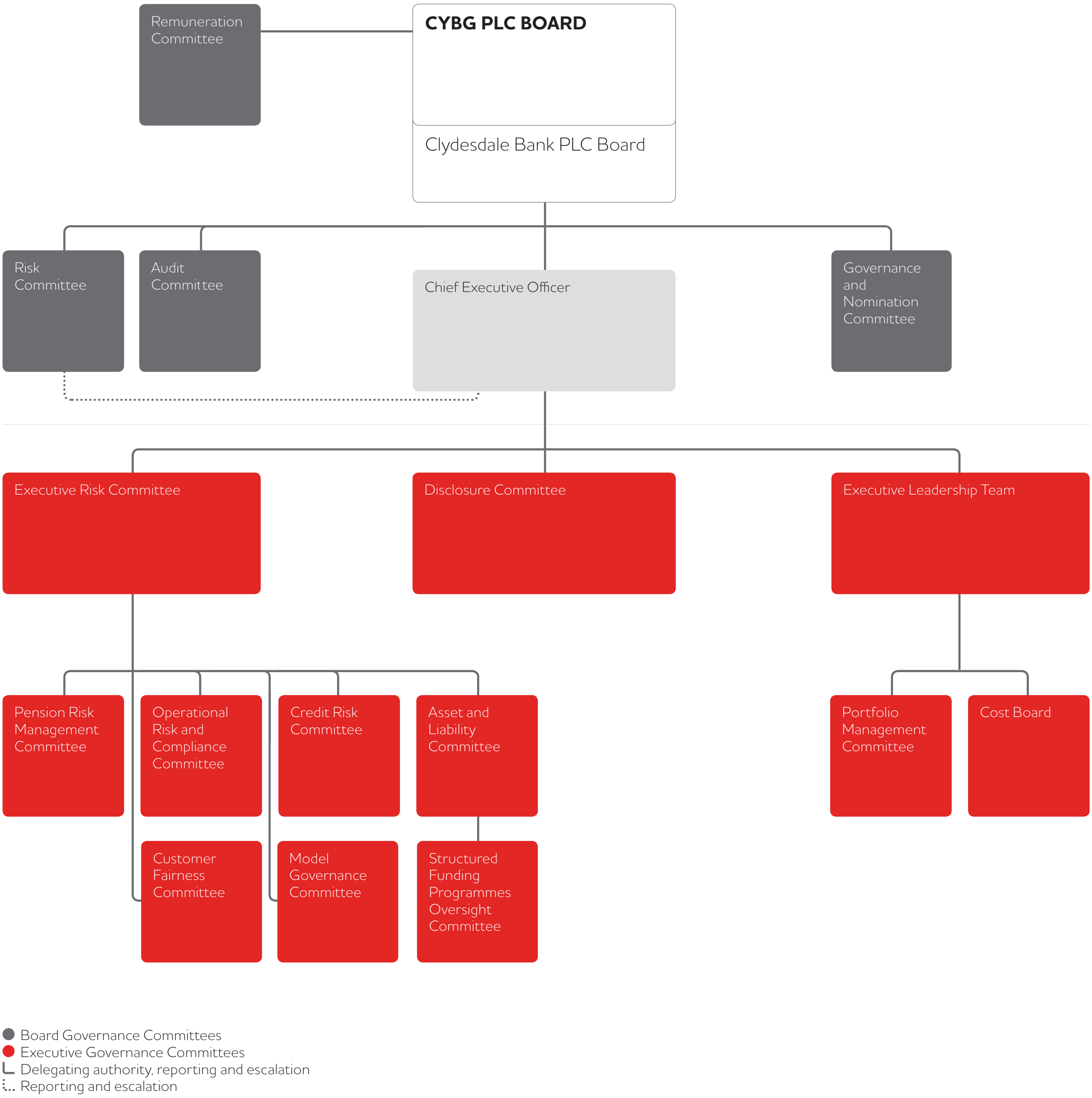
Risk report

Risk governance and oversight

The Group's risk governance structure strengthens risk evaluation and management, while also positioning the Group to manage the changing regulatory environment in an efficient and effective manner.

The Group's risk management is governed via a series of committees, as represented within the diagram which follows.

During the year the Group commenced a review of the executive governance committee layer in the risk governance structure to ensure it balances regulatory, legal and compliance obligations while making timely, customer focused decisions that drive the business forward with any changes expected to be made during 2018 to ensure the framework is both optimal and efficient.



The following Executive level Committees have been established under the authority of the CEO:

Committees	Risk focus
Executive Leadership Team	The Executive Leadership Team supports the CEO to lead the Group to be a strong, customer-focused bank for its communities, by focusing on three business priorities: sustainable growth; efficiency; and capital optimisation
Executive Risk Committee	The Executive Risk Committee supports the CEO in respect of risk and control accountabilities and serves to provide leadership focus on key risk issues including: – endorsing the RAS for approval by the Board; – overseeing and challenging the enterprise wide risk performance and control environment of the Group and business units, including the effective use of policy, frameworks and tools; – monitoring the status of regulatory relationships, the reputation of the Group in relation to its regulators and the changing state of the regulatory landscape including the impacts for and readiness of the Group; – monitoring the strength of risk capability and capacity, including risk training and education plans to ensure an effective risk and control framework; and – reviewing and endorsing risk policies, frameworks and tools for use across the Group.
Disclosure Committee	The Disclosure Committee is responsible for ensuring the Group complies with its continuous disclosure obligations for exchanges on which it has equity and debt securities listed.

The Executive Risk Committee is supported by the following committees:	
Pension Risk Management Committee	The Pension Risk Management Committee is responsible for overseeing pension risk management and strategy. This committee also oversees the interaction with the pension scheme trustees in relation to the risks within the Scheme.
Operational Risk and Compliance Committee	The Operational Risk and Compliance Committee is responsible for ensuring that the RMF and associated policies and standards are fit for purpose and implemented effectively.
Credit Risk Committee	The Credit Risk Committee is responsible for ensuring that the Credit RMF and associated policies remain effective. The committee has oversight of the quality, composition and concentrations of the credit risk portfolio and recommends strategies to adjust the portfolio to react to changes in market conditions.
Asset and Liability Committee (ALCO)	ALCO is responsible for monitoring the performance of the Group against the Board approved capital and funding plans. The committee focuses on the Group's non-traded market risks including capital, funding, liquidity and interest rate risk to ensure that the Group's activity complies with regulatory and corporate governance requirements and also delivers Group policy objectives. The impact of pension risk on capital is also assessed by ALCO.
Structured Funding Programmes Oversight Committee	The Structured Funding Programmes Oversight Committee is responsible for supporting the ALCO in relation to its risk monitoring and oversight responsibilities for all secured funding programmes and supporting the CFO and Treasurer in relation to the compliance of the Regulated Covered Bond (RCB) Programme with FCA regulations and the RCB Sourcebook.
Customer Fairness Committee	The Customer Fairness Committee oversees the effective execution and ongoing development of the Conduct Framework and Customer Fairness Model. It also ensures conduct issues and remediation activities are effectively managed at the appropriate level.
Model Governance Committee	The Model Governance Committee supports the Board in fulfilling its governance responsibilities for material models and rating systems. The Committee oversees the integration and ongoing use of models across the Group, specifically considering the fitness for purpose, usability and scalability of models.

The Executive Leadership Team is supported by the following committees:	
Portfolio Management Committee	The Portfolio Management Committee is responsible for the oversight and management of capital allocation and funding decisions for the product portfolio, related to pricing and sustainable returns.
Cost Board	The Cost Board is the primary forum for the management of costs across the Group. Its primary responsibilities are to approve expenditure within agreed delegated authorities, to oversee business unit expenditure and expense performance and to support the development of a strong expense control culture within the Group.

Risk report

Three Lines of Defence

Effective operation of a Three Lines of Defence model is integral to the Group's approach to risk management and is based on the overriding principle that risk capability must be embedded within the first line of defence teams to be effective. This principle embodies the following concepts:

- commercial decisions are made on the basis of proactive consideration of risk and the impact on customers;
- risk management activities are focused on enhancing sustainable business performance;
- management must use the RMF to support decision making involving risk and reward trade-offs;
- regular assessments are undertaken to confirm the effectiveness of the risk and control frameworks in relation to both the current and emerging risk profile; and
- risk management responsibilities are clearly understood by all colleagues when carrying out their day to day activities.

Control is exercised through a clearly defined delegation of authority, with communication and escalation channels throughout the Group.

1st

Business and enterprise assurance
Responsibility for risk management resides with the business unit director in each area. They are each responsible for ensuring that they have adequate risk coverage and processes in place to ensure they are managing the risks they own within risk appetite and within the guidelines of the RMF. A monthly report of key risks, issues and horizon risks is provided to the Executive Risk Committee. The enterprise assurance function focuses on end-to-end assurance of key processes as well as ensuring risks and controls are being managed appropriately. Reporting is provided to each business unit director as appropriate and to the Executive Risk Committee.

2nd

Risk Management
The risk management team under the Group CRO independently monitors and systematically assesses the Group's risk profile against established risk appetite parameters. Risk management also develops and defines the Group's RMF. They also assist the first line business units in the design and implementation of appropriate risk management policies and strategies and work with the business units to promote awareness of the need to manage risk.

3rd

Internal Audit
Internal Audit's role is to provide independent assurance over the governance, risk management and control framework.

Stress testing

Stress testing is an important and recognised risk management tool, used to assess the vulnerability of financial institutions through the modelling of adverse scenarios. The Group undertakes stress testing, following the Basel Committee principles, and utilising, where appropriate, scenarios provided by the PRA, aimed at understanding potential impacts arising from adverse conditions relevant to its business and to aid the development and understanding of potential management actions and contingency plans.

Stress testing forms an integral part of the overall governance and risk management culture. Involvement from the Board and senior management in the stress-testing programme is essential for its effective operation.

Methodology

Stress testing within the Group complies with regulatory requirements and is subject to a rigorous review and challenge process. The Group's approach ensures that a clear link exists between the economic scenarios and stress-testing outputs, supported by a structured review and sign off process.

While the stress testing process is underpinned by models, it is also reliant on judgements made by senior management and key personnel across the Group who:

- manage the macroeconomic scenario process and prepare and review stressed business plans;
- prepare and review credit stress outputs including impairment charges, RWAs and write offs;
- provide funding and liquidity impacts and construct capital plans based on the outcomes of stress testing; and
- guide on potential management actions in response to stress scenario mitigation.

Reverse stress testing

Reverse stress testing requires a different approach. It starts from an outcome of business failure and identifies instances where this might occur. Severe but plausible scenarios with an unacceptably high risk are used to inform business planning to prevent or mitigate specific business risks. Reverse stress tests are also utilised as the start point for recovery and resolution planning scenarios. The Group also monitors a range of early warning indicators to give management early visibility of potential risks that could give rise to the need to invoke actions in recovery plans.

Stress testing within the Group's risk governance and capital framework

Stress testing outputs are used to inform the strategic planning process and the RAS. The plan is subjected to sensitivity analysis, forming a key element of the planning process from an overall risk assessment perspective, and provides the Board with further detail when looking to approve the plan.

Stress testing informs the assessment and quantification of risk exposures in the course of calculating capital requirements as part of the ICAAP. The Group runs a number of adverse macroeconomic stresses in order to determine the impacts on the Group's financial and capital position, considering changes to impairments, margins, volumes and costs relative to the base case plan and considers the actions which the Group may choose to deploy in response to such events materialising.

Stress testing is also a key feature of the ILAAP where stress-testing scenarios are modelled regularly to provide insight into potential vulnerabilities in the Group's funding and liquidity strategies. Stress-testing results of liquidity are also reported to ALCO on a monthly basis.

The Executive Leadership Team and Board engages at critical points of the stress-testing cycle to provide a robust challenge in relation to the selection and development of scenarios and, thereafter, considers how the results are integrated into future strategic decision making, contingency planning, capital and business planning and risk appetite.

In advance of Board submission, ALCO reviews the scenarios, assumptions and results of liquidity and capital stress testing and provides an initial review and challenge of outputs.

Risk management and internal controls

Assessment of principal risks

The Board is responsible for determining the nature and extent of the principal risks it is willing to take in order to achieve its strategic objectives.

In line with the UK Corporate Governance Code (the Code) requirements, the Directors have performed a robust assessment of the principal risks facing the Group, including those that would threaten its business model and future performance, solvency or liquidity.

The principal risks the Group actively monitors and manages are described on page 19 of the Strategic report.

Risk management and internal controls

The Board actively monitors the Group's risk management and internal control systems. A review of the effectiveness of those systems has been performed incorporating all material controls, including financial, operational and compliance controls.

RISK REPORT

RISK CLASSES

Strongly performing credit portfolios, well positioned for growth

Close monitoring, robust policies and a well-controlled framework support the credit operations of the Group.

Credit risk is the risk that a borrower or counterparty fails to pay the interest or capital due on a loan or other financial instrument.

Credit risk manifests itself in the financial instruments and/or products that the Group offers, and those in which the Group invests (including, among others, loans, guarantees, credit-related commitments, letters of credit, acceptances, inter-bank transactions, foreign exchange transactions, swaps and bonds). Credit risk can be found both on- and off-balance sheet.

Risk appetite

The Group controls the levels of credit risk it takes by placing limits on the amount of risk accepted in relation to one borrower, or group of borrowers, and to geographical, product and industry segments. The management of credit risk within the Group is achieved through both approval and monitoring of individual transactions, regular asset quality analysis of the performance of the various credit risk portfolios, and the independent oversight of credit portfolios across the Group.

Credit strategies and policies

Credit risks associated with lending are managed through the application of detailed lending policies and standards which outline the approach to lending, underwriting criteria, credit mandates, concentration limits and product terms. The Group maintains a dynamic approach to credit management and aims to take necessary steps if individual issues are identified or if credit performance deteriorates, or is expected to deteriorate, due to borrower, economic or sector-specific weaknesses.

Roles and responsibilities for the management, monitoring and mitigation of credit risk within the Group are clearly defined in line with the Group's RMF.

Significant credit risk strategies and policies are approved, and reviewed annually, by the Credit Risk Committee. For complex credit products and services, the Head of Business Risk, Head of Retail Risk and Credit Risk Committee provide a policy framework which identifies and quantifies risks and establishes the means of mitigating such risks. These policies and frameworks are delegated to, and disseminated under the guidance and control of, executive management, with appropriate oversight through governance committees.

Exposures

Credit risk exposures are categorised as Retail (secured and unsecured) and SME.

In terms of loans and advances, credit risk arises both from amounts loaned and commitments to extend credit to customers. To ensure appropriate credit limits exist, especially for SME lending, a single large exposure policy is in place within the Group and forms part of the risk appetite measures that are monitored and reported on a monthly basis. The overall composition and quality of credit portfolio exposures are monitored and periodically reported to the Board and, where required, to the relevant supervisory authorities.

Exposures are also managed in accordance with the large exposure reporting requirements of the CRR.

Unless otherwise noted, the amount that best represents the maximum credit exposure at the reporting date is the carrying value of the financial asset.

Measurement

The Group uses statistical models to measure credit risk exposures. Models are supported by both internal and external data.

The probability of default (PD) (that borrowers will not meet their contractual obligations), current exposures, and the likely loss ratio on defaulted obligations are calculated to measure and mitigate credit risk.

Portfolios are assessed using segmentation for measurement, reporting and monitoring purposes.

Subject to regulatory approval, the Group is progressing toward attaining permission to use IRB models to measure the credit risk of loans and advances to customers.

Meantime, all exposures are measured under the standardised approach for regulatory capital.

Note 3.6 provides details of the Group's approach to the impairment of financial assets and the calculation of impairment charge.

Key credit metrics (audited)

	2017	2016
Impairment charge on credit exposures (£m)		
SME lending (including lease finance)	**33**	31
Retail lending	**15**	8
	48	39
Of which		
Specific charge for impairment losses	**46**	25
Collective charge for impairment losses	**2**	14
	48	39
Impairment provisions held on credit exposures (£m)		
SME lending (including lease finance)	**154**	157
Retail lending	**56**	58
	210	215
Of which		
Specific provision	**56**	64
Collective provision	**154**	151
	210	215
Credit risk adjustments held on loans at fair value (£m)		
SME lending	**11**	24
Of which		
Individually assessed credit risk adjustments	**2**	8
Collectively assessed credit risk adjustments	**9**	16
	11	24
Impairment credits on loans held at fair value	**(6)**	(11)
Past due and impaired assets (£m)		
90+ DPD assets	**161**	150
Impaired assets(1)	**179**	233
Asset quality measures (%)		
90+ DPD plus impaired assets to customer loans	**1.06%**	1.27%
Specific provisions to impaired assets(2)	**32.6%**	30.8%
Net write-offs to customer loans(3)	**0.18%**	0.18%
Total provision to customer loans(4)	**0.69%**	0.79%
Total impairment charge to average customer loans (cost of risk)(5)	**0.14%**	0.09%

(1) Impaired assets for September 2017 and September 2016 includes £4m and £19m of impaired fair value loans respectively.
(2) Total specific provision includes the individually assessed credit risk adjustments on loans at fair value.
(3) Net write-offs includes loans at fair value.
(4) Total provision to customer loans includes the credit risk adjustments on loans at fair value through profit and loss.
(5) Total impairment charge to average customer loans includes loans held at fair value through profit and loss.

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Credit risk

The Group's appetite for lending is strictly defined and adhered to and the strength of the loan book is underpinned by the continued focus on, and maintenance of, high underwriting standards plus early and proactive identification of customers experiencing financial difficulty. The strong lending growth in the year has been delivered in the context of a benign economic environment, which together have contributed to a reduction in the level of impaired loans from £233m to £179m and resulted in the 90+ DPD plus impaired asset ratio falling from 1.27% to 1.06%. While a level of sensitivity to economic shocks remains, no material effects have yet been observed, however, it is accepted a more challenging credit environment is likely to lead to increased impairment from the current low levels.

The increase in impairment charge, from £39m to £48m, reflects a modest increase in charges taken on our unsecured Retail portfolios together with impairment of a small number of historically originated SME exposures. Excluding the individually significant provisions, the underlying level of impairment within the portfolio has remained stable with no sign of material deterioration. The cost of risk has consequently increased by 5bps, but remains low relative to the size of the portfolio.

Within the Retail portfolio, the level of impaired mortgage lending remains modest against a growing book. This reflects the strong credit quality of the portfolio, supported by the low interest rate environment and stable house price indices. The level of 90+ DPD has seen a marginal increase for both secured and unsecured portfolios.

SME asset quality measures continued to improve reflective of the focus on responsible credit decisions and controlled risk appetite which leads to a well-balanced and diverse portfolio. This portfolio will be most susceptible to any material economic downturns following Brexit, in particular any industry specific shocks, e.g. agriculture.

The ratio of total provisions to customer loans reduced by 10bps to 0.69% in the year, driven by the reduced level of specific provisions held for amortised cost and lower collective provision for assets held at fair value. The continued growth in the portfolio has also influenced the decrease in ratio.

Maximum exposure to credit risk (audited)

The table below shows the maximum exposure to credit risk, including derivatives. The maximum exposure is shown gross, before the effect of mitigation through use of master netting and collateral agreements. The table also shows the maximum amount of commitments from the Group's banking operations.

	2017 £m	2016 £m
Cash and balances with central banks (note 3.1)	**6,937**	5,955
Due from other banks	**1,174**	952
Financial assets available for sale (note 3.2)	**2,076**	1,731
Other financial assets at fair value (note 3.3)	**477**	750
Derivative financial assets (note 3.4)	**282**	585
Loans and advances to customers (note 3.5)	**31,293**	29,202
Due from customers on acceptances	**4**	4
	42,243	39,179
Contingent liabilities (note 5.1)	**111**	123
Other credit commitments (note 5.1)	**8,408**	7,690
Maximum credit risk exposure	**50,762**	46,992

Mitigation

The management and mitigation of credit risk within the Group is achieved through both approval and monitoring of individual transactions and asset quality, analysis of the performance of the various credit risk portfolios, and the independent oversight of credit portfolios across the Group. Portfolio monitoring techniques cover such areas as product, industry or geographic concentrations and delinquency trends.

There is regular analysis of the borrower's ability to meet their interest and capital repayment obligations with early support and mitigation steps taken where required. Credit risk mitigation is also supported, in part, by obtaining collateral, and corporate and personal guarantees where appropriate.

Other mitigating measures are described below:

Specialist expertise

Credit quality is managed and monitored by skilled teams including, where required, specialists who provide dedicated support for customers experiencing financial difficulty.

Credit decisions utilise credit scoring techniques and manual underwriting, as appropriate. These tasks are performed by skilled and competent specialists acting within agreed delegated authority levels set in accordance with their experience and capabilities.

Credit policy and adherence to policy standards

Specialist teams oversee credit portfolio performance as well as adherence to credit risk policies and standards. Activities include targeted risk-based reviews, providing an assessment of the effectiveness of internal controls and risk management practices. Bespoke assignments are also undertaken in response to emerging risks and regulatory requirements. Independent assurance reviews are also regularly undertaken by Internal Audit.

Portfolio oversight

Portfolios of credit and related risk exposures and the key benchmarks, behaviours and characteristics by which those portfolios are managed in terms of credit risk exposures, are regularly reviewed. This entails the production and analysis of regular portfolio monitoring reports for review by senior management.

Controls over rating systems

The Group has an Independent Model Validation Unit that sets common minimum standards. The standards are designed to ensure risk models and associated rating systems are developed consistently, and are of sufficient quality to support business decisions and meet regulatory requirements.

Stress testing

Stress test scenarios are regularly prepared with the outcomes reviewed and relevant actions taken. Outputs will typically include impairment charges, RWA, and write-offs. Management will consider how each stress scenario may impact on different components of the credit portfolio. The primary method applied uses migration matrices, modelling the impact of PD rating migrations and changes in portfolio default rates to changes in macroeconomic factors, to obtain a stressed position for the credit portfolios. Loss given default (LGD) is stressed based on property price movements.

The Group also utilises other instruments and techniques across its wider balance sheet. These are summarised below:

Derivatives

The Group maintains control limits on net open derivative positions. At any one time, the amount subject to credit risk is limited to the current fair value of instruments that are favourable to the Group (i.e. assets where their fair value is positive), which, in relation to derivatives, may only be a small fraction of the contract, or notional values used to express the volume of instruments outstanding. This credit risk is managed as part of the customers overall exposure together with potential exposures from market movements.

Master netting agreements

The Group further restricts its exposure to credit losses by entering into master netting arrangements with counterparties with whom it undertakes a significant volume of transactions. Master netting arrangements do not generally result in an offset of balance sheet assets and liabilities, as transactions are usually settled on a gross basis. However, credit risk associated with the favourable contracts is reduced by a master netting arrangement to the extent that, if any counterparty failed to meet its obligations in accordance with the agreed terms, all amounts with the counterparty are terminated and settled on a net basis. Derivative financial instrument contracts are typically subject to the International Swaps and Derivatives Association (ISDA) master netting agreements, as well as Credit Support Annexes (CSA), where relevant, around collateral arrangements attached to those ISDA agreements. Derivative exchange or clearing counterparty agreements exist where contracts are settled via an exchange or clearing house.

Credit assessment and mitigation for Retail and SME customers

The Group uses a variety of lending criteria when assessing applications for Retail customers. The approval process uses credit scorecards, as well as manual underwriting, and involves a review of an applicant's previous credit history using information held by credit reference agencies.

The Group also assesses the affordability of the borrower under stressed scenarios including increased interest rates. In addition, the Group has in place quantitative thresholds, such as maximum limits on the level of borrowing to income and the ratio of borrowing to collateral. Some of these limits relate to internal approval levels and others are hard limits above which the Group will reject the application.

For residential mortgages, the Group's policy is to accept only standard applications with a LTV less than 95%. The Group has maximum percentage LTV limits which depend upon the loan size. Product types such as BTL and residential interest-only mortgages are controlled by transactional limits covering both LTV and value.

For SME customers, credit risk is managed in accordance with lending policies, the Group's risk appetite and the RMF. Lending policies and performance against risk appetite are reviewed regularly. Credit risk is further mitigated by focusing on business sectors where the Group has specific expertise and through limiting exposures on higher value loans and to certain sectors. When making credit decisions for SME customers the Group will routinely assess the primary source of repayment, most typically the cash generated by the customer through its normal trading cycle. Secondary sources of repayment are also considered and while not the focus of the lending decision, collateral will be taken when appropriate. The Group seeks to obtain security cover, and where relevant, personal guarantees from borrowers.

Monitoring

Credit policies and procedures, which are subject to ongoing review, are documented and disseminated in a form that supports the credit operations of the Group.

- *Credit Risk Committee (CRC)* The CRC ensures that the credit RMF and associated policies remain effective. The Committee has oversight of the quality, composition and concentrations of the credit risk portfolio and considers strategies to adjust the portfolio to react to changes in market conditions.
- *RAS measures* Measures are monitored monthly and reviewed bi-annually, at a minimum, to ensure that the measures accurately reflect the Group's risk appetite, strategy and concerns relative to the wider macro environment. All measures are subject to extensive engagement with the Executive Leadership Team and the Board, and are subject to endorsement from executive governance committees prior to Board approval. Regulatory engagement is also scheduled as appropriate.
- *Risk concentration* Concentration of risk is managed by client/counterparty, product, geographical region and industry sector. In addition, single name exposure limits exist to control exposures to a single entity/counterparty. Concentrations are also considered through the RAS process focusing particularly on comparing the portfolio against market benchmarks.
- *Single large exposure excesses* All excesses are reported to the Transactional Credit Committee (TCC) and relevant Head of Risk. Any exposure which continues or is expected to continue beyond 30 days will also be submitted to the TCC with proposals to correct the exposure within an agreed period, not to exceed 12 months.

Concentrations

Loans and advances to customers (audited)

	2017 £m	2016 £m
Overdrafts	**1,524**	1,536
Credit cards	**396**	400
Lease finance	**594**	515
Mortgages	**23,480**	21,836
Other term lending – SME	**4,762**	4,393
Other term lending – Retail	**709**	690
Trade finance	**23**	26
Gross loans and advances to customers	**31,488**	29,396
Accrued interest receivable	**75**	76
Unearned income	**(28)**	(26)
Deferred and unamortised fee income	**(32)**	(29)
Impairment provisions on credit exposures (note 3.6)	**(210)**	(215)
	31,293	29,202

The Group also has a portfolio of fair valued business loans and advances of £477m (2016: £750m) (note 3.3). Combined with the above this is equivalent to total loans and advances of £31,770m (2016: £29,952m).

	2017		2016	
Retail secured credit by loan size concentration (audited)	**£m**	**%**	£m	%
£0–£99k	**4,207**	**17.9%**	4,456	20.4%
£100k–£249k	**6,962**	**29.7%**	6,807	31.2%
£250k–£499k	**7,004**	**29.8%**	6,153	28.2%
£500k–£999k	**4,259**	**18.1%**	3,572	16.3%
£1m–£2.49m	**1,006**	**4.3%**	806	3.7%
> = £2.5m	**42**	**0.2%**	42	0.2%
Total	**23,480**	**100%**	21,836	100%

Retail secured credit average LTVs by loan size (unaudited)(1)	2017			2016		
	Residential	**BTL**	**Total**	Residential	BTL	Total
£0–£99k	**46.6%**	**52.9%**	**47.7%**	47.5%	51.7%	48.2%
£100k–£249k	**59.1%**	**58.6%**	**58.9%**	58.2%	56.4%	57.6%
£250k–£499k	**60.6%**	**60.7%**	**60.6%**	57.7%	60.4%	58.9%
£500k–£999k	**60.0%**	**58.2%**	**59.4%**	56.1%	59.9%	57.5%
£1m–£2.49m	**61.1%**	**48.7%**	**59.3%**	54.6%	49.0%	53.7%
> = £2.5m	**58.1%**	**44.7%**	**57.1%**	50.0%	44.2%	49.6%
Total	**56.9%**	**58.6%**	**57.5%**	54.7%	57.8%	55.8%

(1) LTV of the mortgage portfolio is defined as mortgage portfolio weighted by balance and indexed using the MIAC Acadametrics indices at a given date. Prior period comparatives have been restated on the new basis of indexation, the previous basis adopted the Halifax House Price Index.

Industry concentration of assets

The following tables show the levels of industry concentration of credit risk as at 30 September:

Gross loans and advances to customers including loans designated at fair value through profit or loss (audited)(1)	2017 £m	2016 £m
Government and public authorities	**32**	36
Agriculture, forestry, fishing and mining	**1,454**	1,458
Financial, investment and insurance	**650**	698
Property – construction	**279**	262
Manufacturing	**574**	577
Instalment loans to individuals and other personal lending (including credit cards)	**1,274**	1,344
Property – mortgage	**23,480**	21,836
Asset and lease financing	**594**	515
Other commercial and industrial	**3,630**	3,421
	31,967	30,147

Contingent liabilities and credit-related commitments (audited)	2017 £m	2016 £m
Government and public authorities	**426**	422
Agriculture, forestry, fishing and mining	**375**	382
Financial, investment and insurance	**165**	125
Property – construction	**154**	156
Manufacturing	**588**	658
Instalment loans to individuals and other personal lending (including credit cards)	**1,945**	1,931
Property – mortgage	**2,305**	1,780
Asset and lease financing	**125**	98
Other commercial and industrial	**2,436**	2,261
	8,519	7,813

(1) Includes balances due from customers on acceptances and excludes accrued interest.

Mitigation and management of credit risk

Credit quality of loans and advances
For SME lending, the Group has an internally developed credit rating system, as defined under the Group's credit risk management policy, which uses data drawn from a number of sources to assess the potential risk in lending to the Group's customers. This system assigns an indication of the PD for each customer and can be broadly mapped to external agencies rating scales. Impaired assets consist of SME lending and secured Retail lending where current circumstances indicate that losses of loan principal and/or interest may be incurred.

Description	eCRS[1]	PD
Senior investment grade	1 to 5	0 < 0.11
Investment grade	6 to 11	0.11 < 0.55
Sub-investment grade	12 to 23	0.55 < 99.99

(1) eCRS – electronic Customer Rating System.

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed by reference to the Group's standard credit rating system. The credit rating system is supported by a variety of financial analytics, combined with processed market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories and are derived in accordance with the Group's ratings policy.

The table below represents the credit quality of SME loans and advances that are neither past due nor impaired:

Audited	**2017 £m**	2016 £m
Senior investment grade	**946**	1,077
Investment grade	**1,807**	1,557
Sub-investment grade	**3,873**	3,533
	6,626	6,167

Credit quality of loans held at fair value through profit and loss that are neither past due nor impaired:

Audited	**2017 £m**	2016 £m
Senior investment grade	**3**	6
Investment grade	**231**	259
Sub-investment grade	**237**	466
	471	731

For Retail lending, the Group has developed specific credit rating systems for both origination of new lending and for ongoing customer and account management purposes. These systems assign risk estimates to all Retail lending and enable active management of customer exposures and portfolios.

Collateral

Collateral held as security and other credit enhancements
The Group evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Group upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held can vary, but may include:

– specific charges over defined assets of the counterparty;

– a floating charge over all assets and undertakings of an entity, including uncalled capital and called but unpaid capital;

– specific or interlocking guarantees; and

– loan agreements which include affirmative and negative covenants and in some instances guarantees of counterparty obligations.

Generally, the Group does not take possession of collateral it holds as security or call on other credit enhancements that would result in recognition of an asset on its balance sheet.

It is the Group's policy to dispose of repossessed properties with the proceeds used to reduce or repay the outstanding balance. In general, the Group does not occupy repossessed properties for its own business use.

The LTV ratio of Retail mortgage lending, coupled with the relationship of the debt to customers' income, is key to the credit quality of these loans. The table below sets out the indexed LTV analysis of the Group's Retail mortgage stock.

LTV (audited)[1]	2017 %	2016 %
Less than 50%	**33**	34
50% to 75%	**49**	50
76% to 80%	**7**	6
81% to 85%	**4**	4
86% to 90%	**4**	2
91% to 95%	**1**	1
96% to 100%	**–**	–
Greater than 100%	**–**	–
Unknown	**2**	3
	100	100

(1) LTV of the mortgage portfolio is defined as mortgage portfolio weighted by balance and indexed using the MIAC Acadametrics indices at a given date. Unknown represents loans where data is not currently available due to front book data matching still to be completed and a *de minimis* amount due to weaknesses in historic data capture processes. Prior period comparatives have been restated on the new basis of indexation, previous basis adopted the Halifax House Price Index.

Residential mortgages
Residential property is the Group's main source of collateral and means of mitigating loss in the event of the default credit risk inherent in its residential mortgage portfolios. All lending activities are supported by an appropriate form of valuation using either professional or indexed (subject to policy rules and confidence levels) valuations.

Commercial property
Commercial property is the Group's main source of collateral on SME lending and means of mitigating loss in the event of default. Collateral for the majority of commercial loans comprises first legal charges over freehold or long leasehold property (including formal Companies House registration where appropriate).

Non-property related collateral
In addition to residential and commercial property based security, the Group also takes other forms of collateral when lending. This can involve obtaining security against the underlying loan through the use of cash collateral and/or netting agreements, both of which reduce the original exposure by the amount of collateral held, subject to volatility and maturity adjustments where applicable.

The Group also operates a policy of obtaining security against the underlying loan via the use of guarantees, which can be either limited or unlimited, making the guarantor liable for only a portion or all of the debt.

The following table shows the total non-property collateral held by sector at 30 September in terms of cash, guarantees (these guarantors are predominantly other financial institutions who are considered to be of a high credit quality) and netting. The exposure amount shown below is the total gross exposure (before any credit risk mitigation and credit conversion factors have been applied where applicable) for arrangements which have some form of associated collateral held against it and is not the total exposure for each asset class, as disclosed elsewhere in this section.

2017 (audited)	**Cash £m**	**Guarantee £m**	**Netting £m**	**Total £m**	**Exposure £m**
Central government or central banks	**3,264**	**–**	**–**	**3,264**	**4,629**
Corporates	**27**	**25**	**42**	**94**	**104**
Financial institutions	**874**	**–**	**–**	**874**	**970**
Past due items	**–**	**–**	**–**	**–**	**4**
Public sector entities	**–**	**–**	**–**	**–**	**–**
Regional government or local authorities	**–**	**–**	**59**	**59**	**59**
Retail	**–**	**–**	**–**	**–**	**–**
Secured by mortgages on commercial real estate	**3**	**–**	**31**	**34**	**74**
Secured by mortgages on residential property	**1**	**–**	**3**	**4**	**9**
	4,169	**25**	**135**	**4,329**	**5,849**

2016 (audited)	Cash £m	Guarantee £m	Netting £m	Total £m	Exposure £m
Central government or central banks	721	–	–	721	1,027
Corporates	49	40	32	121	135
Financial institutions	504	–	–	504	600
Past due items	–	–	–	–	3
Public sector entities	–	–	–	–	–
Regional government or local authorities	–	–	94	94	94
Retail	–	–	–	–	–
Secured by mortgages on commercial real estate	4	–	35	39	107
Secured by mortgages on residential property	2	–	3	5	12
	1,280	40	164	1,484	1,978

The increase in cash collateral held and corresponding exposure is due to increased repurchase (repo) and similar transactions outstanding at 30 September 2017 (including TFS drawings), reflected within Central Governments or Central Banks. The increase in cash collateral held and corresponding exposure in financial institutions is due to an increase in the reimbursement receivable from NAB in relation to the conduct indemnity deed (described further in note 3.14).

Corporates is the largest sector utilising other risk mitigation techniques, with all three methods utilised dependent on credit quality. The extent to which these will be used is dependent on the specific circumstances of the customer.

Forbearance

Forbearance is considered to take place when the Group grants concessions to assist customers who are experiencing, or who are about to experience, difficulties in meeting their financial commitments to the Group. The Group's forbearance policies and definitions comply with the guidance established by the European Banking Authority for financial reporting. Forbearance concessions include the granting of more favourable terms and conditions than those provided either at drawdown of the facility or which would not ordinarily be available to other customers with a similar risk profile. Forbearance parameters are regularly reviewed and refined as necessary to ensure they are consistent with the latest industry guidance and prevailing practice, as well as ensuring that they adequately capture and reflect the most recent customer behaviours and market conditions. The Group makes every effort to treat customers fairly and aligns its forbearance practices to that principle.

While forbearance alone is not necessarily an indicator of impaired status, it is a trigger for the review of the customer's credit profile and forbearance is only granted when there is a realistic prospect of the customer repaying all facilities in full. If there is any concern over future cash flows and the Group incurring a loss, then forborne loans will also be classified as impaired in accordance with the Group's impairment policy.

Exposures classified as forborne and performing at the date forbearance measures are granted, continue to be reported as subject to forbearance for a minimum period of two years from that date (the probation period). Exposures classified as forborne and which are non-performing when customers were granted forbearance cannot exit non-performing status for a minimum of 12 months from the date forbearance was granted, and cannot exit forbearance status for a further two years from the date of returning to performing status (three years in total).

The Group has identified a number of situations that in isolation are not considered to be forbearance:

- facilities that have been temporarily extended pending review and where no concession has been granted for reasons relating to the actual or apparent financial stress of a customer;
- a reduction in asset quality to a level where actual, or apparent, financial stress is not evident;
- where changes are made to the terms of a borrower's interest structure or repayment arrangement on a commercial basis; and
- late provision of financial information, in the absence of other indicators of financial difficulty, is not in all cases considered a non-commercial breach of non-financial covenants.

For both Retail and SME, where the Group has made a demand for repayment, the customer's facilities have been withdrawn or where a debt repayment process has been initiated, the exposure is classified as forborne if the debt is subject to any of the mentioned forbearance concessions.

Retail forbearance

The Group utilises various forbearance measures for retail customers, specific to the individual customer and their circumstances. Customers may potentially be subject to more than one forbearance strategy at any one time where this is considered to be the most appropriate course of action.

Debt management for mortgage customers in financial difficulty

To support customers who are encountering financial difficulties, cases are managed on an individual basis, with the circumstances of each customer considered separately and the action taken judged as being affordable and sustainable for the customer. Operationally, the provision and review of such assistance is controlled by various methods. These include the application of an appropriate policy framework, controls around the execution of policy, regular review of the different treatments to confirm that they remain appropriate, monitoring of customers' performance including the level of payments received, and management visibility of the nature and extent of assistance provided and the associated risk.

Help is provided through the Financial Care Team where tailored repayment programmes can be agreed. Customers are actively supported and referred to free money advice agencies when they have multiple credit facilities, including those at other lenders, that require restructuring.

One component of the Group's approach is to contact customers showing signs of financial difficulty to discuss their circumstances and offer solutions to prevent their accounts falling into arrears.

The tables below summarise the level of forbearance in respect of the Group's mortgage portfolio at 30 September:

As at 30 September 2017 (audited)	**Total Retail loans and advances subject to forbearance measures**			**Impairment allowance on Retail loans and advances subject to forbearance measures**	
	Number of loans	**Gross carrying amount £m**	**% of total portfolio**	**Impairment allowance £m**	**Coverage %**
Formal arrangements	**1,614**	**164**	**0.69**	**3.9**	**2.43**
Temporary arrangements	**1,418**	**174**	**0.74**	**3.0**	**1.72**
Interest-only conversion	**202**	**30**	**0.13**	**0.2**	**0.56**
Term extension	**149**	**12**	**0.05**	**0.1**	**0.51**
Other	**29**	**2**	**0.01**	**–**	**0.61**
Legal	**167**	**16**	**0.07**	**0.9**	**5.66**
	3,579	**398**	**1.69**	**8.1**	**2.04**

As at 30 September 2016 (audited)	Total Retail loans and advances subject to forbearance measures			Impairment allowance on Retail loans and advances subject to forbearance measures	
	Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance £m	Coverage %
Formal arrangements	1,843	169	0.78	5.5	3.27
Temporary arrangements	1,460	160	0.73	2.7	1.68
Interest-only conversion	154	22	0.10	0.1	0.26
Term extension	123	11	0.05	0.1	0.61
Other	22	2	0.01	–	0.84
Legal	195	20	0.09	1.1	5.60
	3,797	384	1.76	9.5	2.48

The Group also has a number of customers with interest-only mortgages past maturity, not subject to forbearance. The Group has formal processes embedded to proactively track and facilitate prematurity customer engagement to bring the cases to a formal conclusion, which is generally aimed to be achieved within six months after the loan has reached maturity. Complex cases can take longer than this to reach conclusion. At 30 September 2017, the Group had 97 (2016: 102) customers with interest-only mortgages not subject to forbearance and which were post six-month maturity with a total value of £14m (2016: £12m).

A further forbearance reserve of £4m (2016: £4m) is presently held within the overall collective provision. The effect of this on the above tables would be to increase the impairment allowance noted above to £12.1m (2016: £13.5m) and to increase overall coverage to 3.05% (2016: 3.52%). When all other avenues of resolution including forbearance have been explored, the Group will take steps to repossess and sell underlying collateral. In the year to 30 September 2017, there were 50 repossessions of which 13 were voluntary (2016: 78 including 27 voluntary).

Retail forbearance – unsecured consumer credit

The Group currently exercises limited forbearance strategies in relation to other types of consumer credit, including current accounts, unsecured loans and credit cards. The Group has assessed the total loan balances subject to forbearance on other types of consumer credit to be £11m at 30 September 2017 (2016: £14m), representing 1.02% of the unsecured Retail portfolio (2016: 1.33%). Impairment provisions on forborne balances totalled £3.1m at 30 September 2017 (2016: £4.2m), providing overall coverage of 27.18% (2016: 29.02%).

SME forbearance

Forbearance is considered to exist for SME customers where one or more concessions are granted on a non-commercial basis. The Group reports SME forbearance at a customer level and at a value which incorporates all facilities and the related impairment allowance, irrespective of whether each individual facility is subject to forbearance. Authority to grant forbearance measures for SME customers is held by the Group's Strategic Business Services unit and is exercised, where appropriate, on the basis of detailed consideration of the customer's financial position and prospects.

Where a customer is part of a larger group, forbearance is exercised and reported across the Group at the individual entity level. Where modification of the terms and conditions of an exposure meeting the criteria for classification as forbearance results in derecognition of loans and advances from the balance sheet and the recognition of a new exposure, the new exposure shall be treated as forborne.

The tables below summarise the total number of arrangements in place and the loan balances and impairment provisions associated with those arrangements.

	Total SME loans and advances subject to forbearance measures			**Impairment allowance on SME loans and advances subject to forbearance measures**	
As at 30 September 2017 (audited)	**Number of loans**	**Gross carrying amount £m**	**% of total portfolio**	**Impairment allowance £m**	**Coverage %**
Term extension	**206**	**190**	**2.58**	**12.8**	**6.71**
Deferral of contracted capital repayments	**109**	**141**	**1.91**	**20.4**	**14.47**
Reduction in contracted interest rate	**3**	**1**	**0.02**	**–**	**3.37**
Alternative forms of payment	**5**	**28**	**0.37**	**8.1**	**29.40**
Debt forgiveness	**3**	**11**	**0.15**	**1.4**	**12.70**
Refinancing	**19**	**33**	**0.44**	**4.4**	**13.41**
Covenant breach/reset/waiver	**50**	**155**	**2.11**	**8.1**	**5.24**
	395	**559**	**7.58**	**55.2**	**9.88**

	Total SME loans and advances subject to forbearance measures			Impairment allowance on SME loans and advances subject to forbearance measures	
As at 30 September 2016 (audited)	Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance £m	Coverage %
Term extension	350	320	4.43	25.3	7.90
Deferral of contracted capital repayments	118	143	1.99	18.2	12.69
Reduction in contracted interest rate	7	8	0.12	0.6	7.01
Alternative forms of payment	7	35	0.48	11.2	32.37
Debt forgiveness	8	26	0.36	2.4	9.16
Refinancing	22	51	0.70	4.9	9.76
Covenant breach/reset/waiver	62	208	2.88	8.6	4.12
	574	791	10.96	71.2	8.99

Included in other financial assets at fair value is a portfolio of loans that is included in the above table. The value of fair value loans subject to forbearance at 30 September 2017 is £45m (2016: £101m), representing 0.61% of the total SME portfolio (2016: 1.40%). Impairment allowances on these amounts totalled £4m (2016: £11m), a coverage of 8.89% (2016: 10.82%).

Credit quality of customer lending

An assessment of the credit quality of loans and advances to customers is shown below:

Distribution of loans and advances to customers by credit quality (audited)

As at 30 September 2017	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending[1] £m	Total £m
Gross loans and advances:							
Neither past due nor impaired	51	384	635	23,104	572	6,054	**30,800**
Past due but not impaired	7	12	16	327	22	129	**513**
Impaired	–	–	–	49	–	126	**175**
	58	396	651	23,480	594	6,309	**31,488**

As at 30 September 2016	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending[1] £m	Total £m
Gross loans and advances:							
Neither past due nor impaired	57	388	612	21,485	502	5,665	28,709
Past due but not impaired	6	12	15	285	11	144	473
Impaired	–	–	–	66	2	146	214
	63	400	627	21,836	515	5,955	29,396

(1) SME lending includes business overdrafts.

Credit risk categorisation	Description
Neither past due nor impaired	Loans that are not in arrears and where there is no objective evidence of impairment.
Past due but not impaired	Loans that are in arrears but have not been individually assessed as impaired.
Impaired	Loans which have been individually assessed for impairment as there is objective evidence of impairment, including changes in customer circumstances.

Loans and advances which were past due but not impaired

Loans and advances that are past due but not impaired are classified as such for secured lending, where the net current market value of supporting security is sufficient to cover all principal, interest and other amounts (including legal, enforcement, realisation costs etc.) due on the facility.

Unsecured retail lending and credit cards are written off when they reach 180 DPD and are not designated as impaired, in compliance with the EU Payment Accounts Directive.

The distribution of gross loans and advances that are past due but not impaired is analysed below:

2017 (audited)	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending[1] £m	Total £m
1 to 29 DPD	**5**	**6**	**6**	**142**	**22**	**88**	**269**
30 to 59 DPD	**1**	**2**	**3**	**32**	**–**	**10**	**48**
60 to 89 DPD	**–**	**1**	**2**	**30**	**–**	**2**	**35**
Past due 90 days and over	**1**	**3**	**5**	**123**	**–**	**29**	**161**
	7	**12**	**16**	**327**	**22**	**129**	**513**

2016 (audited)	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending(1) £m	Total £m
1 to 29 DPD	5	6	6	81	11	82	191
30 to 59 DPD	–	2	3	65	–	27	97
60 to 89 DPD	–	1	2	28	–	4	35
Past due 90 days and over	1	3	4	111	–	31	150
	6	12	15	285	11	144	473

Movement in impairment provisions throughout the year

2017 (audited)	**Retail overdrafts £m**	**Credit cards £m**	**Other retail lending £m**	**Mortgages £m**	**Lease finance £m**	**SME lending(1) £m**	**Total £m**
Opening balance	**3**	**6**	**10**	**39**	**2**	**155**	**215**
Charge for the year	**2**	**6**	**9**	**(2)**	**–**	**33**	**48**
Amounts written off	**(4)**	**(9)**	**(13)**	**(4)**	**–**	**(45)**	**(75)**
Recoveries of amounts written off in previous years	**3**	**4**	**6**	**–**	**–**	**5**	**18**
Other(2)	**–**	**–**	**–**	**–**	**–**	**4**	**4**
Closing balance	**4**	**7**	**12**	**33**	**2**	**152**	**210**
Specific	**–**	**–**	**–**	**13**	**–**	**43**	**56**
Collective	**4**	**7**	**12**	**20**	**2**	**109**	**154**
	4	**7**	**12**	**33**	**2**	**152**	**210**

2016 (audited)	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending(1) £m	Total £m
Opening balance	5	7	11	39	2	166	230
Charge for the year	(1)	3	5	1	1	30	39
Amounts written off	(4)	(9)	(14)	(2)	–	(39)	(68)
Recoveries of amounts written off in previous years	4	5	7	1	–	1	18
Other(2)	(1)	–	1	–	(1)	(3)	(4)
Closing balance	3	6	10	39	2	155	215
Specific	–	–	–	19	1	44	64
Collective	3	6	10	20	1	111	151
	3	6	10	39	2	155	215

(1) SME lending includes business overdrafts.
(2) Other includes the recognition of certain impaired loans which were previously recorded at Fair Value Through Profit or Loss, the unwind of net present value elements of specific provisions and other minor movements.

Movement in gross impaired loan balances throughout the year (unaudited)

	2017 £m	2016 £m
Opening balance	**214**	238
New	**72**	96
Write-off	**(49)**	(41)
Returned to performing	**(62)**	(79)
Closing balance	**175**	214

In addition to the gross impaired loans, there were also £4m and £19m impaired fair value loans for September 2017 and September 2016 respectively.

Other credit risks

The Group is exposed to credit risk on its other banking activities, which are subject to mitigation and monitoring. No provisions are currently held for these exposures.

The table below shows the maximum exposure to credit risk for the components of the balance sheet excluding loans and advances to customers and other financial assets at fair value. The maximum exposure is shown gross, before the effect of mitigation through use of master netting and collateral agreements. The table also shows the maximum amount of commitments from its banking operations.

Maximum exposure to credit risk (audited)

	2017 £m	2016 £m
Cash and balances with central banks (note 3.1)	**6,937**	5,955
Due from other banks	**1,174**	952
Financial assets available for sale (note 3.2)	**2,076**	1,731
Derivative financial assets (note 3.4)	**282**	585
	10,469	9,223
Contingent liabilities (note 5.1)	**111**	123
Other credit commitments (note 5.1)	**8,408**	7,690
Maximum credit risk exposure	**18,988**	17,036

£5.9bn of cash is held with the BoE. Due from other banks is all with senior investment grade counterparties. Available for sale financial assets and the credit rating of counterparties are discussed in note 3.2.

Offsetting of financial assets and liabilities

The Group does not have any financial assets or financial liabilities that are offset with the net amount presented on the balance sheet. This is because IAS 32 'Financial Instruments – Presentation' states that there should be both an enforceable right to set off and the intention either to settle on a net basis or to realise the asset and settle the liability simultaneously. Neither of these conditions are met by the Group. The table below illustrates the amounts for financial instruments that are covered by enforceable netting arrangements (i.e. offsetting agreements and any related financial collateral). The table excludes financial instruments not subject to offset and that are only subject to collateral arrangements (e.g. loans and advances).

The net amounts presented in the table are not intended to represent the Group's exposure to credit risk, as the Group will use a wide range of strategies to mitigate credit risk in addition to netting and collateral.

2017 (audited)	**Gross amounts £m**	**Gross amounts offset on balance sheet £m**	**Net amounts presented on balance sheet[(1)] £m**	**Net amounts not offset on balance sheet: Financial instruments £m**	**Net amounts not offset on balance sheet: Cash collateral pledged/ received £m**	**Net amount £m**
Assets						
Derivative financial instruments[(2)]	**282**	**–**	**282**	**(72)**	**(21)**	**189**
Liabilities						
Derivative financial instruments[(2)]	**376**	**–**	**376**	**(72)**	**(203)**	**101**
Securities sold under repurchase agreement	**1,864**	**–**	**1,864**	**(1,864)**	**–**	**–**

2016 (audited)	Gross amounts £m	Gross amounts offset on balance sheet £m	Net amounts presented on balance sheet[(1)] £m	Net amounts not offset on balance sheet: Financial instruments £m	Net amounts not offset on balance sheet: Cash collateral pledged/ received £m	Net amount £m
Assets						
Derivative financial instruments[(2)]	585	–	585	(306)	(55)	224
Liabilities						
Derivative financial instruments[(2)]	598	–	598	(306)	(245)	47
Securities sold under repurchase agreement	1,226	–	1,226	(1,226)	–	–

(1) Collateral amounts (cash and non-cash financial collateral) are reflected at their fair value; however, this amount is limited to the net balance sheet exposure in order to exclude any over collateralisation.
(2) Derivative financial instruments comprise both trading and hedging derivative assets and liabilities.

Derivative financial instrument contracts are typically subject to ISDA master netting agreements, as well as CSAs, where relevant, around collateral arrangements attached to those ISDA agreements, or derivative exchange or clearing counterparty agreements if contracts are settled via an exchange or clearing house. The amounts included in the Financial instruments column refer to amounts that are subject to relevant close out netting arrangements under a relevant ISDA agreement.

Balance sheet and prudential regulation risks

Strong foundations supporting resilience and growth

A robust balance sheet position underpinned by the alignment of risk appetite to strategy and a proactive approach to addressing the impact of changing regulatory obligations.

Balance sheet risks in the financial services industry are highly regulated with ongoing changes in the regulatory environment expected to influence the risks and their management. The key risks include capital, liquidity and funding risks, market risk which in the case of the Group is non-traded market risk (incorporating interest rate and foreign exchange risks), pension risk and non-traded equity risk.

Risk appetite

The primary objective for the management of balance sheet risks is to maintain the risk profile within approved risk limits, to maintain the confidence of the Group's customers and other stakeholders. Balance sheet risks are also managed to protect current and future earnings from the impact of market volatility. The Group applies a prudent approach to balance sheet risks in order to safeguard the ongoing strength and resilience of the balance sheet.

Risk appetite is approved for balance sheet risks by the Board, with authority delegated to ALCO for subsequent implementation and monitoring. The Board has established a range of measures of risk appetite for capital including CET1, leverage and minimum holdings of capital. Measures for funding and liquidity risks consider the structure of the balance sheet and include, among others, measures relating to the proportion of customer funding, the Group's overall funding profile and an overall liquidity adequacy rule (OLAR). The OLAR covers the Board's appetite in relation to regulatory liquidity requirements and also covers the need to maintain access to liquidity resources sufficient to accommodate outflows of funds in a range of stress scenarios over a three-month period.

The Group's participation in wholesale markets, along with its use of financial instruments, is to fund its banking activities and to manage the liquidity and interest rate risks arising from these activities. The Group establishes an appetite for these risks based on an overriding principle that the Group will not engage in proprietary risk taking.

Capital

Capital is held by the Group to protect its depositors, to cover inherent risks in a normal and stressed operating environment and to support the Group's strategy of sustainable growth. Capital risk is the risk that the Group has insufficient quantity or quality of capital to support its operations.

Mitigation measures

The Group's Capital Risk Policy Standard provides the framework for the manner in which capital is managed within the Group. The objectives of the policy standard are to manage efficiently the capital base to optimise shareholder returns while maintaining robust capital adequacy, meeting regulators' requirements, managing the ratings agencies' assessment of the Group and ensuring that excessive leverage is not taken. A shortfall in capital resources would occur when the Group exceeds its risk appetite and is at risk of not having sufficient capital to support future growth objectives.

Measurement

The Group manages capital in accordance with prudential rules issued by the PRA and FCA, which implemented CRD IV legislation with effect from 1 January 2014. The Group's approach to Pillar 1 is to use the standardised approaches to calculating RWAs. The standardised approaches are inherently conservative and the Group is developing the capability to utilise IRB methods for the calculation of credit risk capital. A waiver to utilise IRB models was submitted to the PRA during 2017.

A rigorous approach is taken to assess risks that are not adequately covered by Pillar 1, including interest rate risk and pension risk. The Group also undertakes a range of stress scenarios in order to test the impact on capital arising from severe yet plausible scenarios. These approaches to capital are thoroughly documented in the Group's ICAAP and this is subject to review, challenge and approval by the Board.

Capital buffers

The regulatory capital buffer framework is intended to ensure firms maintain a sufficient amount of capital above their regulatory minimum in order to withstand periods of stress. The UK is implementing the provisions on capital buffers outlined in the CRD to create combined capital buffers including a Capital Conservation Buffer (CCB); a Countercyclical Capital Buffer (CCyB); a Global Systemically Important Institution Buffer; and a Systemic Risk Buffer (SRB). In the UK, the CCB has been introduced with transitional provisions from 2016 (0.625%) to 2019 (2.5%).

The CCyB has been effective from 1 May 2014 and is dependent upon the BoE view of credit conditions in the economy. On 27 June 2017, the BoE Financial Policy Committee (FPC) increased the UK CCyB rate to 0.5%, from 0%, to take effect from 27 June 2018. Absent a change in the outlook, and consistent with its stated policy for a standard risk environment and of moving gradually, the FPC expects to increase the rate to 1% at its November 2017 meeting which will take effect in November 2018.

The Group's capital planning considers the impact of all relevant capital buffers.

↓ CET1	↑ LDR	↑ LCR
12.4%	115%	164%
2016: 12.6%	2016: 112%	2016: 140%

The PRA's final rules on the approach to identifying other systemically important institutions (O-SII) were published in February 2016. In line with expectations, the Group's principal subsidiary, Clydesdale Bank PLC was not designated an O-SII. Similarly the FPC issued its final framework for setting the SRB in May 2016. This confirmed that banks with total assets of less than £175bn (which includes the Group) will be subject to a 0% SRB.

Minimum requirement for own funds and eligible liabilities (MREL)

In November 2016, the BoE provided additional information on how MREL will be applied to firms that are subject to the use of resolution tools that the BoE would employ in the event of a firm entering resolution. From 1 January 2022, those firms, which include the Group, will be required to hold both their going-concern requirements together with additional MREL of an amount equal to those going concern requirements. The timetable for meeting MREL has been extended to 2022 and the BoE will review calibration and transition by the end of 2020, before setting end-state MREL. Interim MREL has been established for the transitional period.

Monitoring

The capital plan is approved by the Board on an annual basis. The Group's ALCO monitors the capital plan and forecast positions on a monthly basis. This ensures that performance trends are appropriately reviewed and that there is transparency on the impact on capital ratios, risk appetite and the future outlook.

Recent developments

Information on banking reform, ring-fencing and resolution, all of which may impact the Group's capital and funding structures, are provided in the regulatory and political environment update on page 17.

Balance sheet and prudential regulation risks

Capital position

The Group's capital position as at 30 September is summarised below:

Regulatory capital (unaudited)[1]

CET1 capital	2017 £m	2016 £m
Capital instruments	**88**	88
Retained earnings and other reserves	**2,854**	2,673
Regulatory adjustments and deductions		
Defined benefit pension fund assets[2]	**(135)**	–
Prudent valuation adjustment[3]	**(4)**	(7)
Intangible assets[4]	**(339)**	(256)
Deferred tax asset relying on future profitability[5]	**(28)**	(35)
Cash flow hedge reserve	**1**	(66)
	2,437	2,397
Tier 1 capital		
Additional Tier 1 (AT1) capital instruments	**450**	450
Total Tier 1 capital	**2,887**	2,847
Tier 2 capital		
Subordinated debt	**473**	474
Credit risk adjustments	**154**	151
Total Tier 2 capital	**627**	625
Total capital	**3,514**	3,472

(1) This table shows the capital position on a CRD IV 'fully loaded' basis.
(2) The defined benefit pension fund asset (net of deferred tax liabilities) does not qualify as capital for regulatory purposes.
(3) A prudent valuation adjustment is applied in respect of fair-valued instruments as required under regulatory capital rules.
(4) Intangible assets shall be deducted from capital for regulatory purposes.
(5) Under CRD IV, deferred tax assets that rely on future profitability are deducted from CET1 capital.

Reconciliation of statutory total equity to regulatory capital (unaudited)	2017 £m	2016 £m
Statutory total equity	**3,402**	3,211
Deductions from capital	**(478)**	(263)
Deferred tax asset relying on future profitability	**(28)**	(35)
Cash flow hedge reserve	**1**	(66)
Foreseeable AT1 dividends and charges	**(10)**	–
Regulatory Tier 1 capital	**2,887**	2,847

Regulatory capital flow of funds (unaudited)	CRD IV 2017 £m	CRD IV 2016 £m
CET1 capital		
CET1 capital at 1 October	**2,397**	2,405
Share for share exchange and nominal reduction	**–**	(135)
Share premium	**–**	(670)
Retained earnings and other reserves (including structured entities)	**181**	576
Prudent valuation adjustment	**3**	(2)
Intangible assets	**(83)**	9
Deferred tax asset relying on future profitability	**7**	238
Defined benefit pension fund assets	**(135)**	42
Cash flow hedge reserve	**67**	(66)
CET1 capital at 30 September	**2,437**	2,397
Tier 1 capital		
Tier 1 capital at 1 October	**450**	450
Capital instruments repurchased: Perpetual Capital Notes	**–**	(450)
Capital instruments issued: Perpetual Subordinated Contingent Convertible Notes	**–**	450
Tier 1 capital at 30 September	**450**	450
Total Tier 1 capital	**2,887**	2,847
Tier 2 capital		
Tier 2 capital at 1 October	**625**	598
Credit risk adjustments	**3**	13
Other movements	**(1)**	–
Capital instruments repurchased: subordinated debt	**–**	(475)
Capital instruments issued: subordinated debt	**–**	474
Removal of minority interest deduction on subordinated debt	**–**	15
Tier 2 capital at 30 September	**627**	625
Total capital	**3,514**	3,472

Minimum Pillar 1 capital requirements (unaudited)	2017 £m	2016 £m
Credit risk	**1,420**	1,352
Operational risk	**130**	130
Counterparty risk	**11**	17
Credit valuation adjustment	**13**	23
Tier 1 regulatory capital requirements	**1,574**	1,522

Balance sheet and prudential regulation risks

RWA movements

RWA flow statement (unaudited)	2017 £m	2016 £m
RWAs at 1 October	**19,029**	18,227
Book size growth	**529**	619
Book quality (improvement)/deterioration[1]	**(28)**	183
Methodology and policy[2]	**148**	–
RWAs at 30 September	**19,678**	19,029

(1) The improvement in book quality is primarily due to the continued diversification in the Liquid Asset Buffer, where we are investing in a number of high quality liquid assets from AAA rated issuance programmes.

(2) The definition of default was enhanced to capture a broader interpretation of the regulatory requirements as part of the Group's programme of activity to prepare for IRB accreditation, which led to an increase in RWAs. This change does not reflect any movement in the underlying risk profile of the portfolio and is only a reporting and Probability of Default model build enhancement.

Pillar 1 RWAs and capital requirements by business line (unaudited)

	At 30 September 2017			At 30 September 2016		
Capital requirements for calculating RWAs	**Capital required £m**	**RWA £m**	**Exposure £m**	Capital required £m	RWA £m	Exposure (restated) £m
Central governments or central banks[1]	**–**	**–**	**12,947**	–	–	8,139
Regional governments or local authorities	**2**	**19**	**156**	2	20	192
Public sector entities	**–**	**5**	**155**	–	5	13
Multilateral development banks	**–**	**–**	**205**	–	–	195
Financial institutions	**13**	**163**	**1,453**	19	234	1,344
Corporates[1]	**273**	**3,418**	**3,791**	273	3,419	3,732
Retail	**72**	**905**	**1,207**	72	897	1,196
Secured by mortgages on immovable property	**961**	**12,001**	**28,203**	897	11,242	26,482
Exposures in default	**47**	**590**	**483**	33	408	340
Collective investments undertakings	**–**	**1**	**1**	–	3	3
Equity exposures	**–**	**5**	**3**	1	11	9
Items associated with particularly high risk	**3**	**40**	**26**	1	15	10
Covered bonds	**4**	**48**	**477**	2	19	191
Other items[1]	**45**	**557**	**585**	52	633	627
Total credit risk	**1,420**	**17,752**	**49,692**	1,352	16,906	42,473
Operational risk	**130**	**1,621**		130	1,623	
Counterparty risk	**11**	**138**		17	214	
Credit valuation adjustment	**13**	**167**		23	286	
	1,574	**19,678**		1,522	19,029	

The Exposure amounts disclosed above are post credit conversion factors and pre credit mitigation.

(1) FY2016 comparatives have been restated for the following with no impact to total RWA or capital requirement:
- £1.1bn of BoE backing assets reallocated from Other items to Central government or central banks asset class; and
- £114m exposure reallocated from Corporates to Other items asset class.

Capital position and CET1 (unaudited)	2017 £m	2016 £m
RWA(1)		
Retail mortgages	**8,646**	7,998
Business lending	**7,359**	7,087
Other retail lending	**932**	915
Other lending	**148**	152
Other(2)	**667**	754
Credit risk	**17,752**	16,906
Credit valuation adjustment	**167**	286
Operational risk	**1,621**	1,623
Counterparty risk	**138**	214
Total RWAs	**19,678**	19,029
Capital ratios		
CET1 ratio(3)	**12.4%**	12.6%
Tier 1 ratio	**14.7%**	15.0%
Total capital ratio	**17.9%**	18.2%

(1) RWAs are calculated under the standardised approach.
(2) The items included in the Other exposure class that attract a capital charge include items in the course of collection, cash in hand, fixed assets and deferred tax assets that are not deducted.
(3) CET1 capital is comprised of shares issued and related share premium, retained earnings and other reserves less specified regulatory adjustments.

While RWAs increased by £649m, driven by growth in mortgages, underlying capital generation post AT1 distribution of 13bps (before the net impact of pension movements, and below-the-line charges such as the Group's proportion of conduct provision charges and exceptional restructuring charges) ensured the CET1 ratio remained robust at 12.4%.

As announced in the Strategic report the Board has recommended a 1p per share dividend. The dividend would equate to approximately £9m of CET1 (equivalent to 4bps of CET1 based on RWAs as at 30 September 2017).

Leverage ratio (unaudited)	2017 £m	2016 £m
Total Tier 1 capital for the leverage ratio		
Total CET1 capital	**2,437**	2,397
AT1 capital	**450**	450
Total Tier 1	**2,887**	2,847
Exposures for the leverage ratio		
Total assets as per published financial statements	**43,231**	39,929
Adjustment for off-balance sheet items	**2,019**	1,982
Adjustment for derivative financial instruments	**(228)**	(399)
Adjustment for securities financing transactions (SFTs)	**1,461**	601
Other adjustments	**(505)**	(364)
Leverage ratio exposure	**45,978**	41,749
Leverage ratio	**6.3%**	6.8%
Modified leverage ratio(1)	**7.4%**	8.0%

(1) The Group's leverage ratio on a modified basis, excluding qualifying central bank claims from the exposure measure in accordance with the policy statement issued by the PRA in October 2017. The Group is currently excluded from the full reporting requirements of the UK leverage ratio framework.

The leverage ratio is monitored against a Board set RAS with the responsibility for managing the ratio delegated to ALCO, which monitors it on a monthly basis.

The leverage ratio is the ratio of Tier 1 capital to total exposure, defined as:

- capital: Tier 1 capital defined according to CRD IV on an end point basis (assuming the full impact of CRD IV requirements on Tier 1 capital were in force with no transitional provisions); and
- exposures: total on- and off-balance sheet exposures (subject to credit conversion factors) as defined in the delegated act amending CRR article 429 (Calculation of the Leverage Ratio), which includes deductions applied to Tier 1 capital.

Other regulatory adjustments consist of adjustments that are required under CRD IV to be deducted from Tier 1 capital. The removal of these from the exposure measure ensures consistency is maintained between the capital and exposure components of the ratio. The Group's leverage ratio is 6.3% which exceeds the Basel Committee's proposed minimum of 3%, applicable from 2018.

The UK leverage ratio framework, which came in to force on 1 January 2016, is relevant to PRA regulated banks and building societies with consolidated retail deposits equal to or greater than £50bn. The Group is currently excluded from these requirements. On 3 October 2017, the PRA published a policy statement – 'UK Leverage Ratio treatment of claims on central banks'.

The PRA Rulebook has been amended to:

- align with its July 2016 modification by consent to exclude central bank claims matched by deposits in the same currency and of identical or longer maturity from the definition of the total leverage exposure measure in the UK leverage ratio framework;
- increase the minimum leverage ratio requirement from 3% to 3.25% of total exposures; and
- align the UK leverage ratio reporting and disclosure requirements to the proposed definition of the total exposure measure and 3.25% minimum leverage ratio requirement.

If these modifications are applied to the Group, this results in an increase in the leverage ratio from 6.3% under CRD IV to 7.4% on the PRA modified basis as a result of the Group's significant exposures to central banks within its liquid asset portfolio and Note cover.

Funding and liquidity risk

Funding risk relates to the impact on the Group's strategy of being unable to raise funds from customers and the wholesale markets of sufficient quantity and of appropriate mix and tenor. An inability to raise sufficient funds may lead to a reduction in lending growth or a requirement to raise the price paid for deposits, both outcomes having an adverse effect on shareholder value. Where funding risk manifests itself in an adverse effect on mix and tenor, for example, a high proportion of short-term wholesale deposits, there is an increased liquidity risk to the Group.

Liquidity risk is the risk that the Group is unable to meet its current and future financial obligations as they fall due at acceptable cost. These obligations include the repayment of deposits on demand or at their contractual maturity dates, the repayment of borrowings and loan capital as they mature, the payment of operating expenses and tax, the payment of dividends and the ability to fund new and existing loan commitments.

Risk assessment

The framework for the Group's approach to funding risk leads to the development of a Group funding plan that is subject to approval by the Board and is consistent with risk appetite and the Group's strategic objectives. The development of the Group's funding plan is informed by the requirements of the Group's Balance Sheet Risk Policy Standards.

Liquidity risk exposures are subject to assessment under both regulatory and internal requirements. Exposures relate to the outflow of funds under a series of stress scenarios less the impact of inflows from assets, liquidation of high-quality liquid assets or through other actions instigated by the Group. Liquidity within the Group is managed in accordance with the ILAAP that is approved by the Board. The ILAAP documents the manner in which the Group meets its OLAR which covers all regulatory and internal liquidity requirements. In addition, the Group has a policy standard which details, among other items, the control standards and risk measurement requirements for liquidity, authorities and responsibilities.

Oversight of liquidity risk is undertaken by ALCO. To meet the requirements of regulatory authorities the liquidity of the Group is managed on a daily basis using a combination of cumulative cash flow mismatch, scenario analysis and stress tests to ensure that normal daily cash requirements are met and to ensure adequate sources of liquidity are available to support unforeseen cash outflows. ALCO delegates daily management responsibilities to the Treasury function within agreed tolerances. All balance sheet risks are subject to independent oversight from the second line balance sheet and liquidity risk oversight function.

Stress testing of the Group's liquidity risk is undertaken on a frequent basis and results are provided to ALCO and the Board. The ILAAP is used to establish key risk drivers and assumptions for liquidity risk and these provide the framework for ongoing stress testing. Stress testing considers the impact of severe yet plausible scenarios to consider the potential impact on the Group's funding and liquidity profile. The Group holds a portfolio of high-quality assets that acts as a buffer against the impact of liquidity risk. Funding plans take a long-term view and these consider the impact of prolonged periods of market disruption in order to identify potential vulnerabilities in the profile of the Group's funding.

A Contingency Funding Plan has been established for management of an escalated liquidity requirement if the Group experiences either restricted access to wholesale funding or a large increase in the withdrawal of funds. The plan identifies triggers for escalation, details the action required, allocates the key tasks to individuals, provides a time frame and defines a management committee to manage the action plan.

The Group has a number of different sources of funding which are considered to be well diversified in terms of the type of instrument and product, counterparty, term structure and market.

The Group can source funding through a range of channels including the following:

- customer deposits;
- access to short-term money market funding;
- term structured funding through Lanark residential mortgage securitisation programme (owner occupied);
- Lannraig BTL mortgage securitisation programme;
- regulated covered bond (RCB) programme;
- senior unsecured funding; and
- access to facilities within the BoE Sterling Monetary Framework and the TFS (the TFS closes to new drawings in February 2018).

The Group's securitisation and covered bond programmes offer investors the opportunity to purchase mortgage-backed debt. These sources are focused on a range of different investors and depositors with a range of maturities. Funding is typically raised in GBP, USD and EUR and is swapped back to GBP to fund the predominantly GBP balance sheet.

Monitoring

The Treasury function is responsible for the development and execution of strategy subject to oversight from the risk management function. In relation to funding and liquidity risk, the primary management committee is ALCO. ALCO meets monthly and reports to the Executive Risk Committee.

The Group continues to have a strong funding and liquidity position and seeks to achieve an appropriate balance between profitability and liquidity risk. Funding is predominantly provided by Retail and SME customers and this is supported by medium-term secured funding issuance from the Group's Lanark and Lannraig securitisation programmes, and its RCB platform and TFS. These funding programmes are a source of strength for the Group and leverage the Group's high-quality mortgage book as a source of collateral for secured funding.

The Group monitors liquidity and funding with reference to a number of measures including LCR, LDR and NSFR (see financial results section).

Balance sheet and prudential regulation risks

Sources of funding (audited)

The table below provides an overview of the Group's sources of funding as at 30 September.

	2017 £m	2016 £m
Total assets	**43,231**	39,929
Less: other liabilities	**(3,509)**	(3,818)
Funding requirement	**39,722**	36,111
Funded by:		
Due to customers	**27,718**	27,090
Due to other banks	**3,817**	1,309
of which:		
Securities sold under agreements to repurchase	**1,864**	1,226
Term Funding Scheme	**1,901**	–
Other	**52**	83
Debt securities in issue	**4,785**	4,501
Equity	**3,402**	3,211
Total funding	**39,722**	36,111

The Group's funding objectives are to prudently manage the sources and tenor of funds in order to provide a sound base from which to support sustainable customer growth. At 30 September 2017, the Group had a funding requirement of £39,722m (2016: £36,111m) with the primary funding requirement being to support loans and advances to customers.

Due to customers

The majority of the Group's funding requirement was met by customer deposits of £27,718m (2016: £27,090m). Customer deposits are comprised of non-interest bearing demand deposits, interest bearing deposits and term deposits from a range of sources including Retail, SME and other corporate customers. The increase of £628m in 2017 was predominantly due to growth in non-interest bearing deposits (£388m) and term deposits (£503m) offset by a managed reduction in higher rate interest bearing deposits (£198m).

Due to other banks and debt securities in issue (wholesale funding)

Due to other banks of £3,817m (2016: £1,309m) was primarily comprised of: £1,864m of securities sold under agreement to repurchase; and £1,901m of drawings under the TFS.

Debt securities in issue of £4,785m (2016: £4,501m) was primarily comprised of: £2,834m of residential mortgage-backed securities issued through the Group's Lanark programme; £327m of securities issued through the Group's BTL securitisation programme (Lannraig); £700m of regulated covered bonds; £300m of senior debt; and £475m of subordinated debt.

Equity

Equity of £3,402m (2016: £3,211m) was also used to meet the Group's funding requirement. Equity is comprised of ordinary share capital, retained earnings, other equity investments and a number of other reserves. For full details on equity refer to section 4 of the Notes to the consolidated financial statements.

External credit ratings

The Group's credit ratings have remained unchanged over the past year. S&P assigns a long-term credit rating of 'BBB-' to the Group, two notches below that of Clydesdale Bank PLC, reflecting their non-operating holding company methodology. Fitch assigns an issuer default rating of 'BBB+', in line with that of Clydesdale Bank PLC, again reflecting their holding company methodology.

Fitch announced the outcome of their annual review of Clydesdale Bank PLC and CYBG PLC ratings on 7 September 2017. All current ratings were affirmed, with a stable outlook. On 15 September 2017, Moody's placed the long-term ratings of Clydesdale Bank PLC on review for upgrade. The review will focus on progress in the execution of the Group's strategic plan as well as the extent to which enhancements in management, risk and control frameworks and processes have been embedded. On 15 November 2017, S&P moved the outlook on Clydesdale Bank PLC and CYBG PLC back to stable from negative as a result of an update to an industry-wide exercise following the EU referendum.

The Group's long-term credit ratings are summarised below:

	Outlook as at 20 Nov 2017[1]	30 Sep 2017	30 Sep 2016
CYBG PLC			
Fitch	Stable	BBB+	BBB+
Standard & Poor's	Stable	BBB-	BBB-
Clydesdale Bank PLC			
Fitch	Stable	BBB+	BBB+
Standard & Poor's	Stable	BBB+	BBB+
Moody's[2]	Review for upgrade	Baa2	Baa2

(1) For detailed background on the latest credit opinions, by S&P and Fitch, please refer to the respective rating agency websites.
(2) Long-term deposit rating.

Additional collateral to be provided in the event of a notch downgrade
The Group monitors the movements in its credit ratings and the related requirement to post collateral for payment systems and clearing houses. These figures are not considered material compared to the volume of unencumbered liquid assets.

Liquid assets
The quantity and quality of the Group's liquid assets are calibrated to the Board's view of liquidity risk appetite and remain at a prudent level above regulatory requirements. The Group was compliant with all internal and regulatory liquidity metrics at 30 September 2017.

The liquid asset portfolio provides a buffer against sudden and potentially sharp outflows of funds and liquid assets must therefore be of a high quality so they can be realised for cash and cannot be encumbered for any other purpose (e.g. to provide collateral for payments systems). Details on encumbered assets are provided in the following section.

The liquid asset portfolio is primarily comprised of cash at the BoE, UK Government Securities (Gilts) and listed securities (e.g. bonds issued by supra-nationals and AAA rated covered bonds).

Liquid asset portfolio	2017 £m	2016 £m
Cash and balances with central banks	**4,367**	3,702
UK government treasury bills and gilts	**1,129**	1,187
Other debt securities	**829**	399
Total	**6,325**	5,288

The liquid asset portfolio has seen some diversification over 2017 with an increase in Other Debt securities. Before investing in any security an assessment is completed for both the credit quality and the treatment for liquidity purposes. ALCO oversees the composition of the liquid asset portfolio.

Further information can be found in sections 3.1 and 3.2 of the Notes to the consolidated financial statements (Section 3.1 Cash and balances with central banks of £6,937m include £2,570m of assets that are encumbered to support issuance of Scottish bank notes and to support payments systems and £44m of mandatory central bank deposits; section 3.2 Listed securities of £2,066m comprises £1,221m of UK Government Treasury Bills and Gilts, of which £92m is encumbered to support payments systems and £845m of Other debt securities (listed securities), of which £16m is encumbered to support payment systems).

Balance sheet and prudential regulation risks

Encumbered assets by asset category

Examples of reasons for asset encumbrance include, among others, supporting the Group's secured funding programmes to provide stable term funding to the Group, use of assets as collateral for payments systems in order to support customer's transactional activity, and providing security for the Group's issuance of Scottish bank notes. The Group monitors the level of asset encumbrance to ensure an appropriate balance is maintained.

Encumbered assets by asset category (audited)

	Assets encumbered with non-central bank counterparties					Other assets				
						Assets not positioned at the central bank				
September 2017	Covered bonds £m	Securi-tisations £m	Other £m	Total £m	Positioned at the central bank (including encumbered) £m	Readily available for encumbrance £m	Other assets capable of being encumbered £m	Cannot be encumbered £m	Total £m	**Total £m**
Cash and balances with central banks	–	–	–	–	2,850	4,087	–	–	6,937	**6,937**
Due from other banks	46	358	338	742	–	–	432	–	432	**1,174**
Investments – available for sale	–	–	–	–	95	1,971	–	10	2,076	**2,076**
Other financial assets	–	–	–	–	–	–	477	–	477	**477**
Derivatives	–	–	–	–	–	–	–	282	282	**282**
Loans and advances to customers	1,347	5,841	–	7,188	6,294	5,940	8,906	2,965	24,105	**31,293**
Intangible assets	–	–	–	–	–	–	–	339	339	**339**
Deferred tax assets	–	–	–	–	–	–	–	154	154	**154**
Other assets	–	–	–	–	–	–	100	399	499	**499**
Total assets	1,393	6,199	338	7,930	9,239	11,998	9,915	4,149	35,301	**43,231**

	Assets encumbered with non-central bank counterparties					Other assets				
						Assets not positioned at the central bank				
September 2016	Covered bonds £m	Securi-tisations £m	Other £m	Total £m	Positioned at the central bank (including encumbered) £m	Readily available for encumbrance £m	Other assets capable of being encumbered £m	Cannot be encumbered £m	Total £m	Total £m
Cash and balances with central banks	–	–	–	–	2,468	3,487	–	–	5,955	5,955
Due from other banks	156	282	337	775	–	–	177	–	177	952
Investments – available for sale	–	–	–	–	101	1,594	36	–	1,731	1,731
Other financial assets	–	–	–	–	–	–	750	–	750	750
Derivatives	–	–	–	–	–	–	–	585	585	585
Loans and advances to customers	1,149	5,144	–	6,293	2,902	3,946	13,003	3,058	22,909	29,202
Intangible assets	–	–	–	–	–	–	–	256	256	256
Deferred tax assets	–	–	–	–	–	–	–	183	183	183
Other assets	–	–	–	–	–	–	122	193	315	315
Total assets	1,305	5,426	337	7,068	5,471	9,027	14,088	4,275	32,861	39,929

Assets and liabilities by maturity

The following tables represent a breakdown of the Group's balance sheet, according to the assets and liabilities contractual maturity. Many of the longer-term monetary assets are variable rate products, with behavioural maturities shorter than the contractual terms. Accordingly, this information is not relied upon by the Group in its management of interest rate risk. The Group has disclosed certain term facilities within loans and advances to customers with a revolving element at the maturity of the facility as this best reflects their contractual maturity.

2017 (audited)	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	**Total £m**
Assets							
Cash and balances with central banks	5,430	–	–	–	–	1,507	**6,937**
Due from other banks	701	473	–	–	–	–	**1,174**
Financial assets available for sale	–	3	256	1,334	473	10	**2,076**
Other financial assets at fair value	–	4	16	225	232	–	**477**
Derivative financial instruments	–	19	72	116	75	–	**282**
Loans and advances to customers	1,783	292	764	5,048	23,010	396	**31,293**
Due from customers on acceptances	–	4	–	–	–	–	**4**
All other assets	–	203	49	–	–	736	**988**
Total assets	7,914	998	1,157	6,723	23,790	2,649	**43,231**
Liabilities							
Due to other banks	45	1,172	700	1,900	–	–	**3,817**
Other financial liabilities at fair value	–	–	–	26	–	–	**26**
Derivative financial instruments	–	21	31	132	192	–	**376**
Due to customers	22,185	917	2,220	2,396	–	–	**27,718**
Liabilities on acceptances	–	4	–	–	–	–	**4**
Debt securities in issue	–	620	503	2,613	1,049	–	**4,785**
All other liabilities	2,197	174	–	–	–	732	**3,103**
Total liabilities	24,427	2,908	3,454	7,067	1,241	732	**39,829**
Off-balance sheet items							
Contingent liabilities	–	19	40	7	3	42	**111**
Other credit commitments	8,408	–	–	–	–	–	**8,408**
Total off-balance sheet items	8,408	19	40	7	3	42	**8,519**

Balance sheet and prudential regulation risks

2016 (audited)	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Assets							
Cash and balances with central banks	4,642	–	–	–	–	1,313	5,955
Due from related entities	–	–	–	–	–	–	–
Due from other banks	869	83	–	–	–	–	952
Financial assets available for sale	–	7	20	1,019	649	36	1,731
Other financial assets at fair value	–	34	88	275	353	–	750
Derivative financial instruments	2	46	72	241	224	–	585
Loans and advances to customers	2,021	285	648	4,271	21,577	400	29,202
Due from customers on acceptances	–	4	–	–	–	–	4
All other assets	111	36	40	–	–	563	750
Total assets	7,645	495	868	5,806	22,803	2,312	39,929
Liabilities							
Due to other banks	81	417	311	500	–	–	1,309
Other financial liabilities at fair value	–	2	11	35	–	–	48
Derivative financial instruments	2	47	73	123	353	–	598
Due to customers	21,168	1,802	1,933	2,187	–	–	27,090
Liabilities on acceptances	–	4	–	–	–	–	4
Due to related entities	–	–	–	–	–	–	–
Debt securities in issue	–	18	214	3,472	797	–	4,501
All other liabilities	1,960	77	132	–	–	999	3,168
Total liabilities	23,211	2,367	2,674	6,317	1,150	999	36,718
Off-balance sheet items							
Contingent liabilities	–	19	44	12	48	–	123
Other credit commitments	7,690	–	–	–	–	–	7,690
Total off-balance sheet items	7,690	19	44	12	48	–	7,813

Cash flows payable under financial liabilities by contractual maturity

2017 (audited)	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	**Total £m**
Due to other banks	44	1,173	708	1,912	–	–	**3,837**
Other financial liabilities at fair value	–	–	1	27	–	–	**28**
Trading derivative financial instruments	–	26	36	79	28	–	**169**
Due to customers	22,185	918	2,220	2,397	–	–	**27,720**
Liabilities on acceptances	–	4	–	–	–	–	**4**
Debt securities in issue	32	624	554	2,841	1,195	–	**5,246**
All other financial liabilities	2,197	174	–	–	–	732	**3,103**
Hedging derivative liabilities							
Contractual amounts payable	–	6	39	225	194	–	**464**
Total liabilities	24,458	2,925	3,558	7,481	1,417	732	**40,571**

2016 (audited)	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Due to other banks	81	420	318	505	–	–	1,324
Other financial liabilities at fair value	–	2	12	40	–	–	54
Trading derivative financial instruments	2	43	43	50	208	–	346
Due to customers	21,169	1,943	1,954	2,217	–	–	27,283
Liabilities on acceptances	–	4	–	–	–	–	4
Debt securities in issue	–	23	285	3,712	991	–	5,011
All other financial liabilities	1,912	–	–	–	–	–	1,912
Hedging derivative liabilities							
Contractual amounts payable	–	8	71	141	100	–	320
Total liabilities	23,164	2,443	2,683	6,665	1,299	–	36,254

The balances in the cash flow tables above will not agree directly to the balances in the consolidated balance sheet as the table incorporates all cash flows, on an undiscounted basis, related to both principal as well as those associated with all future coupon payments.

Market risk

Market risk is the risk associated with adverse changes in the fair value, or accrual income and expense, of assets and liabilities held by the Group as a result of movements in market factors such as interest rates, foreign exchange rates, volatility and credit spreads. The Group's balance sheet is predominantly UK based and is denominated in GBP, therefore foreign exchange risk is not a major part of the Group's risk profile.

Structural interest rate risk comprises the sensitivity of the Group's current and future net interest income and economic value to movements in market interest rates. The major contributors to interest rate risk are:

– the investment of non-interest bearing deposits and equity into interest-bearing assets;

– the mismatch between repricing dates of interest-bearing assets and liabilities;

– basis risk, for example, the inability of the pricing 'basis' for customer asset and liability products to be replicated in the financial markets or the risk arising from changing relationships between different interest rate yield curves; and

– customer optionality, e.g. the right to repay borrowing in advance of contract maturity dates.

Balance sheet and prudential regulation risks

Exposures

The focus of the Group's activity is to provide high-quality banking services to its customers. These services include the provision of foreign exchange products and derivative products to enable customers to manage risks within their businesses. As a result of these activities, the Group may be exposed to forms of market risk that would arise from movements in price on these products. Controls include the hedging of these products as and when they arise.

Measurement

Interest rate risk in the banking book (IRRBB) is measured, monitored, and managed from both an internal management and regulatory perspective. The RMF incorporates both market valuation and earnings-based approaches. In accordance with the Group IRRBB Policy Standard. risk measurement techniques include: basis point sensitivity; value at risk (VaR), earnings at risk (EaR), interest rate risk stress testing, repricing analysis, cash flow analysis, and scenario analysis.

The key features of the internal interest rate risk management model are:

- the use of basis point sensitivity analysis;
- VaR and EaR are measured on a statistical basis: 99% confidence level with appropriate holding periods depending on varying risk types:
- historical simulation approach utilising instantaneous interest rate shocks including parallel rate movements and twists in the yield curve to explore risks around exposures to movements in short- or long-term interest rates;
- static balance sheet (i.e. any new business is assumed to be matched, hedged or subject to immediate repricing);
- investment term for capital is modelled with a benchmark term agreed by ALCO;
- investment term for core non-interest bearing assets and liabilities is modelled on a behavioural basis with a benchmark term agreed by ALCO; and
- assumptions covering the behavioural life of products and customer behaviour for optionality are reviewed and approved by ALCO.

Foreign exchange risk is assessed based on the absolute exposure in each currency.

Mitigation measures

Market risks are overseen by ALCO with delegation for day-to-day management given to Treasury. Treasury use a number of techniques and products to manage market risks including interest rate swaps, cash flow netting and foreign exchange. Basis risk is managed through a combination of wholesale market basis risk management products, pricing strategies and product innovation. As part of an objective to secure stable and optimal net interest income over both a 12-month period and over the long term, mismatch risk can be minimised with the investment of equity and non-interest bearing deposits targeting the stability of net interest income. The use of derivatives gives rise to the need to apportion transactions into hedge relationships.

Fair value hedges

The Group hedges part of its existing interest rate risk, resulting from potential movements in the fair value of fixed rate assets and liabilities. The fair value of these swaps is disclosed in note 3.18. There were no transactions for which fair value hedge accounting had to be discontinued in the year.

Cash flow hedges

The Group hedges a portion of the variability in future cash flows attributable to interest rate and foreign currency risk. The interest and foreign currency risk arise from variable interest rate assets and liabilities which are hedged using cross currency and interest rate swaps, and material non-GBP denominated assets which are hedged using foreign exchange forward contracts. There were no transactions for which cash flow hedge accounting had to be discontinued in the period as a result of the highly probable cash flows no longer being expected to occur. The fair value of derivatives is disclosed in note 3.18.

Monitoring
Model parameters and assumptions are reviewed and updated on at least an annual basis. Material changes require the approval of ALCO. Oversight of market risk is conducted by the Group's balance sheet and liquidity risk oversight team that is independent of the Treasury function. The Board and Executive Risk Committee, through ALCO's oversight, monitors risk to ensure it remains within approved policy limits and Board requirements.

	Value at risk		Earnings at risk	
Interest rate risk (audited)	**2017 £m**	2016 £m	**2017 £m**	2016 £m
As at 30 September	**25**	15	**4**	2
Average value during the year	**23**	25	**2**	5
Minimum value during the year	**15**	13	**1**	2
Maximum value during the year	**36**	36	**4**	11

Principal financial assets and liabilities
The following table shows the Group's principal financial assets and liabilities and the main non-traded market risk types they are exposed to:

Audited	**2017 £m**	Liquidity risk	Interest rate risk	Foreign exchange risk	Credit risk
Assets					
Cash and balances with central banks	**6,937**				●
Financial assets available for sale	**2,076**	●	●		●
Loans and advances to customers	**31,293**	●	●	●	●
Derivative financial instruments	**282**	●	●	●	●
Other financial assets at fair value	**477**	●	●		●
Liabilities					
Due to customers	**27,718**	●	●	●	
Due to other banks	**3,817**	●	●	●	
Derivative financial instruments	**376**	●	●	●	
Other financial liabilities at fair value	**26**	●	●		
Debt securities in issue	**4,785**	●	●	●	

Audited	2016 £m	Liquidity risk	Interest rate risk	Foreign exchange risk	Credit risk
Assets					
Cash and balances with central banks	5,955				●
Financial assets available for sale	1,731	●	●		●
Loans and advances to customers	29,202	●	●	●	●
Derivative financial instruments	585	●	●	●	●
Other financial assets at fair value	750	●	●		●
Liabilities					
Due to customers	27,090	●	●	●	
Due to other banks	1,309	●	●	●	
Derivative financial instruments	598	●	●	●	
Other financial liabilities at fair value	48	●	●		
Debt securities in issue	4,501	●	●	●	

Foreign currency assets and liabilities split by type
The Group does not incur material foreign currency exposure.

Repricing periods of assets and liabilities by asset/liability category
The following table shows the repricing periods of the Group's assets and liabilities as assessed by the Group. This repricing takes account of behavioural assumptions where material and the Group's policy to hedge capital in accordance with a benchmark term agreed by ALCO in order to reduce variability in net interest income.

Items are allocated to time buckets in the table below by reference to the earlier of the next contractual interest rate repricing date and the residual maturity date.

2017 (unaudited)	Overnight £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Non-interest bearing £m	**Total £m**
Assets							
Cash and balances with central banks	6,756	9	24	148	–	–	**6,937**
Due from other banks	1,125	49	–	–	–	–	**1,174**
Financial assets available for sale	234	362	100	1,020	360	–	**2,076**
Other financial assets at fair value	477	–	–	–	–	–	**477**
Loans and advances to customers	8,537	5,356	5,496	11,811	247	(154)	**31,293**
Other assets	–	–	–	–	–	1,274	**1,274**
Total assets	17,129	5,776	5,620	12,979	607	1,120	**43,231**
Liabilities							
Due to other banks	3,292	517	8	–	–	–	**3,817**
Due to customers	10,708	1,107	3,923	11,965	15	–	**27,718**
Other financial liabilities at fair value	26	–	–	–	–	–	**26**
Debt securities in issue	42	3,968	–	475	300	–	**4,785**
Other liabilities	1,285	44	116	711	–	1,327	**3,483**
Equity	–	165	441	2,796	–	–	**3,402**
Total liabilities and equity	15,353	5,801	4,488	15,947	315	1,327	**43,231**
Notional value of derivatives managing interest rate sensitivity	89	3,044	(478)	(2,767)	112	–	
Total interest rate gap sensitivity	1,687	(3,069)	1,610	(201)	180	(207)	
Cumulative interest rate gap sensitivity	1,687	(1,382)	228	27	207	–	

2016 (unaudited)	Overnight £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Non-interest bearing £m	Total £m
Assets							
Cash and balances with central banks	5,798	8	21	128	–	–	5,955
Due from other banks	949	3	–	–	–	–	952
Financial assets available for sale	252	285	–	665	495	34	1,731
Loans and advances to customers	10,122	4,443	4,484	10,958	165	(216)	29,956
Other assets	–	–	–	–	–	1,335	1,335
Total assets	17,121	4,739	4,505	11,751	660	1,153	39,929
Liabilities							
Due to other banks	67	929	313	–	–	–	1,309
Due to customers	10,738	1,476	3,703	11,213	12	–	27,142
Debt securities in issue	204	3,822	–	475	–	–	4,501
Other liabilities	1,564	38	102	628	–	1,434	3,766
Equity	–	173	460	2,578	–	–	3,211
Total liabilities and equity	12,573	6,438	4,578	14,894	12	1,434	39,929
Notional value of derivatives managing interest rate sensitivity	(1,298)	(1,610)	501	2,869	(462)	–	
Total interest rate gap sensitivity	3,250	(3,309)	428	(274)	186	(281)	
Cumulative interest rate gap sensitivity	3,250	(59)	369	95	281	–	

Pension risk

The Group operates a defined benefit (DB) pension scheme, the Yorkshire and Clydesdale Bank Pension Scheme (the Scheme). Clydesdale Bank PLC is the Scheme's principal employer and there are no other participating employers. Following a consultation process the Scheme was closed to future accrual on 1 August 2017 for the majority of members. A small number of members elected to keep DB accruals subject to making an increased contribution to the Scheme and to also forego other remuneration benefits.

DB pension schemes provide a promise to pay members a pre-determined level of income at retirement which is independent of the contributions and investment returns (assets) used to fund these benefit promises (collectively the liabilities). As such, there are significant risks associated with managing a DB scheme. These risks will continue until the Scheme is formally wound up, either in the event that all the liabilities are transferred to a third party (for example an insurer) or once all individual member benefits are paid.

The Scheme's assets are held under a separate trust and the Scheme is managed by a corporate Trustee Board independently of the Group, per the Scheme Trust Deed and Rules. Therefore, the Group's ability to directly manage the Scheme is limited to certain powers within the governing documentation. Aside from the Group's role to sponsor the Scheme to ensure there are sufficient assets to meet benefit payments as they fall due, the Group's focus is directed on mitigating the impact on capital and earnings through working with the trustee to implement risk reduction initiatives. Several activities have been implemented since 2003 with the specific aim of reducing risk in the Scheme, including a de-risking journey plan, benefit reforms and the outcome of the 2017 consultation on future accruals.

The principal cause of risk within the Scheme is the difference between the assets and the liabilities. The assets are exposed to market valuation movements, within and between asset classes, while the liabilities are more sensitive to interest rate and inflation rate changes, and changes in other actuarial assumptions which may not be borne out in experience, for example life expectancy. There are various bases, with differing assumptions, for measuring the Scheme liabilities whereas Scheme assets are consistently valued at current market values. The two key bases used to value DB scheme liabilities are IAS 19, a standardised accounting measure which is the basis for income statement, balance sheet and capital reporting, and the Trustee's Technical Provisions basis which determines the cash funding contributions to the Scheme to repair any deficit agreed as part of a triennial valuation.

The IAS 19 valuation is disclosed in note 3.16. The rate used to discount the liabilities on the IAS 19 basis is a key driver of volatility and, as prescribed by IAS 19, is based on yields on high-quality corporate bonds. Therefore, the IAS 19 valuation can move adversely because of low rates and narrowing credit spreads. Inflation is another key source of volatility. This is because member benefits have an element of index linking and therefore the liabilities increase with rises in long-term inflation assumptions, although in practice, over the long term, the relationship between interest and inflation rates tends to be negatively correlated resulting in a degree of risk offset.

The triennial valuation (the valuation) uses the Trustee's actuarial assumptions and a liability discount rate based on gilt yields. The last formal valuation indicated a deficit of £290m as at 30 September 2016 (after allowing for changes to future accrual from 1 August 2017), a reduction from the 30 September 2013 reported deficit of £450m. There has been no change to the deficit reduction schedule agreed with the Trustees in June 2014, with a further payment of £50m in May 2017, to be followed by payments of £50m in each year ending 31 March 2019, 31 March 2020, 31 March 2021 and 31 March 2022. A payment of £55m is due in the year ending 31 March 2023.

Details of retirement benefit obligations are included in section 3.16 of the Notes to the consolidated financial statements.

Regulatory, compliance and conduct risk

Effectively addressing legacy issues and building a platform for growth

The Group continues to focus to address and eliminate legacy conduct issues while seeking to ensure that regulators' expectations are met and our current and future proposition is compliant and fair to customers.

Regulatory and compliance risk

Regulatory and compliance risk is the risk of: failing to understand and comply with relevant laws, regulations, licence conditions, supervisory requirements, self-regulatory industry codes of conduct and voluntary initiatives; failing to identify, monitor and respond to changes in the regulatory environment; damaging the Group's relationship with its regulators through non-compliance with requirements, not keeping regulators informed of relevant issues that affect (or which may affect) the Group, not responding effectively to the information requests and review findings of the regulators, by providing incorrect or inadequate information, not meeting regulatory deadlines or obstructing the regulator from fulfilling its role.

Risk appetite

The Group has no appetite for actions resulting in breaches of regulation or for inaction to address systemic process and control failures leading to material non-compliance.

Mitigation measures

- The Group has a regulatory engagement policy designed to ensure an open and cooperative relationship is maintained with regulators at all times, ensuring that all key interactions with regulators are managed, recorded and escalated as appropriate.
- All colleagues are required to achieve mandated standards to meet their 'compliance gateway' obligations.
- Material changes to regulatory policies and protocols are approved by either the Executive Leadership Team or the Board.
- The Group CRO and Risk Leadership Team consider compliance risk topics when setting risk appetite and through ongoing risk assessment, profiling and reporting.

Monitoring

A risk management oversight and compliance monitoring plan is approved by Board's Risk Committee on an annual basis which independently assesses the control framework underpinning compliance with laws and regulations.

Conduct risk

Conduct risk is the risk of undertaking business in a way which is contrary to the interests of our customers resulting in the delivery of inappropriate customer outcomes, customer detriment, regulatory censure, redress costs and/or reputational damage.

Risk appetite

The Group is committed to acting in the interests of its customers, and has no appetite for conduct risk.

Mitigation measures

The Group has a conduct framework which recognises the key conduct risks inherent in the Group's strategy through which it seeks to apply the highest standards in the design and sale of products, and the treatment of its customers. The framework ensures fair customer outcomes supported by a good customer experience. This is achieved in a number of ways including continuous monitoring and responding to customer feedback and complaints. In addition, if things do go wrong, action is taken to ensure we put things right for our customers.

Products are designed and sold to meet customer needs and expectations with governance processes embedded to ensure those objectives are met.

Consideration of customer outcomes is embedded within the Group's operating processes, and metrics are regularly monitored to help ensure outcomes are appropriate.

Exposures

As part of the demerger from NAB in 2016, NAB and the Group have entered into a Conduct Indemnity Deed where NAB has agreed to provide the Group with an indemnity in respect of certain historic liabilities relating to conduct in the period prior to the demerger date. Details of the Conduct Indemnity Deed are included in note 3.14 – Provisions.

There continues to be a great deal of uncertainty and significant judgement is required in determining the quantum of conduct risk-related liabilities with note 3.14 reflecting the Group's current position in relation to redress provisions for PPI, interest rate hedging products (IRHPs) and other smaller historic conduct matters. The final amount required to settle the Group's potential liabilities for these matters is materially uncertain. The Group will continue to reassess the adequacy of provisions for these matters and the assumptions underlying the calculations at each reporting date based upon experience and other relevant factors at that time.

Monitoring

This is a principal focus of the Board, senior management and regulators, and the Group seeks to ensure customers are treated fairly and products are designed and sold to meet their needs. The Group also works to ensure that customer expectations are met and complaints are dealt with effectively and fairly. All Three Lines of Defence consider conduct risk as part of their oversight and assurance activities.

Proactive operational risk management with enhanced risk frameworks

The Group continues to strengthen the controls that provide a continuity of service, while identifying areas of operational efficiency, and ensuring the level of operational risk capital reflects our risk profile.

Operational risk (including people risks) is the risk of loss resulting from inadequate or failed internal processes, people strategies and systems or from external events including, for example, the prospect of a cyber attack. It is a core component of the RMF and is embedded in day-to-day business activities. Responsibilities are set out in a structured operational risk framework that seeks to identify, assess, mitigate, monitor, and report the operational risks and events that could impact the achievement of business objectives or impact core business processes.

Business units are responsible for the day-to-day management of operational risk, with oversight from the risk management function, and independent assurance activities undertaken by internal audit.

The requirements of the operational RMF are defined in an overarching operational risk policy and related minimum standards, and reflect the Group's operational risk appetite.

Risk appetite

The Group is prepared to tolerate a level of operational risk exposure within agreed thresholds and limits. Operational risks arise from day-to-day business activities, which may result in direct or indirect losses and could adversely impact the Group's financial performance, levels of customer care and reputation.

Approach to monitoring and mitigating exposures

Losses may result from both internal and external events, and are categorised using risk categories aligned to Basel II. The Basel II categories are used to ensure that data can be reported externally and compared with other industry data.

The Group has identified, assessed and is currently monitoring all key operational risks across the above noted categories, including undertaking an assessment of control effectiveness, monitoring trends in key risk indicators and escalating events, in accordance with policy requirements.

Stress testing

The Group undertakes scenario analysis to gain insights into the stresses the business could be subject to in the event of this type of operational risk materialising. The Group maintains a suite of operational risk scenarios covering top operational risks relevant to its business. As part of the scenario analysis approach, the suite of operational risk scenarios are reviewed and updated on a regular basis for existing potential impacts and identification of potential new risk events. Management then document a proposed response to identify how the scenarios would be managed and monitored if they occurred.

Risk category	
Operational resilience risk	The risks associated with the ability of the Group to quickly adapt to disruptions while maintaining continuous business operations and safeguarding people, assets and overall brand equity, even in the face of adverse events, shocks and chronic or incremental changes.
Information technology risk	The risks associated with inadequate and failed information technology processes and components (including hardware, software and networking components).
Change risk	The risks associated with a failure to execute and deliver change that could result in an inability to meet our strategic objectives, including failing to meet our customer, regulator, colleague, or shareholders' expectations, at a Group level and local management level.
Third-party risk	The risks associated with ensuring the Group's outsourced and offshoring arrangements are controlled effectively, including the risk of failure to service existing and new customers, and the potential cessation of specific activities, or the risk of personally identifiable information or Group sensitive data being exposed or exploited, or the risk of financial, reputational and regulatory censure if the third party enters into any illegal or unethical activities.
Data risk	The risks associated with the accuracy, management and use of data that underpins decision-making at every level across the organisation.

A strengthened and robust financial crime framework

The Group continues to invest in its systems and controls to prevent, detect, screen and report financial crime, demonstrating a tangible uplift in effectiveness.

Financial crime risk is the risk that the Group's products and services will be used to facilitate financial crime against the Group, its customers or third parties. It encompasses the risk of failing to understand and comply with relevant laws, regulations and supervisory requirements relating to money laundering, terrorism financing, bribery and corruption and sanctions and embargoes. It also includes risks associated with external or internal acts intended to defraud, misappropriate, and circumvent policy, funds, information, regulations and property. The Group maintains an overarching financial crime policy and four policy standards aligned to each material financial crime risk. These are:

Sanctions – The Group has no appetite for non-compliance with the legal and regulatory obligations relating to sanctions and embargoes. To reflect the Group's risk appetite and to protect the Group from financial and reputational damage, including regulatory censure, fines and enforcement action, the Sanctions and Embargoes Policy articulates a set of minimum standards and requirements which must be complied with.

Anti-money laundering – The Group applies a prescribed high-risk customer model which sets out the types of customer it has no risk appetite to onboard, as well as customers with whom the Group is prohibited from entering into or maintaining a customer relationship. All other customers who are not prescribed shall be subject to controls commensurate with their risk.

Anti-bribery and corruption – The Group does not tolerate the direct or indirect offer, payment, solicitation or acceptance of bribes in any form. The Group has in place risk assessments, policies and guidelines on interacting with customers, suppliers and agents, including specific policies for gifts and hospitality. Senior managers across the business are required to complete an evaluation of risk areas as part of the risk assessment process.

Fraud – The Group accepts that, in order to conduct business in a commercially viable manner, it is willing to sustain fraud losses within an agreed set of parameters. The application of fraud risk management considers customer impacts, industry trends and financial impacts of fraud which, on occasion, provide conflicting priorities. Emerging risks are identified and assessed with action taken to mitigate them. An agreed loss plan is set and performance against this is overseen by the policy owner and reported through the appropriate governance committees. With regard to internal fraud, the Group recognises the risk of internal fraud but has no appetite for it. Consequently there is a control framework in place to mitigate that risk.

Exposures

There are currently no significant exposures to report. The Group continues to review the external environment for any change in regulatory or legislative direction, taking action as appropriate.

Mitigation measures

Risk assessments against the four financial crime policy standards take place on an annual basis. Over and above these assessments, regular oversight of higher-risk activities takes place as part of the formal oversight plan and embedded activity takes place throughout the year. Key performance metrics relative to critical financial crime systems are kept under review to ensure ongoing effectiveness. Third party tools are used to test system effectiveness where available and appropriate. Training completion and compliance is subject to annual oversight.

All standards are reflected in the Group policy and standards and financial crime prevention manual, the content of which is provided by financial crime risk and updated as appropriate.

Monitoring

The financial crime team is responsible for strategy, governance, standard setting, oversight, training and reporting to the competent authorities and governance committees/Board.

The control framework is owned by financial crime risk but management and execution of customer identity and verification, customer due diligence, enhanced due diligence, identifying high-risk customers, including correspondent banking relationships and record keeping is the responsibility of first line business units.

Account opening pass rates are overseen as part of a regular process undertaken by financial crime risk and reported monthly.

Higher-risk customers are referred to financial crime risk and senior management within Customer Banking for agreement and sign off that business is within appetite and then continue to be monitored on an ongoing basis.

Screening customers for sanctions or politically exposed persons and transaction monitoring is carried out by financial crime risk. Sanctions screening for payments is carried out by the Payments team in the first line. Critical financial crime systems oversight is independently tested by Internal Audit.

Robust strategy development and monitoring

Strategy is delivered within a well-defined risk appetite and RMF with continual monitoring in place.

Strategic, business and financial performance risk is the risk of significant loss, loss of earnings or damage arising from business decisions that impact the long-term interests of the Group's stakeholders or from an inability to adapt to external developments.

Risk appetite

The Group intends to grow and increase share in target markets, and has clear strategies for its business model and for target customers and products, but it has no appetite to achieve its targets in an unsustainable fashion, or one which may result in damaging outcomes for the Group, its customers or other stakeholders.

Exposures

The Group operates amid intense, increasing competition. Peer and challenger banks, some with innovative business models and low cost bases, such as fast-growing peer-to-peer lenders and crowd funders, allied with rapid technological change, notably in payments and mobile banking, present a fast-evolving, challenging environment. These trends and new regulations also necessitate a large change agenda, which diverts management attention, imposes costs and which may not deliver expected benefits.

At the same time, the low interest rate environment constrains income, reduces margins and, by inhibiting capital generation, reduces strategic room for manoeuvre. As such, income growth and margin expectations over the Group's planning horizon are balanced, highlighting that this environment contributes to significant business risk, the risk that Group net income fails to grow as targeted, or falls.

Mitigation measures

CYBG was divested from NAB and listed in February 2016, but strategic changes necessary for success when independent were assessed over a prolonged prior period. Moreover, CYBG has a long history as a full service UK bank and benefits from an experienced Board and Executive Leadership Team, such that the overall strategy has evolved through a mature and robust process.

The Group's risk appetite represents a 'risk envelope' against which chosen strategies and financial plans are assessed and within which chosen strategies must operate. The RAS, and associated risk appetite framework, is therefore a key means of controlling strategic risk. The risk appetite framework comprises an extensive system of measures, thresholds and other controls, which together ensure that the Group operates within the Board's approved appetite for strategic risk.

Monitoring

A range of financial and non-financial metrics, including RoTE, lending growth, customer acquisition, NIM and others, are key performance indicators used to monitor performance relative to strategic objectives. They are monitored against the Financial Plan by the Group's Board and Executive Leadership Team, who react to deviations from targets and modify strategy accordingly.

FINANCIAL STATEMENTS

Independent auditor's report to the members of CYBG PLC

Our opinion on the financial statements

In our opinion:

- the CYBG PLC Group financial statements and Parent company financial statements (the "financial statements") give a true and fair view of the state of the Group's and of the Parent company's affairs as at 30 September 2017 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the Parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

What we have audited
The CYBG PLC financial statements comprise:

Group	Parent company
Consolidated Income Statement for the year ended 30 September 2017	
Consolidated Statement of Comprehensive Income for the year ended 30 September 2017	
Consolidated Balance Sheet as at 30 September 2017	Company Balance Sheet as at 30 September 2017
Consolidated Statement of Changes in Equity for the year ended 30 September 2017	Company Statement of Changes in Equity for the year ended 30 September 2017
Consolidated Statement of Cash Flows for the year ended 30 September 2017	Company Statement of Cash Flows for the year ended 30 September 2017
Related notes 1.1 to 5.5 to the financial statements	Related notes 6.1 to 6.6 to the financial statements
Certain required disclosures have been presented elsewhere in the Annual Report and Accounts, rather than in the notes to the financial statements. These have been cross-referenced from the financial statements and are identified as audited.	

The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the Parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

Basis for opinion
We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the audit of the financial statements section of our report below. We are independent of the Group and Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

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Conclusions relating to principal risks, going concern and viability statement

We have nothing to report in respect of the following information in the annual report, in relation to which the ISAs (UK) require us to report to you whether we have anything material to add or draw attention to:

- the disclosures in the annual report set out on page 19 that describe the principal risks and explain how they are being managed or mitigated;
- the Directors' confirmation set out on page 71 in the annual report that they have carried out a robust assessment of the principal risks facing the entity, including those that would threaten its business model, future performance, solvency or liquidity;
- the Directors' statement set out on page 191 in the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, and their identification of any material uncertainties to the entity's ability to continue to do so over a period of at least 12 months from the date of approval of the financial statements;
- whether the Directors' statement in relation to going concern required under the Listing Rules in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit; or
- the Directors' explanation set out on page 125 in the annual report as to how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the entity will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Overview of our audit approach

Key audit matters	– Payment Protection Insurance ("PPI") and other conduct related provisioning. – SME lending impairment provisions – Revenue recognition – Effective interest method accounting.
Audit scope	– We performed an audit of the complete financial information of the Group and Parent. – Our Group audit scope included all CYBG PLC subsidiaries.
Materiality	– Overall Group materiality was £17m which represents 0.5% of shareholders' equity.

Independent auditor's report to the members of CYBG PLC

Key audit matters

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

Key audit matters	Our response to the risk	Key observations communicated to the Board's Audit Committee
Payment Protection Insurance ("PPI") and other conduct related provisioning Please refer to pages 79 to 87 (Audit Committee report), pages 219 to 222 (Provisions for liabilities and charges note), pages 237 to 238 (Contingent liabilities and commitments note). The Group has material provisions relating to its conduct towards its past and present customers relating to past PPI sales and other conduct related matters. The Group benefits from a conduct indemnity deed granted by its former parent, under which 90.3% of remediation costs for past conduct issues can be reimbursed up to a capped total amount. The Group contributes 9.7% of such costs. While this limits the impact on the Group's results and equity, unutilised amounts remaining under the indemnity are an important factor in the assessment of the Group's overall financial position. In March 2017, the FCA published Policy Statement 17/3 containing its final rules and guidance on PPI complaints. The Policy Statement confirmed a new rule that sets a deadline of 29 August 2019 for consumers to complain about the way they were sold PPI. During the year, the Group has also made progress with its past business review for other conduct related matters. Significant judgements and assumptions are required to be made by the Directors in relation to the timing, volume and quantum of future redress payments and associated administration costs that will be required. The most significant assumption is total anticipated future PPI complaint volumes. The effects of these judgements are material, so this was considered to be a significant audit risk.	We considered the results of the testing of key controls operating within the PPI and other conduct case handling and recording processes which supported the data used in the determination of key provision assumptions. We found that we could place reliance on these controls. We examined the models used by the Directors to determine a best estimate of the provisions for mis-sold payment protection insurance ("PPI") and other products. We assessed the appropriateness of PPI provision model assumptions, including case volumes, redress per claim, uphold rates and case processing costs, which were informed by the Group's historic experience. We tested the clerical accuracy of the Directors' provision calculations and sensitivity analysis. In evaluating the Directors' provision assumptions, we examined correspondence during the year between the Group and the FCA, and regulatory pronouncements, such as PS 17/3. We compared the Directors' assumptions to our own expectations based on the Group's historical experience, current trends and our industry knowledge.	We communicated to the Audit Committee that provisions for PPI redress and other conduct related matters held by the Group were reasonably estimated. We noted that the Bank's disclosures describe the uncertainties and risks associated with determining the provisions, and the sensitivity of the provisions to changes in key assumptions. As disclosed on page 222 in Note 3.14, we also noted that £148m of the Capped Indemnity remains undrawn, and that this provides a level of protection to the Group should future costs relating to PPI claims exceed the Directors' estimate. The estimations of provisions for PPI claims and other conduct related matters are inherently uncertain and required significant judgements to be made by the Directors. The Directors' best estimate for future PPI claims and associated costs involved probability weighting a number of possible outcomes. The most significant assumption is the volume of future, new PPI complaints, details of which are reported on page 220 in Note 3.14. We determined an independent range of reasonable future PPI cost outcomes using the Group's historical experience of PPI claims, and we compared this range to the Directors' estimate. We found no material differences in this comparison. We communicated to the Audit Committee that provisions for other conduct related matters, had been determined based on appropriate evidence and were fairly stated at 30 September 2017.

Key audit matters	Our response to the risk	Key observations communicated to the Board's Audit Committee
SME lending impairment provisions Please refer to pages 79 to 87 (Audit Committee report), and pages 210 to 212 (Impairment provisions on credit exposures note). The majority of the Group's non-retail lending portfolio relates to small and medium sized enterprises ('SMEs') which can be vulnerable to both domestic and foreign market volatility. Estimating the Group's collective and specific provisioning is subjective, requires the Directors to exercise significant judgement, and incorporates the use of various assumptions. Due to the materiality of the provisions and level of judgment involved, this was considered to be a significant audit risk.	We tested controls over impairment calculations and the generation of portfolio data for use in these calculations. These controls included those covering the identification and assessment of potentially impaired loans, the transfer of data from source systems to impairment models, and the calculation of specific impairment provisions. We determined that we could rely on these controls for the purposes of our audit. We performed loan file testing on a sample of impaired loans to determine whether the specific provisions held by the Group were, in our judgement, sufficient and appropriate. Our approach included the use of our own valuation specialists to independently test key assumptions underpinning a sample of collateral values used in provision calculations. We evaluated the completeness of SME loans assessed for impairment by the Directors and examined key loans where no impairment provisions were held. We tested the collective impairment provision model by examining the logic of the model calculations, the accuracy of data inputs, and the appropriateness of key assumptions and loan ratings used within the model. We tested the Directors' judgements in determining overlays to the collective impairment models for appropriateness of methodology and accuracy of calculation.	We communicated to the Audit Committee that the impairment models, calculations and assumptions employed by the Group were reasonable as at 30 September 2017 and that these resulted in impairment provisions that were appropriately estimated. We also concluded that the disclosures presented were in compliance with IFRSs. We independently determined a range of appropriate outcomes for the level of incurred but not reported losses existing in the Group's loan portfolio. The Directors' post model adjustments resided within our range of acceptable outcomes. We assessed and challenged the calculations and related judgements for a sample of specific impairment provisions and did not identify any material differences to the provisions determined by the Directors.

Independent auditor's report to the members of CYBG PLC

Key audit matters	Our response to the risk	Key observations communicated to the Board's Audit Committee
Revenue recognition – Effective Interest method Please refer to page 198 (net interest income accounting policy). For certain product fees, the Group operates a model to recognise fee income (included within interest income) under the effective interest method. The effective interest method spreads the recognition of product fee income over the life of a financial instrument, as these are in substance an integral part of the overall yield. Effective interest models are sensitive to judgements about the expected lives of the product portfolios to which they relate. Due to the complexity of calculations, the degree of judgement exercised by the Directors in respect of the expected lives of the product portfolios and the different products for which fees are recognised, this is considered a significant audit risk.	We gained an understanding of key controls and assessed the appropriateness of key assumptions used within the Group's effective interest model, primarily the average loan life assumption, which we corroborated against underlying loan data, our knowledge of market conditions and observed practice in the UK mortgage sector. We performed data integrity testing on the key sources of information feeding the effective interest calculation. This involved sample testing data from business systems to the loan data used in the model and vice-versa. We examined the journals recording the deferral and amortisation of fee income to verify that the revenue deferred and amortised over the life of the underlying loans was appropriate and aligned with the effective interest model output.	As set out on page 209 in Note 3.5, the Group has recorded £32m of net deferred income in relation to fee income and expenses deferred under the Group's effective interest method of accounting. We communicated to the Audit Committee that the effective interest adjustments recognised in interest income had been appropriately derived. We also communicated that the assumptions made by the Directors were reasonable in the context of the Group's lending portfolios and current observable customer behaviours.

In the prior year, our auditor's report included a key audit matter in relation to recoverability of the deferred tax asset. There was a significant reduction in the valuation of the Group's deferred tax asset in the prior financial year and consequently this was not considered a key audit matter in the current year.

Our application of materiality

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

Audit materiality

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

We determined audit materiality for the Group to be £17m (2016: £17m) which approximates 0.5% of the total equity attributable to owners of the Parent company ('Group equity'). The reason for selecting this measure as the basis for our audit materiality consideration is that the Group was loss making in recent financial periods. Given the importance of equity to the Group's solvency and regulatory capital resources, we judged equity to be the most relevant basis for setting audit materiality.

Performance materiality

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

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality should be set at 75% (2016: 50%) of our audit materiality, namely £12.75m (2016: £8.5m). We have set performance materiality at this percentage due to our previous experience as auditors of the Group, from which we concluded that there is a lower expectation of material financial statement inaccuracies due to the effective control environment and only minor audit differences resulting from our prior and current year work. We set performance materiality at a more conservative percentage of 50% in the prior year as 2016 was CYBG PLC's first year reporting as a publicly listed company.

Reporting threshold

This is the amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.85m (2016: £0.85m), which is set at 5% of our audit materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

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

Other information

The other information comprises the information included in the annual report set out on pages 1 to 175, including the Strategic Report set out on pages 1 to 37, the Financial Results set out on pages 38 to 48, Governance set out on pages 49 to 126, the Risk Report set out on pages 127 to 175, and Additional Information set out on pages 249 to 263 other than the financial statements and our auditor's report thereon. The Directors are responsible for the other information.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

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

We have nothing to report in this regard.

In this context, we also have nothing to report in regard to our responsibility to specifically address the following items in the other information and to report as uncorrected material misstatements of the other information where we conclude that those items meet the following conditions:

- **Fair, balanced and understandable** set out on page 126 – the statement given by the Directors that they consider the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the group's performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or
- **Audit committee reporting** set out on pages 79 to 87 – the section describing the work of the audit committee does not appropriately address matters communicated by us to the audit committee is materially inconsistent with our knowledge obtained in the audit; or
- **Directors' statement of compliance with the UK Corporate Governance Code** set out on page 62 – the parts of the Directors' statement required under the Listing Rules relating to the company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R(2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code.

Independent auditor's report to the members of CYBG PLC

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the Directors' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the Group and the Parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the Directors' report.

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

- adequate accounting records have not been kept by the Parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit

Responsibilities of Directors

As explained more fully in the Directors' responsibilities statement set out on page 126, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

Auditor's responsibilities for the audit of the financial statements

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

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

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

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Group and determined that the most significant were the regulations, licence conditions and supervisory requirements of the Prudential Regulation Authority ('PRA') and the Financial Conduct Authority ('FCA').
- We understood how the Group complies with these legal and regulatory frameworks by making enquiries of management, internal audit, and those responsible for legal and compliance matters. We also: reviewed correspondence between the Group and UK regulatory bodies; reviewed minutes of the Board and Executive Risk Committee; and gained an understanding of the Group's approach to governance, demonstrated by the Board's approval of the Group's governance framework and the Board's review of the Group's risk management framework ('RMF') and internal control processes.

- We assessed the susceptibility of the Group's financial statements to material misstatement, including how fraud might occur, by considering the controls that the Group has established to address risks identified by the entity, or that otherwise seek to prevent, deter or detect fraud. We also considered performance and incentive plan targets and their potential to influence management to manage earnings or influence the perceptions of investors.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations identified in the paragraphs above. Our procedures involved inquiries of legal counsel, executive management, internal audit, and focused testing, as referred to in the Key Audit Matters section above.
- The Group operates in the banking industry which is a highly regulated environment. As such the Senior Statutory Auditor considered the experience and expertise of the engagement team to ensure that the team had the appropriate competence and capabilities, which included the use of specialists where appropriate.

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

Other matters we are required to address:

- We were appointed as CYBG PLC's External Auditor and signed an engagement letter on 14 January 2016, prior to CYBG PLC becoming the holding company of the Group on its demerger from NAB and IPO in February 2016.
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Company and we remain independent of the Group and the Company in conducting the audit.
- The audit opinion is consistent with the additional report to the audit committee.

Ernst & Young LLP

Steven Robb (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP,
Statutory Auditor
Leeds

20 November 2017

Notes

1. The maintenance and integrity of the CYBG PLC website is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Consolidated income statement

for the year ended 30 September	Note	2017 £m	2016 £m
Interest income and similar income		**1,075**	1,101
Interest expense and similar charges		**(231)**	(295)
Net interest income	2.2	**844**	806
Gains less losses on financial instruments at fair value		**6**	9
Other operating income		**186**	182
Non-interest income	2.3	**192**	191
Total operating income		**1,036**	997
Personnel expenses		**(166)**	(280)
Restructuring expenses		**(67)**	(45)
Depreciation and amortisation expense		**(87)**	(88)
Other operating and administrative expenses		**(400)**	(468)
Total operating and administrative expenses before impairment losses	2.4	**(720)**	(881)
Operating profit before impairment losses		**316**	116
Impairment losses on credit exposures	3.6	**(48)**	(39)
Profit on ordinary activities before tax		**268**	77
Tax expense	2.5	**(86)**	(241)
Profit/(loss) for the year		**182**	(164)
Profit/(loss) attributable to ordinary shareholders		**146**	(206)
Profit attributable to other equity holders		**36**	42
Profit/(loss) for the year attributable to equity holders		**182**	(164)
Basic earnings/(loss) per share (pence)	2.6	**17.3**	(22.5)
Diluted earnings/(loss) per share (pence)	2.6	**17.2**	(22.5)

All material items dealt with in arriving at the profit before tax for the above years relate to continuing activities.

The notes on pages 191 to 240 form an integral part of these financial statements.

Consolidated statement of comprehensive income

for the year ended 30 September	Note	2017 £m	2016 £m
Profit/(loss) for the year		**182**	(164)
Items that may be reclassified to the income statement			
Change in cash flow hedge reserve			
(Losses)/gains during the year		**(84)**	105
Transfers to the income statement		**(4)**	(1)
Taxation thereon		**21**	(25)
		(67)	79
Change in available for sale reserve			
(Losses)/gains during the year		**(7)**	29
Transfers to the income statement		**(20)**	(8)
Taxation thereon		**7**	(6)
		(20)	15
Total items that may be reclassified to the income statement		**(87)**	94
Items that will not be reclassified to the income statement			
Remeasurement of defined benefit pension plans	3.16	**154**	(179)
Taxation thereon		**(35)**	43
Total items that will not be reclassified to the income statement		**119**	(136)
Other comprehensive income/(losses), net of tax		**32**	(42)
Total comprehensive income/(losses) for the year, net of tax		**214**	(206)
Total comprehensive income/(losses) attributable to ordinary shareholders		**178**	(248)
Total comprehensive income attributable to other equity holders		**36**	42
Total comprehensive income/(losses) attributable to equity holders		**214**	(206)

The notes on pages 191 to 240 form an integral part of these financial statements.

Consolidated balance sheet

as at 30 September	Note	2017 £m	2016 £m
Assets			
Cash and balances with central banks	3.1	**6,937**	5,955
Due from other banks		**1,174**	952
Financial assets available for sale	3.2	**2,076**	1,731
Other financial assets at fair value	3.3	**477**	750
Derivative financial instruments	3.4	**282**	585
Loans and advances to customers	3.5	**31,293**	29,202
Due from customers on acceptances		**4**	4
Current tax assets		**–**	2
Property, plant and equipment	3.8	**86**	99
Investment properties	3.9	**14**	22
Intangible assets	3.10	**339**	256
Deferred tax assets	3.11	**154**	183
Defined benefit pension assets	3.16	**207**	–
Other assets		**188**	188
Total assets		**43,231**	39,929
Liabilities			
Due to other banks	3.12	**3,817**	1,309
Other financial liabilities at fair value	3.3	**26**	48
Derivative financial instruments	3.4	**376**	598
Due to customers	3.13	**27,718**	27,090
Liabilities on acceptances		**4**	4
Provisions for liabilities and charges	3.14	**554**	852
Debt securities in issue	3.15	**4,785**	4,501
Retirement benefit obligations	3.16	**3**	79
Deferred tax liabilities	3.11	**75**	27
Other liabilities	3.17	**2,471**	2,210
Total liabilities		**39,829**	36,718
Equity			
Share capital	4.1	**88**	88
Other equity instruments	4.1	**450**	450
Capital reorganisation reserve	4.1	**(839)**	(839)
Merger reserve	4.1	**633**	633
Other reserves	4.1	**15**	100
Retained earnings		**3,055**	2,779
Total equity		**3,402**	3,211
Total liabilities and equity		**43,231**	39,929

The notes on pages 191 to 240 form an integral part of these financial statements.

These financial statements were approved by the Board of Directors on 20 November 2017 and were signed on its behalf by:

David Duffy
Chief Executive Officer

Ian Smith
Chief Financial Officer

CYBG PLC, Registered number: 09595911

Consolidated statement of changes in equity

	Note	Share capital £m	Share premium account £m	Capital reorganisation reserve £m	Merger reserve £m	Other equity instruments £m	Other reserves: Equity based compensation reserve £m	Other reserves: Asset revaluation reserve £m	Other reserves: Available for sale reserve £m	Other reserves: Cash flow hedge reserve £m	Retained earnings £m	Total equity £m
As at 1 October 2015		223	670	–	–	450	3	2	12	(13)	2,096	3,443
Loss for the year		–	–	–	–	–	–	–	–	–	(164)	(164)
Other comprehensive income/(losses), net of tax		–	–	–	–	–	–	–	15	79	(136)	(42)
Total comprehensive income/(losses) for the year		–	–	–	–	–	–	–	15	79	(300)	(206)
AT1 distribution paid (net of tax)		–	–	–	–	–	–	–	–	–	(28)	(28)
Insertion of new parent company		(223)	(670)	893	–	–	–	–	–	–	–	–
Share for share exchange		1,099	–	(1,732)	633	–	–	–	–	–	–	–
Share capital reduction		(1,011)	–	–	–	–	–	–	–	–	1,011	–
Capital note repurchase (net of tax)		–	–	–	–	(450)	–	–	–	–	(5)	(455)
Capital note issued		–	–	–	–	450	–	–	–	–	–	450
Transfer from equity based compensation reserve		–	–	–	–	–	(4)	–	–	–	4	–
Transfer from asset revaluation reserve		–	–	–	–	–	–	(1)	–	–	1	–
Equity based compensation expensed		–	–	–	–	–	5	–	–	–	–	5
Equity based compensation settled		–	–	–	–	–	2	–	–	–	–	2
As at 30 September 2016	4.1	88	–	(839)	633	450	6	1	27	66	2,779	3,211
Profit for the year		–	–	–	–	–	–	–	–	–	182	182
Other comprehensive (losses)/income, net of tax		–	–	–	–	–	–	–	(20)	(67)	119	32
Total comprehensive (losses)/income for the year		–	–	–	–	–	–	–	(20)	(67)	301	214
AT1 distribution paid (net of tax)		–	–	–	–	–	–	–	–	–	(29)	(29)
Transfer from equity based compensation reserve		–	–	–	–	–	(4)	–	–	–	4	–
Equity based compensation expensed		–	–	–	–	–	6	–	–	–	–	6
As at 30 September 2017	4.1	**88**	**–**	**(839)**	**633**	**450**	**8**	**1**	**7**	**(1)**	**3,055**	**3,402**

The notes on pages 191 to 240 form an integral part of these financial statements.

Consolidated statement of cash flows

for the year ended 30 September	Note	2017 £m	2016 £m
Operating activities			
Profit on ordinary activities before tax		**268**	77
Adjustments for:			
Non-cash or non-operating items included in profit before tax	5.2	**(728)**	(643)
Changes in operating assets	5.2	**(1,857)**	(2,285)
Changes in operating liabilities	5.2	**919**	1,587
Interest received		**1,123**	1,101
Interest paid		**(258)**	(200)
Tax received/(paid) – Group relief		**1**	4
Net cash used in operating activities		**(532)**	(359)
Cash flows from investing activities			
Interest received		**11**	11
Proceeds from sale or maturity of investments		**20**	101
Proceeds from sale of tangible fixed assets[1]		**19**	17
Purchase of tangible fixed assets[1]		**(21)**	(22)
Purchases of investments		**(492)**	(357)
Proceeds from sale of available for sale investments		**60**	56
Purchase and development of intangible assets		**(148)**	(99)
Net cash used in investing activities		**(551)**	(293)
Cash flows from financing activities			
Interest received		**3**	1
Interest paid		**(90)**	(98)
Proceeds from other equity instruments issued		**–**	450
Repurchase of other equity instruments		**–**	(457)
Repurchase of subordinated debt		**–**	(474)
Redemption and principal repayment on residential mortgage backed securities and covered bonds	3.7	**(740)**	(1,029)
Issuance of residential mortgage backed securities and covered bonds	3.7	**750**	750
Issuance of medium-term notes/subordinated debt	3.15	**298**	475
Amounts drawn under the TFS		**1,900**	–
Net decrease in amounts due from related entities		**–**	786
Net decrease in amounts due to related entities		**–**	(106)
Equity based compensation		**–**	2
AT1 distributions		**(36)**	(35)
Net cash provided by financing activities		**2,085**	265
Net increase/(decrease) in cash and cash equivalents		**1,002**	(387)
Cash and cash equivalents at the beginning of the year		**5,950**	6,337
Cash and cash equivalents at the end of the year[2]	5.2	**6,952**	5,950

(1) Tangible fixed assets include property, plant and equipment, investment properties and property inventory.
(2) Cash and cash equivalents is cash and balances with central banks less mandatory deposits plus cash equivalents within other assets, less due to other banks, due to related entities and other liabilities.

The notes on pages 191 to 240 form an integral part of these financial statements.

Notes to the consolidated financial statements

Section 1: Basis of preparation

Overview
This section sets out the Group's accounting policies that relate to the consolidated financial statements as a whole. Where an accounting policy is specific to one note, the policy is described in the note to which it relates. This section also shows new accounting standards, amendments and interpretations, relevant to the Group, and whether they are effective in 2017 or later years. We explain how these changes are expected to impact the financial position and performance of the Group.

1.1 General information
The Company is a public company limited by shares, incorporated in the United Kingdom under the Companies Act and registered in England and Wales.

The consolidated financial statements comprise those of the Company and its controlled entities, together the 'Group'.

1.2 Basis of accounting
The consolidated financial statements have been prepared in accordance with IFRS as adopted by the EU and in accordance with the provisions of the Companies Act 2006.

The financial information has been prepared under the historical cost convention, as modified by the revaluation of land and buildings, investment properties, financial assets available for sale and certain other financial assets and liabilities at fair value through profit or loss. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

1.3 Presentation of risk offsetting and maturity disclosures
Certain disclosures required under IFRS 7 'Financial instruments: disclosures' and IAS 1 'Presentation of financial statements' have been included within the audited sections of the Risk report. Where information is marked as audited, it is incorporated into these financial statements by this cross reference and it is covered by the Independent auditor's report.

1.4 Going concern
The Group's business activities, together with the factors likely to affect its future development, performance and position, are set out in the Strategic report. In addition, the Risk report includes the Group's risk management objectives and the Group's objectives, policies and processes for managing its capital.

In assessing the Group's going concern position as at 30 September 2017, the Directors have considered a number of factors, including the current balance sheet position, the principal and emerging risks which could impact the performance of the Group and the Group's strategic and financial plan which includes future projections of profitability, capital adequacy, liquidity and funding. The assessment concluded that, for the foreseeable future, the Group has sufficient capital to support its operations; has a funding and liquidity base which is strong, robust and well managed with future capacity; and has expectations that performance will continue to improve as the Group's strategy is executed.

As a result of the assessment, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future and therefore believe that the Group is well placed to manage its risks successfully in line with its business model and strategic aims. Accordingly, they continue to adopt the going concern basis in preparing the consolidated financial statements.

1.5 Basis of consolidation
Controlled entities are all entities (including structured entities) to which the Company is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. An assessment of control is performed on an ongoing basis.

Controlled entities are consolidated from the date on which control is established by the Group until the date that control ceases. The acquisition method of accounting is used to account for business combinations other than those under common control. A non-controlling interest is recognised by the Group in respect of any portion of the total assets less total liabilities of an acquired entity or entities that is not owned by the Group. Post-acquisition, income received and expenses incurred by the entity or entities acquired are included in the consolidated income statement on a line by line basis in accordance with the accounting policies set out herein. Balances and transactions between entities within the Group and any unrealised gains and losses arising from those transactions are eliminated in full upon consolidation.

The consolidated financial statements have been prepared using uniform accounting policies.

Section 1: Basis of preparation continued

1.6 Foreign currency

Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The consolidated financial statements are presented in pounds sterling (GBP), which is also the Group's presentation currency, rounded to the nearest million pounds sterling (£m) unless otherwise stated.

Transactions and balances

The Group records an asset, liability, expense or revenue arising from a transaction using the closing exchange rate between the functional and foreign currency on the transaction date. At each subsequent reporting date, the Group translates foreign currency monetary items at the closing rate. Foreign exchange differences arising on translation or settlement of monetary items are recognised in the income statement during the year in which the gains or losses arise.

Foreign currency non-monetary items measured at historical cost are translated at the date of the transaction, with those measured at fair value translated at the date when the fair value is determined. Foreign exchange differences are recognised directly in equity for non-monetary items where any component of associated gains or losses is recognised directly in equity. Foreign exchange differences arising from non-monetary items, whereby the associated gains or losses are recognised in the income statement, are also recognised in the income statement.

1.7 Financial assets and liabilities

Recognition and derecognition

A financial asset or a financial liability is recognised on the balance sheet when the Group becomes party to the contractual provisions of the instrument. Purchases and sales of financial assets classified within fair value through profit or loss are recognised on trade date.

The Group derecognises a financial asset when the contractual cash flows from the asset expire or it transfers the right to receive contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership are transferred. Financial liabilities are derecognised when the Group has discharged its obligation to the contract, or the contract is cancelled or expires.

Offsetting

This can only occur, and the net amount be presented on the balance sheet, when the Group currently has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

1.8 Critical accounting estimates and judgements

The preparation of financial statements requires the use of certain critical accounting estimates and judgements that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosed amount of contingent liabilities. Assumptions made at each balance sheet date are based on best estimates at that date. Although the Group has internal control systems in place to ensure that estimates can be reliably measured, actual amounts may differ from those estimates. The Group considers the most significant use of accounting estimates and judgements relate to the following areas:

- financial assets and liabilities at fair value through profit or loss (note 3.3);
- impairment provisions on credit exposures (note 3.6);
- deferred tax (note 3.11);
- PPI redress provision and other conduct related matters (note 3.14); and
- retirement benefit obligations (note 3.16).

1.9 New accounting standards and interpretations

The Group has adopted the following International Accounting Standards Board (IASB) pronouncements in the current financial year. Except where otherwise stated, these did not have a material impact on the Group's consolidated financial statements:

- amendments to IAS 16 and IAS 38: 'Clarification of Acceptable Methods of Depreciation and Amortisation', issued May 2014 and effective for financial years beginning on or after 1 January 2016. IAS 16 and IAS 38 both establish the principle for the basis of depreciation and amortisation being the expected pattern of consumption of the future economic benefits of an asset. This amendment provides clarification that the use of certain revenue based methods to calculate depreciation is not appropriate.
- 'Annual Improvements to IFRS Standards 2012-2014 Cycle', issued September 2014 and effective for financial years beginning on or after 1 January 2016. The IASB has made amendments to the following standards that are relevant to the Group: IFRS 5: 'Non-current Assets Held for Sale and Discontinued Operations'; IFRS 7: 'Financial Instruments: Disclosures'; IAS 19: 'Employee Benefits'; and IAS 34: 'Interim Financial Reporting'.
- amendments to IAS 1: 'Disclosure Initiative', issued December 2014 and effective for financial years beginning on or after 1 January 2016. This includes a narrow scope amendment providing clarification to existing IAS 1: 'Presentation of Financial Statements' requirements.

New accounting standards and interpretations not yet adopted

IFRS 9 'Financial Instruments' (issued July 2014) and IFRS 15 'Revenue from Contracts with Customers' (issued September 2015) are both effective for financial years beginning on or after 1 January 2018 and have been endorsed by the EU. IFRS 16 'Leases' was issued in January 2016 and is effective for financial years beginning on or after 1 January 2019 and has been endorsed by the EU. Separate updates on the Group's implementation of these new standards can be found at the end of this section.

There are a number of other standards and amendments that are either not available for adoption in the EU or are otherwise not mandatory at 30 September 2017 and have not been applied by the Group in preparing these financial statements. The pronouncements, while relevant to the Group, are not anticipated to have a material impact and include:

- amendments to IAS 12: 'Recognition of Deferred Tax Assets for Unrealised Losses'(1), issued in January 2016 and effective for financial years beginning on or after 1 January 2017. The amendments clarify the requirements on the recognition of deferred tax assets for unrealised losses;
- amendments to IAS 7: 'Disclosure initiative'(1), issued in January 2016 and effective for financial years beginning on or after 1 January 2017. The amendments to IAS 7: 'Statement of Cash Flows' require disclosures that enable users of the financial statements to evaluate changes in liabilities arising from an entity's financing activities;
- amendments to IFRS 2: 'Classification and Measurement of Share-based Payment Transactions'(2), issued in June 2016 and effective for financial years beginning on or after 1 January 2017. The amendments provide guidance on the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments; classification of share-based payments with a net settlement feature for withholding tax obligations; and accounting for modifications to a share-based payment that change the classification from cash-settled to equity-settled;
- amendments to IFRS 9: 'Prepayment Features with Negative Compensation'(2), issued in October 2017 and effective for financial years beginning on or after 1 January 2019. The amendments allow companies to measure particular prepayable financial assets with so-called negative compensation at amortised cost or at fair value through other comprehensive income if a specified condition is met, instead of at fair value through profit or loss;
- 'Annual Improvements to IFRS Standards 2014-2016 Cycle'(2), issued December 2016 and effective for financial years beginning on or after 1 January 2017 or 1 January 2018. The IASB has made amendments to the following standards: IFRS 12: 'Disclosure of Interests in Other Entities' (clarification of the scope of the standard – effective 1 January 2017), and IAS 28: 'Investments in Associates and Joint Ventures' (measuring an associate or joint venture at fair value – effective 1 January 2018);
- IFRIC interpretation 22: 'Foreign Currency Transactions and Advance Consideration'(2), issued December 2016 and effective for financial years beginning on or after 1 January 2018. The new interpretation provides requirements on which exchange rate to use in reporting foreign currency transactions (such as revenue transactions) when payment is made or received in advance; and
- IFRIC interpretation 23: 'Uncertainty over Income Tax Treatments'(2), issued June 2017 and effective for financial years beginning on or after 1 January 2019. The new interpretation applies to any situation in which there is uncertainty as to whether an income tax treatment is acceptable under tax law and is not limited to actual ongoing disputes.

(1) Endorsed by the EU.
(2) Not yet endorsed by the EU.

Section 1: Basis of preparation continued

1.9 New accounting standards and interpretations continued

Updates on the implementation of IFRS 9: 'Financial Instruments', IFRS 15: 'Revenue from Contracts with Customers' and IFRS 16: 'Leases'

The Group continues to assess the requirements of these Standards as it seeks to ensure that the methodology and approach to the key impacts and challenges of the Standards result in a high quality implementation, while continuing to recognise emerging and evolving industry practice.

IFRS 9

CYBG implementation strategy and approach

IFRS 9 was endorsed for adoption in the EU in November 2016 and will be adopted by the Group with effect from 1 October 2018.

Classification and measurement

IFRS 9 changes the classification of financial assets by reducing the number of categories to just three (amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL)). The final classification is based on a combination of the Group's business model and the contractual cash flow characteristics of the instruments. The option to designate a financial asset at FVTPL in IAS 39 is largely retained in IFRS 9, with IFRS 9 also affording a further option to designate certain equity instruments at FVOCI instead of accounting for these as FVTPL. The Group has undertaken an assessment to determine the potential impact of these changes. These are unlikely to result in significant changes to existing measurement bases; however, the final impact will be dependent on the circumstances prevailing on 1 October 2018.

Impairment overview

The Group's IFRS 9 implementation programme is progressing as planned with models built and an end-to-end parallel run exercise to commence during the year beginning 1 October 2017. As expected, there will be a period of refinement required where the series of complex decisions, judgements and assumptions made, particularly in relation to the Group's model methodology, that will be reviewed, sufficiently tested and benchmarked. It is only after a period where the testing environment has stabilised, that the results of the parallel run will provide an indication of the likely impact.

The Group's approach to the new expected credit loss (ECL) methodology in IFRS 9 will leverage, as far as possible, off the model development work that has been undertaken to support the Group's IRB accreditation application. A lifetime ECL calculation will be required for scenarios where the credit quality of a financial asset has been identified through the Group's staging criteria as having significantly deteriorated since original recognition.

The Group's 12 month and lifetime ECL calculation will be based around a 'PD x EAD x LGD' formula:

Term	Defined as	To be IFRS 9 compliant
PD	Probability of default (PD) is an estimate of the probability that a customer will default	Forward-looking 12 month and lifetime PD, which needs to be capable of reflecting changes in the economic environment
EAD	Exposure at default (EAD) is an estimate of the amount the customer will owe at the time of default	Forward-looking and based on contractual limits with certain exceptions for revolving products (such as credit cards) that may contain both a drawn and undrawn element
LGD	Loss given default (LGD) is an estimate of the loss that the Group will suffer if the customer defaults (incorporating any collateral held)	Forward looking with no prescribed floors

There are a number of specific key elements to the IFRS 9 ECL calculation which require the Group to define and articulate the direction it will take in meeting these – that is ensuring that the ECL calculation is *forward-looking* and encompasses a *probability weighted multiple scenario* approach.

The Group currently adopts economic scenario methodology for capital planning and credit stress testing purposes and views the introduction of the IFRS 9 requirements as an extension to these established processes. The Group will align the specific requirements of IFRS 9 to these to ensure a consistent approach is adopted.

The exact nature and number of the economic scenarios (including the necessary economic inputs required for the scenarios), along with their relevant probability weightings, were finalised following experienced credit judgement, discussion and agreement with stakeholders. This will be subject to refinement as the parallel run period progresses.

The adoption of IFRS 9 may result in an increase in the Group's balance sheet provisions for credit losses and may therefore have a negative impact on the Group's regulatory capital position.

Hedge accounting
Macro hedge accounting is being considered in a separate IASB project. There is an option available to retain the existing IAS 39 hedge accounting requirements until the completion of the macro hedge accounting project. The Group proposes to continue applying the hedge accounting requirements of IAS 39 in accordance with this option.

Regulatory capital
The Group notes the pronouncements regarding transitional relief for the likely regulatory capital impact of adopting IFRS 9 from the Basel Committee and also the European Parliament and Commission and will continue to monitor the regulatory landscape over the year ahead in the lead up to the Group's adoption of IFRS 9 for final details on the regulatory capital treatment of the change to an ECL methodology.

The Group will consider the option of spreading the effect of the change to an ECL methodology for regulatory capital purposes should this feature in the finalised version of the rules.

IFRS 15
IFRS 15 was issued in May 2014 and endorsed for use in the EU in September 2016. It is effective for financial years beginning on or after 1 January 2018, and it will be adopted by the Group with effect from 1 October 2018.

The Standard is unlikely to have a significant impact as the majority of the Group's income is generated from financial instruments and is therefore not in scope of the Standard. For those revenues that are in scope (typically fees and other commissions), the Group continues to assess the related performance obligations to identify any fees or other commissions that may require a change in recognition. The Group continues to assess the new disclosure requirements of the Standard.

IFRS 16
IFRS 16 was issued in January 2016 and endorsed for use in the EU. It is effective for financial years beginning on or after 1 January 2019, and will be adopted by the Group with effect from 1 October 2019.

The Group continues to work on and assess the new estimates and judgements required by the Standard and their implications. Operating leases will be brought onto the Group balance sheet with an asset recognised for the contractual 'right of use' and a liability recognised for the contractual payments. The Group expects this work to progress throughout the 2018 reporting period.

Section 2: Results for the year

2.1 Segment information

The Group's operating segments are operating units engaged in providing different products or services and whose operating results and overall performance are regularly reviewed by the Group's Chief Operating Decision Maker, the Executive Leadership Team.

The Group's business is organised into two principal operating segments: SME banking and Retail banking. In addition, Central Functions consist of the Group's back office support functions.

SME banking

The Group's established regional SME franchise offers a full range of banking products and services to meet business customers' banking needs across its small business, commercial, corporate and specialist and acquisition finance segments.

The Group's SME franchise comprises small businesses (which the Group defines as businesses with lending of up to £0.5m but less than £2.0m in turnover) and commercial businesses (which the Group defines as businesses with lending of more than £0.5m and greater than £2.0m in turnover).

Through its SME franchise, the Group offers a full range of lending products and services across a portfolio consisting of term lending, overdrafts and working capital solutions:

- term lending: the Group offers a wide variety of term loans, both secured and unsecured, and offers customers a range of repayment and interest rate options. The majority of the Group's business term lending is LIBOR based;
- overdrafts: business overdrafts are the primary type of revolving variable rate credit facility offered by the Group to business customers;
- invoice finance: the Group advances funds against the customer's trade receivables;
- asset finance: these products provide a method of financing capital equipment purchases;
- international trade services: these products facilitate transactions between a buyer and seller located in different countries. The Group offers import loans, export loans, documentary collections and currency guarantees, together with letters of credit for securing trade; and
- business current accounts: the Group provides business customers day to day banking, current account facilities (including debit cards, cheque books, regular statements, direct debits and standing orders), and online banking.

Retail banking

The Group has a comprehensive regional and national retail banking product proposition with a personal deposit portfolio comprising personal current accounts (PCA), savings accounts and term deposits. The Group's Retail lending portfolio comprises mortgages, personal loans, credit cards, overdrafts and introductions to insurance and investment products through its branch network:

- PCA: the Group offers a full range of PCAs, including, for example, B, a newly launched digital proposition, together with a packaged bank account and a basic bank account;
- savings accounts: the Group offers a variety of savings accounts that pay a variable rate of interest. It also offers cash ISAs that provide depositors tax free returns;
- term deposits: offer a fixed interest rate for a fixed term;
- mortgages: the Group provides mortgage loans on a capital repayment basis, where the loan is required to be repaid during its life, and on an interest-only basis, where the customer pays interest during the term of the mortgage loan with the principal balance required to be repaid in full at maturity. The Group offers both owner occupied mortgage loans and BTL loans;
- personal loans: the Group provides unsecured personal loans through its branch network and through its digital and telephone distribution channels;
- credit cards: the Group currently offers four credit card products; Private MasterCard, Business MasterCard, Gold MasterCard and B MasterCard; and
- overdrafts: the Group provides overdraft lending across a variety of PCA products, subject to the account holder's status.

Geographical areas

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

Operating segments 2017	**SME banking £m**	**Retail banking £m**	**Central functions £m**	**Other[(1)] £m**	**Total £m**
Net interest income	**251**	**644**	**(51)**	**–**	**844**
Non-interest income	**83**	**100**	**(11)**	**20**	**192**
Operating income	**334**	**744**	**(62)**	**20**	**1,036**
Operating and administrative expenses	**(61)**	**(97)**	**(517)**	**(45)**	**(720)**
Impairment losses on credit exposures[(2)]	**(33)**	**(15)**	**–**	**–**	**(48)**
Segment operating profit/(loss) before tax	**240**	**632**	**(579)**	**(25)**	**268**
Average interest earning assets	**10,154[(3)]**	**20,577**	**6,966**	**–**	**37,697**

Operating segments[(4)] 2016	SME banking £m	Retail banking £m	Central functions £m	Other[(1)] £m	Total £m
Net interest income	242	627	(63)	–	806
Non-interest income	87	100	(4)	8	191
Operating income	329	727	(67)	8	997
Operating and administrative expenses	(70)	(119)	(540)	(152)	(881)
Impairment losses on credit exposures[(2)]	(30)	(9)	–	–	(39)
Segment operating profit/(loss) before tax	229	599	(607)	(144)	77
Average interest earning assets	10,404[(3)]	19,063	6,790	–	36,257

(1) 'Other' reflects underlying adjustments to the statutory view of performance and is therefore not recharged to the Group's two principal operating segments, such as conduct related provisions and restructuring costs. For a breakdown of the items included in this category, refer to 'Measuring financial performance – glossary'.

(2) The impairment losses on credit exposures of £15m (2016: £9m) for Retail banking includes losses on certain retail products attributable to SME (private banking) customers.

(3) Average interest earning assets for SME banking include £2.9bn (2016: £3.3bn) of mortgages originated by private banking.

(4) Comparative disclosures have been amended to conform with the current period's presentation.

Liabilities are managed on a centralised basis and therefore are not disclosed by segment.

Section 2: Results for the year continued

2.2 Net interest income

Accounting policy
Interest income is reflected in the income statement using the effective interest method which discounts the estimated future cash payments or receipts over the expected life of the financial instrument, to the net carrying amount of the financial asset or liability.

When calculating the effective interest rate, cash flows are estimated considering all contractual terms of the financial instrument (e.g. prepayment, call and similar options) excluding future credit losses. The calculation includes all fees and points paid or received that are an integral part of the effective interest rate such as transaction costs and all other premiums or discounts. Where it is not possible to reliably estimate the cash flows or the expected life of a financial instrument (or group of financial instruments), the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments) are used.

Loan origination and commitment fees are recognised within the effective interest rate calculation. Non-utilisation of a commitment fee is recognised as revenue upon expiry of the agreed commitment period. Loan related administration and service fees are recognised as revenue over the period of service.

Interest income and interest expense on hedged assets and liabilities and financial assets and liabilities designated as fair value through profit or loss are also recognised as part of net interest income.

Where a trading derivative is economically hedging an interest-bearing financial asset or liability designated at fair value through profit or loss, the interest income and expense attributable to the derivative is recognised within net interest income and not as part of the fair value movement of the trading derivative.

	2017 £m	2016 £m
Interest income and similar income		
Loans and advances to other banks	**11**	22
Financial assets available for sale	**11**	11
Loans and advances to customers	**1,030**	1,037
Financial assets at fair value through profit or loss	**18**	27
Due from related entities	**–**	1
Other interest income	**5**	3
Total interest income and similar income	**1,075**	1,101
Less: interest expense and similar charges		
Due to other banks	**15**	8
Financial liabilities at fair value through profit or loss	**–**	1
Due to customers	**126**	188
Debt securities in issue	**90**	87
Due to related entities	**–**	11
Total interest expense and similar charges	**231**	295
Net interest income	**844**	806

2.3 Non-interest income

Accounting policy

Gains less losses on financial instruments at fair value

This includes fair value gains and losses from three distinct activities:

- derivatives classified as held for trading – the full change in fair value of trading derivatives is recognised inclusive of interest income and expense arising on those derivatives except when economically hedging other assets and liabilities at fair value outlined in note 2.2;
- other financial assets and liabilities designated at fair value through profit or loss – these relate to the Group's fixed interest rate loan portfolio and related term deposits (note 3.3), which were designated at inception as fair value through profit or loss. The fair value of these loans is derived from the future loan cash flows using appropriate discount rates and includes adjustments for credit risk and credit losses. The valuation technique used is reflective of current market practice; and
- hedged assets, liabilities and derivatives designated in hedge relationships – fair value movements are recognised on both the hedged item and hedging derivative in a fair value hedge relationship (the net of which represents hedge ineffectiveness), and hedge ineffectiveness on cash flow hedge relationships (note 3.4).

Fees and commissions

Where not integral to the effective interest rate, these are recognised on an accruals basis as the services are provided or on completion of the underlying transaction.

	2017 £m	2016 £m
Gains less losses on financial instruments at fair value		
Interest rate derivatives	**45**	3
Other assets and liabilities at fair value(1)	**(35)**	7
Ineffectiveness arising from fair value hedges (note 3.4)	**(4)**	–
Ineffectiveness arising from cash flow hedges (note 3.4)	**–**	(1)
	6	9
Other operating income		
Fees and commissions	**146**	151
Margin on foreign exchange derivative brokerage	**18**	19
Gains on disposal of available for sale financial assets	**20**	8
Net fair value movement on investment properties	**(1)**	(1)
Other income	**3**	5
	186	182
Total non-interest income	**192**	191

(1) A credit risk gain on other assets and liabilities at fair value of £6m, offset by a fair value loss of £41m, has been recognised in the current year (2016: £11m gain and £4m loss, respectively).

On 28 April 2017, MasterCard completed its acquisition of 94.2% of VocaLink. By virtue of its 3.24% shareholding in VocaLink, the Group received cash consideration of £25m. The resulting gain of £20m, which was recognised in the available for sale reserve following the acquisition announcement in 2016, was recycled to the income statement and is included within 'Gains on disposal of available for sale financial assets' in the current year.

Section 2: Results for the year continued

2.4 Operating and administrative expenses

Accounting policy
Personnel expenses primarily consist of wages and salaries, accrued bonus and social security costs arising from services rendered by employees during the financial year.

The Group recognises bonus costs where it has a present obligation that can be reliably measured. Bonus costs are recognised over the relevant service period required to entitle the employee to the reward.

The Group's accounting policies on pension expenses and equity based compensation are included in notes 3.16 and 4.2 respectively.

	2017 £m	2016 £m
Personnel expenses	**166**	280
Restructuring expenses (note 3.14)	**67**	45
Depreciation and amortisation expense (notes 3.8, 3.10)	**87**	88
Other operating and administrative expenses	**400**	468
Total operating and administrative expenses	**720**	881

Personnel expenses comprise the following items:

	2017 £m	2016 £m
Salaries, wages and non-cash benefits and social security costs	**171**	211
Defined contribution pension expense	**19**	20
Defined benefit pension (income)/expense (note 3.16)	**(54)**	28
Equity based compensation (note 4.2)	**6**	5
Other personnel expenses	**24**	16
Personnel expenses	**166**	280

The Group recognised gains in relation to its defined benefit pension scheme in the year. A past service credit of £88m is included in personnel expenses as a result of the closure of the Scheme to future accrual for the majority of members. In addition, a curtailment gain of £13m was recognised in respect of redundancies which did not attract an enhancement entitlement and offsets against the related restructuring costs.

The average number of FTE employees of the Group during the year was made up as follows:

	2017 Number	2016 Number
Managers	**2,234**	2,460
Clerical staff	**3,806**	4,258
	6,040	6,718

The average monthly number of employees was 6,818 (2016: 7,567).

All staff are contracted employees of the Group and its subsidiary undertakings. The average figures above do not include contractors.

Other items of significance to the Group which are included within other operating and administrative expenses are:

	2017 £m	2016 £m
Operating lease charges	**29**	30
Impairment losses on software (note 3.10)	**–**	45
PPI redress expense (note 3.14)	**48**	44
Other conduct expenses (note 3.14)	**10**	7
Separation costs	**8**	11
Auditor's remuneration	**2**	2

Auditor's remuneration included within other operating and administrative expenses:

	2017 £'000	2016 £'000
Fees payable to the Company's auditor for the audit of the Company's financial statements	**20**	20
Fees payable to the Company's auditor for the audit of the Company's subsidiaries	**1,251**	1,387
Total audit fees	**1,271**	1,407
Audit related assurance services	**124**	180
Other assurance services	**308**	35
Total non-audit fees	**432**	215
Fees payable to the Company's auditor in respect of associated pension schemes	**63**	75
Total fees payable to the Company's auditor	**1,766**	1,697

Non-audit services performed by the auditor during the year included agreed upon procedures under the Conduct Indemnity arrangement with NAB; regular profit attestations; preparation of a comfort letter for the global medium term note programme issuance; and a client asset regulatory review.

In addition to the above, out of pocket expenses of £48k (2016: £58k) were borne by the Group, principally related to reimbursement of travel expenses incurred by staff when performing the above services.

2.5 Taxation

Accounting policy

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it is related to items recognised directly in equity, in which case the tax is also recognised in equity.

Current tax is the expected tax payable or receivable on the taxable profit or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years. Deferred tax assets and liabilities are recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax is determined using tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

	2017 £m	2016 £m
Current tax		
UK corporation tax		
Current year	**17**	12
Adjustment in respect of prior years	**–**	(3)
	17	9
Deferred tax (note 3.11)		
Current year	**64**	236
Adjustment in respect of prior years	**5**	(4)
	69	232
Tax expense for the year	**86**	241

The tax assessed for the year differs from that arising from applying the standard rate of corporation tax in the UK. A reconciliation from the expense implied by the standard rate to the actual tax expense is as follows:

	2017 £m	2016 £m
Profit on ordinary activities before tax	**268**	77
Tax expense based on the standard rate of corporation tax in the UK of 19.5% (2016: 20%)	**52**	15
Effects of:		
Disallowable expenses	**9**	8
Conduct indemnity adjustment	**7**	(1)
Deferred tax assets (recognised)/written off	**(21)**	237
Impact of rate changes	**34**	(11)
Adjustments in respect of prior years	**5**	(7)
Tax expense for the year	**86**	241

Section 2: Results for the year continued

2.5 Taxation continued

The total amount of tax, current and deferred, recognised directly in equity during the year was a credit of £1m (2016: £21m).

Disallowable expenses represent, in the main, the Group's share of incremental conduct charges that are not deductible in computing taxable profits.

The Conduct indemnity adjustment represents the receipt from/payment to the Group's former parent less refunds attributable in accordance with the indemnity agreement (note 3.14).

The rate at which deferred tax is recognised in respect of the defined benefit pension scheme has changed due to the closure of the Scheme. The surplus is accounted for as a potential refund to the employer, not a reduction in future contributions. In accordance with tax legislation this 'authorised surplus payment' is recognised as a deferred tax liability at 35%. There is an overall rate change in respect of the pension of £37m with £30m taken to the income statement and £7m to the statement of other comprehensive income.

2.6 Earnings per share (EPS)

Accounting policy

Basic earnings per share

Basic earnings per share is calculated by taking the profit attributable to ordinary shareholders of the parent company and dividing this by the weighted-average number of ordinary shares outstanding during the period.

Diluted earnings per share

This requires the weighted average number of ordinary shares in issue to be adjusted to assume conversion of all dilutive potential ordinary shares. These arise from awards made under equity based compensation schemes. Share awards with performance conditions attaching to them are not considered to be dilutive unless these conditions have been met at the reporting date.

The Group presents basic and diluted earnings/(loss) per share data in relation to the ordinary shares of CYBG PLC.

	2017 £m	2016 £m
Profit/(loss) attributable to ordinary shareholders	**146**	(206)
Tax relief on AT1 distribution attributable to ordinary equity holders	**7**	7
Tax relief on loss on repurchase of CYB Investments Limited (CYBI) AT1 issued to NAB	**–**	1
Profit/(loss) attributable to ordinary equity holders for the purposes of basic and diluted EPS	**153**	(198)

	2017 Number of shares (million)	2016 Number of shares (million)
Weighted-average number of ordinary shares in issue		
– Basic	**883**	880
– Diluted	**884**	880
Basic earnings/(loss) per share (pence)	**17.3**	(22.5)
Diluted earnings/(loss) per share (pence)(1)	**17.2**	(22.5)

(1) The comparative has been restated so that the dilutive effect of the potentially dilutive share based payment awards has been excluded from the calculation on the basis that it would have reduced the loss per share.

Section 3: Assets and liabilities

3.1 Cash and balances with central banks

	2017 £m	2016 £m
Cash assets	**1,507**	1,313
Balances with central banks (including EU payment systems)	**5,430**	4,642
	6,937	5,955
Less mandatory deposits with central banks[1]	**(44)**	(43)
Included in cash and cash equivalents (note 5.2)	**6,893**	5,912

(1) Mandatory deposits are not available for use in the Group's day to day business and are non-interest bearing.

3.2 Financial assets available for sale

Accounting policy

Available for sale financial assets are recognised on trade date and comprise listed and unlisted non-derivative financial assets not classified into any other financial asset category. They are initially recognised at fair value including direct and incremental transaction costs, and subsequently measured at fair value. Gains and losses arising from changes in fair value are included as a separate component of equity until sale or impairment, at which point the cumulative gain or loss is transferred to the income statement.

All available for sale financial assets are continually monitored for evidence of any impairment, which would typically be deemed to have arisen where there is evidence of a significant or prolonged reduction in the fair value of the security below its cost. Where such evidence of impairment exists, the cumulative net loss previously recognised directly in equity is transferred to the income statement.

In situations where evidence suggests a subsequent increase in value, reversals of impairment of previously impaired equity instruments are recognised directly in equity; reversals of impairment of debt instruments are recognised in the income statement.

Interest income, determined using the effective interest method, is recognised in the income statement. Impairment losses and translation differences on monetary items are recognised in the income statement within the year in which they arise.

	2017 £m	2016 £m
Listed securities	**2,066**	1,695
Unlisted securities	**4**	29
Other financial assets	**6**	7
	2,076	1,731

Refer to note 3.18 for further information on the valuation methodology applied to available for sale assets and their classification within the fair value hierarchy.

Credit quality of investments

	2017 £m	2016 £m
Available for sale		
Senior investment grade	**2,066**	1,695
Other	**10**	36
	2,076	1,731

Senior investment grade securities

These include £1,221m (2016: £1,286m) of UK Government Gilts. The remainder relates to highly liquid, AAA-rated corporate bonds.

Section 3: Assets and liabilities continued

3.3 Financial assets and liabilities at fair value through profit or loss

Accounting policy
Financial assets and liabilities are designated at fair value through profit or loss, with gains and losses recognised in the income statement as they arise (note 2.3), when this reduces an accounting mismatch or where the performance is evaluated on a fair value basis. In such cases, transaction costs are recognised immediately in the income statement upon initial recognition of the financial asset and liability.

The derivatives related to the assets and liabilities at fair value through profit or loss do not meet the requirements for hedge accounting and are accounted for as held for trading derivative financial instruments (note 3.4).

Critical accounting estimates and judgements
Where the fair values of financial assets and financial liabilities recorded on the balance sheet cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where such data is not available, judgement is required to establish fair values. The judgements include considerations of liquidity and model inputs.

The most significant judgement is in relation to the Group's fair value loan portfolio. The most significant input impacting the carrying value of the loans other than interest rates is the future expectation of credit losses. Sensitivity analysis indicating the impact of reasonably possible changes in this input on the fair value is provided in note 3.18.

	2017 £m	2016 £m
Financial assets at fair value through profit or loss		
Loans and advances	**477**	750
Financial liabilities at fair value through profit or loss		
Due to customers – term deposits	**26**	48

Loans and advances
Included in financial assets at fair value through profit or loss is a historical portfolio of loans (sales ceased in 2012). Interest rate risk associated with these loans is managed using interest rate derivative contracts and the loans are recorded at fair value to avoid an accounting mismatch. The maximum credit exposure of the loans is £477m (2016: £750m) including accrued interest receivable of £2m (2016: £4m). The cumulative loss in the fair value of the loans attributable to changes in credit risk amounts to £11m (2016: £24m) and the change for the current year is a decrease of £13m (2016: decrease of £14m), of which £6m (2016: £11m) has been recognised in the income statement.

The loans are classified as Level 3 in the fair value hierarchy (note 3.18).

Due to customers – term deposits
Included in other financial liabilities at fair value are fixed rate deposits, the interest rate risk on which is hedged using interest rate derivative contracts. The deposits are recorded at fair value to avoid an accounting mismatch.

The change in fair value attributable to changes in the Group's credit risk is £Nil (2016: £Nil). The Group is contractually obligated to pay £1m (2016: £3m) less than the carrying amount at maturity to the deposit holder.

The term deposits are classified as Level 3 in the fair value hierarchy (note 3.18).

3.4 Derivative financial instruments

Accounting policy

All derivative instruments manage exposures to interest rates and foreign currency and are recognised on the balance sheet at fair value on trade date. The carrying value of a derivative is measured at fair value throughout the life of the contract. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative. The notional amount of a derivative contract is not recorded on the balance sheet but disclosed as part of this note.

The method of recognising the resulting fair value gain or loss on a derivative depends on whether it is designated as a hedging instrument and, if so, the nature of the item being hedged. Certain derivatives are designated as either hedges of highly probable future cash flows attributable to a recognised asset or liability, or a highly probable forecast transaction (a cash flow hedge); or hedges of the fair value of recognised assets or liabilities or firm commitments (a fair value hedge).

Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in equity. Specifically, the separate component of equity (note 4.1) is adjusted to the lesser of the cumulative gain or loss on the hedging instrument, and the cumulative change in fair value of the expected future cash flows on the hedged item from the inception of the hedge. Any remaining gain or loss on the hedging instrument is recognised in the income statement. The carrying value of the hedged item is not adjusted. Amounts accumulated in equity are transferred to the income statement in the period in which the hedged item affects profit or loss.

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

Fair value hedge

The carrying value of the hedged item on initial designation is adjusted for the fair value attributable to the hedged risk. Subsequently, changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The movement in the fair value of the hedged item attributable to the hedged risk is made as an adjustment to the carrying value of the hedged asset or liability. Where the hedged item is derecognised from the balance sheet, the adjustment to the carrying amount of the asset or liability is immediately transferred to the income statement.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item is amortised to the income statement on an effective interest basis over the remaining life of the asset or liability.

Hedge effectiveness

The Group documents, at the inception of a transaction, the relationship between hedging instruments and the hedged items, and the Group's risk management objective and strategy for undertaking these hedge transactions. The documentation covers how effectiveness will be measured throughout the life of the hedge relationship and its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. A hedge is expected to be highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated are expected to offset in a range of 80% to 125%.

Derivatives held for trading

The Group uses derivatives for risk management purposes and does not have a trading book. However, derivatives that do not meet the hedging criteria within IAS 39, or for which hedge accounting is not applied, are classified as held for trading. Changes in value of held for trading derivatives are immediately recognised in the income statement (note 2.3).

Section 3: Assets and liabilities continued

3.4 Derivative financial instruments continued

The tables below analyse derivatives between those designated as hedging instruments and those classified as held for trading.

	2017 £m	2016 £m
Fair value of derivative financial assets		
Designated as hedging instruments	**202**	351
Designated as held for trading	**80**	234
	282	585
Fair value of derivative financial liabilities		
Designated as hedging instruments	**229**	257
Designated as held for trading	**147**	341
	376	598

Cash collateral on derivatives placed with banks totalled £338m (2016: £337m). Cash collateral received on derivatives totalled £31m (2016: £57m). These amounts are included within due from other banks and due to other banks respectively.

The derivative financial instruments held by the Group are further analysed below. The notional contract amount is the amount from which the cash flows are derived and is not an indication of the amounts at risk relating to these contracts.

Total derivative contracts as at 30 September 2017

	Notional contract amount £m	Fair value of assets £m	Fair value of liabilities £m
Derivatives designated as hedging instruments			
Cash flow hedges			
Interest rate swaps	**17,952**	**56**	**104**
Cross currency swaps	**527**	**89**	**–**
Forward foreign exchange	**6**	**–**	**–**
	18,485	**145**	**104**
Fair value hedges			
Interest rate swaps	**1,452**	**57**	**125**
Derivatives designated as held for trading			
Foreign exchange rate related contracts			
Spot and forward foreign exchange	**2,689**	**45**	**47**
Cross currency swaps	**150**	**9**	**9**
Options	**103**	**2**	**2**
	2,942	**56**	**58**
Interest rate related contracts			
Swaps	**983**	**18**	**82**
Swaptions	**33**	**–**	**–**
Options	**477**	**2**	**3**
	1,493	**20**	**85**
Commodity related contracts	**93**	**4**	**4**
Total derivative contracts	**24,465**	**282**	**376**

Total derivative contracts as at 30 September 2016

	Notional contract amount £m	Fair value of assets £m	Fair value of liabilities £m
Derivatives designated as hedging instruments			
Cash flow hedges			
Interest rate swaps	15,526	154	79
Cross currency swaps	760	88	–
Forward foreign exchange	5	–	–
	16,291	242	79
Fair value hedges			
Interest rate swaps	1,452	109	178
Derivatives designated as held for trading			
Foreign exchange rate related contracts			
Spot and forward foreign exchange	2,202	84	78
Cross currency swaps	150	11	11
Options	216	5	5
	2,568	100	94
Interest rate related contracts			
Swaps	1,512	123	233
Swaptions	47	–	1
Options	569	2	4
	2,128	125	238
Commodity related contracts	127	9	9
Total derivative contracts	22,566	585	598

Derivatives traded to manage the Group's interest rate exposure on a net portfolio basis are accounted for as cash flow hedges. Derivatives traded to manage interest rate risk on certain fixed rate assets, such as UK Government Gilts, are accounted for as fair value hedges. The Group also cash flow hedges its foreign currency exposure on material, highly probable non-GBP denominated transactions.

The Group hedging positions also include those designated as foreign currency and interest rate hedges of debt issued from the Group's securitisation and covered bond programmes respectively. As such, certain derivative financial assets and liabilities have been booked in structured entities and consolidated within these financial statements.

Cash flow hedged derivatives include vanilla interest rate swaps within macro hedges and cross currency swaps within a structured entity. The Group has notional commitments in the following periods:

Nominal values per time period	**2017 £m**	2016 £m
Within 0 to 3 months	**92**	1,452
Between 3 and 12 months	**2,986**	6,710
1 to 5 years	**14,817**	8,063
Greater than 5 years	**590**	66
	18,485	16,291

Section 3: Assets and liabilities continued

3.4 Derivative financial instruments continued

The Group has hedged forecast future cash flows, which vary primarily with interest or foreign exchange rates. These cash flows are expected to impact the income statement in the following periods:

	Forecast receivable cash flows 2017 £m	**Forecast payable cash flows 2017 £m**	Forecast receivable cash flows 2016 £m	Forecast payable cash flows 2016 £m
Within 1 year	**52**	**399**	29	261
Between 1 and 2 years	**70**	**86**	16	368
Between 2 and 3 years	**70**	**86**	15	59
Between 3 and 4 years	**44**	**122**	14	77
Between 4 and 5 years	**19**	**6**	8	112
Greater than 5 years	**26**	**18**	–	6
	281	**717**	82	883

	2017 £m	2016 £m
Gain/(loss) arising from fair value hedges (note 2.3)		
Hedging instrument	**1**	15
Hedged item attributable to the hedged risk	**(5)**	(15)
	(4)	–

	2017 £m	2016 £m
Loss from cash flow hedges due to hedge ineffectiveness (note 2.3)	**–**	(1)

3.5 Loans and advances to customers

Accounting policy

Loans and advances to customers arise when the Group provides money directly to a customer and include overdrafts, credit card lending, lease finance, mortgages, invoice financing and term lending.

Loans and advances to customers are initially recognised at fair value including direct and incremental transaction costs. They are subsequently measured at amortised cost, using the effective interest method, adjusted for impairment losses. They are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership.

Leases entered into by the Group as lessor, where the Group transfers substantially all the risks and rewards of ownership to the lessee, are classified as finance leases. The leased asset is not held on the Group balance sheet; instead, a finance lease is recognised representing the minimum lease payments receivable under the terms of the lease, discounted at the rate of interest implicit in the lease. Interest income is recognised in interest receivable, allocated to accounting periods to reflect a constant periodic rate of return.

	2017 £m	2016 £m
Overdrafts	**1,524**	1,536
Credit cards	**396**	400
Lease finance	**594**	515
Mortgages	**23,480**	21,836
Other term lending – SME	**4,762**	4,393
Other term lending – Retail	**709**	690
Trade finance	**23**	26
Gross loans and advances to customers	**31,488**	29,396
Accrued interest receivable	**75**	76
Unearned income	**(28)**	(26)
Deferred and unamortised fee income	**(32)**	(29)
Impairment provisions on credit exposures (note 3.6)	**(210)**	(215)
	31,293	29,202

The Group has transferred a proportion of mortgages to the securitisation and covered bond programmes (note 3.7).

The Group also has a portfolio of fair valued business loans of £477m (2016: £750m) which are held separately as Other financial assets at fair value on the balance sheet (note 3.3). Combined with the above this is equivalent to total loans and advances of £31,770m (2016: £29,952m).

Lease finance

The Group leases a variety of assets to third parties under finance lease arrangements, including vehicles and general plant and machinery. The cost of assets acquired by the Group during the year for the purpose of letting under finance leases and hire purchase contracts amounted to £13m (2016: £5m) and £408m (2016: £381m) respectively. The total receivables from finance leases and hire purchase contracts were £17m (2016: £8m) and £550m (2016: £482m) respectively.

Finance lease and hire purchase receivables

	2017 £m	2016 £m
Gross investment in finance lease and hire purchase receivables		
Due within 1 year	**241**	224
Due within 1 to 5 years	**346**	288
Due after more than 5 years	**7**	3
	594	515
Unearned income	**(27)**	(25)
Net investment in finance lease and hire purchase receivables	**567**	490

Section 3: Assets and liabilities continued

3.6 Impairment provisions on credit exposures

Accounting policy

Assets carried at amortised cost

At each reporting date the Group assesses if there is objective evidence of impairment on a financial asset or group of financial assets due to one or more loss events that occurred after initial recognition but prior to the balance sheet date. Examples of loss events are (i) where there has been an actual breach of contract by the borrower such as a default or delinquency in payment of interest or principal; or (ii) the granting of a concession to the borrower that the Group would not otherwise consider.

The Group first assesses whether objective evidence of impairment exists either individually for assets that are separately significant; or collectively for assets that are not separately significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and collectively assessed for impairment ('collective provisions').

Collective provisions

Collective provisions are generally established for homogenous portfolios such as the Retail portfolios and the small business portfolio within the SME franchise.

Within the Group's Retail environment, past loss experience is a key factor in determining an appropriate collective provision level and takes into account a number of different elements including:

– the number of days past due;
– the realisable value of any security held; and
– the timing of any such security sale.

These and other factors will influence the probability that the customer defaults on the loan (the PD). In the event of a default occurrence, the Retail collective provision calculator provides the amount the Group expects to be irrecoverable from that customer (the LGD). The level and impact of LGD varies significantly between the Group's secured and unsecured lending portfolios.

Collective provisioning for the Group's SME portfolio is also based on the use of PD and LGD. The assets are included in a group of financial assets with similar risk characteristics and collectively assessed for impairment. The modelled collective assessment considers factors such as:

– credit quality;
– levels of arrears;
– credit utilisation;
– loan to collateral ratios; and
– other factors including the Group's internal customer rating system (eCRS).

These characteristics are relevant to the estimation of future cash flows for groups of such assets as they are indicative of the borrower's ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Reliance is placed on the eCRS rating when assessing PD as these are directly mapped within the model. Manual interventions to the eCRS rating, such as the placement on a watch list, will directly lead to an increase in PD and consequently the level of collective provision required. LGD assumptions are driven by the level of security assigned to the customer within the collective provisioning model. These are regularly monitored to ensure comparability with recent actual loss experience.

In addition, for both the Group's Retail and SME portfolios, experienced judgement is used to estimate the amount of an impairment loss. This reflects a limited number of refinements that have been assessed as necessary to reflect specific and evolving circumstances that, by their nature, cannot be adequately captured in the models. The use of judgements and supportable estimates is considered by management to be an essential part of the credit impairment process. The methodology and assumptions used for estimating future cash flows are reviewed regularly to identify and reduce any significant differences between loss estimates and actual loss experience.

Specific provision

If there is objective evidence that an impairment loss has been incurred on a loan, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (including the estimated realisable value of any security) discounted at the asset's original effective interest rate (a 'specific provision').

Specific provision allowances are primarily established against the Group's commercial business within the SME franchise. Assets are reviewed on a regular basis and those showing potential or actual vulnerability are placed onto a watch list where enhanced monitoring is undertaken.

Impairment
When first recognised, the impairment allowance, which is a combination of both the collective and specific provision, is recognised in the income statement.

Following impairment, interest income is recognised using the original effective rate of interest which was used to discount the future cash flows for the purpose of measuring the impairment loss. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. The amount of the reversal is recognised in the income statement.

When a loan is uncollectible, and all necessary internal procedures have been completed, it is written off against the related impairment loss. Subsequent recoveries of amounts previously written off reduce the expense in the income statement.

The Group's impairment policy for available for sale financial assets is included in note 3.2

Critical accounting estimates and judgements
In determining the required level of collective impairment provisions, the Group uses the output from various statistical models, with management judgement required to assess the modelled outputs and, where necessary, make appropriate adjustments.

The key assumptions within the Group's collective provisioning models which give rise to significant estimation uncertainty are the PD and the LGD. Both measures are predicated on expectations of customer behaviour and performance, which requires management to form a judgement based on a wide range of historic and current evidence. The actual amount of the future cash flows and their timing may differ significantly from the assumptions made for the purposes of determining the impairment allowances and consequently these allowances can be subject to variation as time progresses and the circumstances of the customer become clearer.

From an SME perspective, changes made to eCRS will have a direct impact as these are mapped to PDs. Assumption changes on retail customer behaviour will also have an impact on the PDs used.

Within the Retail portfolio, the Group's collective provision is reflective of the fact that the majority of lending is concentrated on customer mortgages, where the available security is generally sufficient to cover the exposure. This differs from the SME portfolio where the availability and strength of the security will have less of an impact on overall recoveries, leading to a potentially higher collective provision charge relative to the overall exposure.

Sensitivities within the collective provision
There are interactions between the various assumptions within the provisioning models which mean that no single factor is likely to move independent of others; however, the sensitivities disclosed below assume all other assumptions remain unchanged.

If the PDs were to move by +/- 5% from those presently used within the Group's provisioning models, the impairment provision would increase/decrease accordingly by £5m.

An important element to the PD is the loss emergence period (LEP) which represents the Group's assessment of the period from when a loss event occurs to eventual default. The impact of the LEP differs between the Group's Retail and SME portfolios. A two-month increase in the LEP would result in a further £2m impairment provision within the SME portfolio; and a further £1m being added to the Retail impairment provision.

To the extent that recovery rates improve from those presently used within each of the Group's provisioning models by 5%, the impairment provision on loans and advances would decrease by £14m. Alternatively, if recovery rates deteriorate by 5%, the impairment provision on loans and advances would increase by £24m.

Provision in the SME portfolio is sensitive not only to default rates and severity of losses, but also to the assessment of risk and security. If 10% of the SME portfolio were to fall by one notch, the impairment provision would increase by £2m.

In addition to modelled outputs, the impairment provision is further impacted by management judgements. These include judgements that reflect elements which are not sufficiently sensitive to the current economic conditions, model risk reserves that are held to cover against a range of potential model limitations, and judgements made in respect of potential recoveries for specific provisions which also involve customer and economic specific conditions. These management judgements do not allow for any meaningful sensitivity comparison.

Section 3: Assets and liabilities continued

3.6 Impairment provisions on credit exposures continued

	2017 £m	2016 £m
Opening balance	**215**	230
Charge for the year	**48**	39
Amounts written off	**(75)**	(68)
Recoveries of amounts written off in previous years	**18**	18
Other[1]	**4**	(4)
Closing balance	**210**	215
Specific	**56**	64
Collective	**154**	151
	210	215

(1) Other includes the unwind of net present value elements of specific provisions and other minor movements.

3.7 Securitisation and covered bond programmes

Accounting policy

The Group sponsors the formation of structured entities, primarily for the purpose of facilitation of asset securitisation and covered bond transactions to accomplish certain narrow and well-defined objectives. Although the Group has no shareholding in these entities, where it is exposed, or has rights, to variable returns from its involvement with the entities and it has the ability to affect those returns through its power over the entity, they are regarded as controlled entities as described in note 1.5 and are consolidated in the Group's financial statements.

Securitisation

The Group has securitised a proportion of its retail mortgage loan portfolio under the Group's master trust securitisation programmes. The securitised mortgage loans have been assigned at principal value to bankruptcy remote structured entities. These structured entities have been funded through the issue of residential mortgage backed debt to third-party institutional debt investors. The Group is entitled to any residual income from the vehicles after the debt obligations and senior expenses of the programmes have been met. The securitised debt holders have no recourse to the Group other than the principal and interest (including fees) generated from the securitised mortgage loan portfolio. The Group continues servicing these mortgage loans in return for an administration fee.

The mortgage loans do not qualify for derecognition because the Group remains exposed to the majority of the risks and rewards of the mortgage loan portfolio, principally the associated credit risk. The securitisation structured entities are consolidated and the securitised mortgage loans retained on the Group's balance sheet. A liability is recognised for the proceeds of the funding transaction. The externally held securitised notes in issue are included within debt securities in issue (note 3.15). There are a number of notes held internally by the Group, not recognised on the balance sheet, which are used as collateral for repurchases and similar transactions or for credit enhancement purposes.

Covered bond

A subset of the Group's retail mortgage loan portfolio has been ring fenced and assigned to a bankruptcy remote limited liability partnership, Clydesdale Covered Bond 2 LLP, associated with the covered bond programme, to provide a guarantee for the obligations payable on the covered bonds issued by the Group. Similar to the securitisation programmes, the Group is entitled to any residual income after all payment obligations due under the terms of the covered bonds and senior programme expenses have been met. The Group continues servicing these mortgage loans in return for an administration fee.

The mortgage loans do not qualify for derecognition because the Group retains all of the risks and rewards of the mortgage loan portfolio. The covered bond partnership is consolidated with the mortgage loans retained on the consolidated balance sheet and the covered bonds issued included within debt securities in issue. The covered bond holders have dual recourse: firstly, to Clydesdale Bank PLC on an unsecured basis; and secondly, to the LLP under the Covered Bond Guarantee secured against the mortgage loans.

Significant restrictions

Where the Group uses its financial assets to raise finance through securitisations and the sale of securities subject to repurchase agreements, this leads to the assets becoming encumbered. Once encumbered, the assets are not available for transfer around the Group.

The assets and liabilities in relation to securitisation and covered bonds in issue at 30 September are as follows:

2017

Liabilities	**Securitisation £m**	**Covered bonds £m**	**Total £m**
At 1 October 2016	**3,208**	**797**	**4,005**
Issuance of debt	**750**	**–**	**750**
Repayments	**(740)**	**–**	**(740)**
Other movements	**24**	**(49)**	**(25)**
At 30 September 2017	**3,242**	**748**	**3,990**
Assets			
Securitised mortgage loans	**6,182**	**1,344**	**7,526**

2016

Liabilities	Securitisation £m	Covered bonds £m	Total £m
At 1 October 2015	3,031	721	3,752
Issuance of debt	750	–	750
Reclassification of notes previously held internally	380	–	380
Repayments	(1,029)	–	(1,029)
Other movements	76	76	152
At 30 September 2016	3,208	797	4,005
Assets			
Securitised mortgage loans	5,435	1,149	6,584

Other movements consist of exchange rate movements on currency denominated bonds and fair value hedge accounting adjustments.

The following table sets out the net position of the fair value of financial assets relating to the securitisation programmes where the counterparty to the associated liabilities has recourse only to the financial assets:

	2017 £m	2016 £m
Fair value of transferred assets	**6,074**	5,417
Fair value of associated liabilities	**3,262**	3,233
	2,812	2,184

There were no events during the year that resulted in any Group transferred financial assets being derecognised.

The Group has contractual and non-contractual arrangements which may require it to provide financial support as follows:

Securitisation programmes

The Group provides credit support to the structured entities via reserve funds, which are partly funded through subordinated debt arrangements and by holding junior notes. Exposures totalled £47m in subordinated debt (2016: £20m) and £856m in junior notes held (2016: £610m). The Group has a beneficial interest in the securitised mortgage portfolio held by the structured entities of £711m (2016: £977m).

Furthermore, the Group has an obligation to repurchase mortgage exposures if certain mortgage loans no longer meet the programme criteria.

Looking forward through future reporting periods there are a number of date based options on the notes issued by the structured entities which could be actioned by them as issuer. These could require the Group, as sponsor, to provide additional liquidity support.

Covered bond programme

The nominal level of over-collateralisation was £681m (2016: £599m) of the outstanding covered bonds. From time to time the obligations of the Group to provide over-collateralisation may increase due to the formal requirements of the programme.

Furthermore, the Group has an obligation to repurchase mortgage exposures if certain mortgage loans no longer meet the programme criteria.

Section 3: Assets and liabilities continued

3.8 Property, plant and equipment

Accounting policy

The Group's freehold and long-term leasehold land and buildings are carried at their fair value as determined by the Directors, taking account of advice received from independent valuers. Fair values are determined in accordance with guidance published by the Royal Institution of Chartered Surveyors, including adjustments to observable market inputs reflecting any specific characteristics of the land and buildings. Directors' valuations are performed annually in July, with the independent valuations carried out on a three-year cycle on an open market basis. The valuations are classified in Level 3 of the fair value hierarchy as defined in note 3.18.

All other items of property, plant and equipment are carried at cost, less accumulated depreciation and impairment losses. Cost includes expenditure that is directly attributable to acquisition of the asset. Impairment is assessed whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

With the exception of freehold land, all items of property, plant and equipment are depreciated or amortised using the straight line method, at rates appropriate to their estimated useful life to the Group. The annual rates of depreciation or amortisation are:

Buildings	50 years
Leases (leasehold improvements)	the lower of the expected lease term or the asset's remaining useful life
Fixtures and equipment	3–10 years

Residual values and useful lives of assets are reviewed at each reporting date. Depreciation is recognised within depreciation expense in the income statement.

	Freehold land and buildings £m	Long-term leasehold land and buildings £m	Building improvements £m	Fixtures and equipment £m	Total £m
Cost or valuation					
At 1 October 2015	10	3	171	105	289
Additions	–	–	15	7	22
Disposals	(4)	–	(32)	(12)	(48)
At 30 September 2016	6	3	154	100	263
Additions	–	–	14	7	21
Disposals	(1)	–	(25)	(5)	(31)
At 30 September 2017	**5**	**3**	**143**	**102**	**253**
Accumulated depreciation					
At 1 October 2015	1	–	105	74	180
Charge for the year	–	–	15	10	25
Disposals	–	–	(30)	(11)	(41)
At 30 September 2016	1	–	90	73	164
Charge for the year (note 2.4)	–	–	14	8	22
Disposals	–	–	(16)	(3)	(19)
At 30 September 2017	**1**	**–**	**88**	**78**	**167**
Net book value					
At 30 September 2017	**4**	**3**	**55**	**24**	**86**
At 30 September 2016	5	3	64	27	99

Valuations

A comparison of the carrying value between the revaluation basis and the historical cost basis, for freehold and long-term leasehold land and buildings, is shown below:

	2017 £m	2016 £m
Carrying value as included under the revaluation basis	**7**	8
Carrying value if the historical cost basis had been used	**6**	7

3.9 Investment properties

Accounting policy

Investment properties are measured at fair value and are revalued annually by the Directors. The valuations are based upon advice received from independent valuers and performed on an open market basis. Adjustments are made to observable market data for comparable properties for specific characteristics such as the nature, location or condition of the asset. Fair value movements are recognised in the income statement in the period in which they arise.

Investment properties are classified in Level 3 of the fair value hierarchy as defined in note 3.18.

	2017 £m	2016 £m
At 1 October	**22**	32
Disposals	**(7)**	(10)
Revaluation	**(1)**	–
At 30 September	**14**	22

During the year 86% (2016: 97%) of the investment properties generated total rental income of £1m (2016: £1m) and incurred operating and administrative expenses of £1m (2016: £1m). The operating and administrative expenses of the investment properties that did not generate rental income were £Nil (2016: £Nil).

Section 3: Assets and liabilities continued

3.10 Intangible assets

Accounting policy
Capitalised software costs are stated at cost, less amortisation and any provision for impairment.

Identifiable and directly associated external and internal costs of acquiring and developing software are capitalised where the software is controlled by the Group, and where it is probable that future economic benefits that exceed its cost will flow from its use over more than one year. Costs associated with maintaining software are recognised as an expense as incurred. Capitalised computer software costs are amortised on a straight line basis over their expected useful lives, usually between three and 10 years. Impairment losses are recognised in the income statement as incurred.

Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable, which typically arises when the benefits associated with the software were substantially reduced from what had originally been anticipated or the asset has been superseded by a subsequent investment. In such situations, an impairment loss is recognised for the amount by which the carrying amount of an asset exceeds its recoverable amount. The recoverable amount of an asset is the higher of its fair value less costs of disposal or its value in use.

Intangible assets which are fully amortised are reviewed annually to consider whether the assets remain in use.

Capitalised software costs	2017 £m	2016 £m
Cost		
At 1 October	**463**	427
Additions	**148**	99
Write-off	**(22)**	(63)
At 30 September	**589**	463
Accumulated amortisation		
At 1 October	**207**	162
Charge for the year (note 2.4)	**65**	63
Write-off	**(22)**	(63)
Impairment (note 2.4)	**–**	45
At 30 September	**250**	207
Net book value at 30 September	**339**	256

£3m (2016: £13m) of the £148m (2016: £99m) software additions do not form part of internally generated software projects.

3.11 Deferred tax

Accounting policy

Deferred tax assets and liabilities are recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. A deferred tax asset is recognised for unused tax losses and unused tax credits only if it is probable that future taxable amounts will arise against which those temporary differences and losses may be utilised.

Critical accounting estimates and judgements

The Group has deferred tax assets of £154m (2016: £183m); the reduction from the previous balance sheet date is due to the movement in the defined benefit pension scheme to a surplus and the utilisation of the capital allowance deferred tax asset. The Group has assessed the recoverability of these deferred tax assets at 30 September 2017 and considers it probable that sufficient future taxable profits will be available against which the underlying deductible temporary differences can be utilised over the corporate planning horizon.

At 30 September 2017, the Group had an unrecognised deferred tax asset of £180m (2016: £202m) representing trading losses with a gross value of £1,058m (2016: £1,186m). Although there is no prescribed period after which losses expire, a deferred tax asset has not been recognised in respect of these losses as the Directors have insufficient certainty over their recoverability in the foreseeable future.

Movement in net deferred tax asset

	2017 £m	2016 £m
At 1 October	**156**	379
Recognised in the income statement (note 2.5)	**(69)**	(232)
Recognised directly in equity	**(8)**	9
At 30 September	**79**	156

The Group has recognised deferred tax in relation to the following items:

	2017 £m	2016 £m
Deferred tax assets		
Tax losses carried forward	**28**	35
Capital allowances	**120**	127
Cash flow hedge reserve	**1**	1
Transitional adjustment – available for sale reserve	**3**	–
Employee equity based compensation	**2**	2
Defined benefit pension scheme deficit	**–**	18
	154	183
Deferred tax liabilities		
Defined benefit pension scheme surplus	**(72)**	–
Cash flow hedge reserve	**–**	(21)
Gains on unlisted available for sale investments	**(3)**	(6)
	(75)	(27)
Net deferred tax asset	**79**	156

The statutory rate of UK corporation tax is 19% from 1 April 2017 and as enacted in Finance Act 2016 will fall to 17% from 1 April 2020. In accordance with IAS 12, these rates are taken into account in assessing the value at which assets are expected to be realised and liabilities settled.

Finance Bill (No. 2) 2017 contains draft legislation in respect of the Corporate Tax Loss Restriction and the Corporate Interest Restriction which was due to apply from 1 April 2017. As the legislation was not substantively enacted at the balance sheet date it has not been applied in the calculation of the tax position at 30 September 2017. Management expects that given the Group's particular asset profile in respect of losses, application of the new rules would have resulted in an immaterial increase in the deferred tax asset recognised on the balance sheet. This is expected given that the new rules are designed to accelerate the payment of corporation tax.

The rate at which deferred tax is recognised in respect of the defined benefit pension scheme has changed due to the closure of the Scheme to the majority of members (note 3.16). The surplus is accounted for as a potential refund to the employer, rather than a reduction in future contributions. In accordance with tax legislation this 'authorised surplus payment' is recognised as a deferred tax liability at 35%. There is an overall rate change in respect of the pension of £37m with £30m charged in the income statement and £7m charged directly to equity.

Section 3: Assets and liabilities continued

3.12 Due to other banks

Accounting policy

Repurchase agreements

Securities sold subject to repurchase agreements ('repos') are retained in their respective balance sheet categories. The associated liabilities are included in amounts due to other banks based upon the counterparties to the transactions.

The difference between the sale and repurchase price of repos is treated as interest and accrued over the life of the agreements using the effective interest method.

	2017 £m	2016 £m
Securities sold under agreements to repurchase	**1,864**	1,226
Transaction balances with other banks	**21**	23
Deposits from other banks	**31**	60
Secured loans	**1,901**	–
	3,817	1,309

The underlying securities sold under agreements to repurchase have a carrying value of £2,660m (2016: £1,657m).

Secured loans comprise amounts drawn under the TFS.

3.13 Due to customers

	2017 £m	2016 £m
Non-interest bearing demand deposits	**2,548**	2,160
Interest bearing demand deposits	**19,130**	19,328
Term deposits	**5,957**	5,454
Other wholesale deposits	**18**	12
	27,653	26,954
Accrued interest payable	**65**	136
	27,718	27,090

3.14 Provision for liabilities and charges

Accounting policy

Provisions for liabilities and charges are recognised when a legal or constructive obligation exists as a result of past events, it is probable that an outflow of economic benefits will be necessary to settle the obligation, and the obligation can be reliably estimated. Provisions for liabilities and charges are not discounted to the present value of their expected net future cash flows except where the time value of money is considered material.

Critical accounting estimates and judgements

PPI redress provision and other conduct related matters

Management has exercised significant judgement around the key assumptions that underpin the estimates and used estimation techniques to quantify them. Ongoing regulatory review and input, as well as rulings from the Financial Ombudsman Service over time, and the Group's internal reviews and assessments of customer complaints, will continue to impact upon the nature and extent of conduct related customer redress and associated costs for which the Group may ultimately become liable in future periods.

Significant judgement is required in determining the key assumptions used to estimate the quantum of the provision, including the level of future complaint volumes, uphold rates (how many claims are, or may be, upheld in the customer's favour), and redress costs (the average payment made to customers). Also factored into the estimate is the effect of the judgements required around the outcome of the remediation activity. The provision is therefore subject to inherent uncertainties as a result of the subjective nature of the assumptions used in quantifying the overall estimated position at 30 September 2017, consequently, the provision calculated may be subject to change in future years if outcomes differ to those currently assumed. Sensitivity analysis indicating the impact of reasonably possible changes in key assumptions on the PPI provision is presented within this note.

There are similar uncertainties and judgements for other conduct risk related matters, however the level of liability is materially lower.

	2017 £m	2016 £m
PPI redress provision		
Opening balance	**725**	774
Charge to the income statement (note 2.4)	**48**	44
Charge reimbursed/reimbursable under Conduct Indemnity	**446**	406
Utilised	**(797)**	(499)
Closing balance	**422**	725
Customer redress and other provisions		
Opening balance	**101**	214
Charge to the income statement (note 2.4)	**10**	8
Charge reimbursed/reimbursable under Conduct Indemnity	**88**	27
Utilised	**(90)**	(148)
Closing balance	**109**	101
Restructuring provision(1)		
Opening balance	**26**	18
Charge to the income statement	**58**	39
Utilised	**(61)**	(31)
Closing balance	**23**	26
Total provisions for liabilities and charges	**554**	852

(1) Restructuring provision includes surplus lease space provision.

Section 3: Assets and liabilities continued

3.14 Provision for liabilities and charges continued

PPI redress

In common with the wider UK retail banking sector, the Group continues to deal with complaints and redress issues arising out of historic sales of PPI. During the year, the Group reassessed the level of provision that was considered appropriate to meet current and future expectations in relation to the mis-selling of PPI policies and concluded that a further charge of £494m was required incorporating the Group's estimate of the impact of PS17/3 issued on 2 March 2017 relating to a proposed time bar for complaints in August 2019. It also incorporated a reassessment of the costs of processing cases and the impact of experience adjustments. Only 9.7% of the charge impacts the Group's income statement (£48m) as a result of the Capped Indemnity. The total provision raised to date in respect of PPI is £2,140m (2016: £1,646m), with £422m of this remaining (2016: £725m) comprising £201m for customer initiated complaints and proactive customer contact (2016: £299m); £80m for the remediation of complaints closed prior to August 2014 (2016: £257m); and £142m for costs of administering the redress programme (2016: £169m).

To 30 September 2017, the Group has received 361,000 complaints (2016: 282,000) and has allowed for 73,000 further walk in complaints. This reflects an expectation that the volume of walk in complaints will reduce compared to most recent experience as the time bar approaches. Future complaint volumes could differ from the Group's assumption, which could result in a further provision being required.

The Group implemented a comprehensive new PPI complaint handling process from August 2014 which involved making a number of significant changes to the PPI operations which resulted in an increase in operational and administrative costs. As reported previously, the Group is in the process of re-opening approximately 180,000 complaints and reviewing the original decision reached in light of the new PPI complaint handling processes. As at 30 September 2017, this exercise is approximately 83% complete.

In addition to the remediation activity described above, the Group has completed a past business review (PBR) of certain PPI sales, to determine if there was actual or potential customer detriment in the sales process leading to a risk of mis-sale and the potential for proactive redress. The review indicated a more favourable outcome than allowed for in the assumptions underpinning the provision as at 30 September 2016.

The increase in provision has taken into account all of the above factors as well as a revision in the Group's expectation of new customer initiated complaints in light of current experience with the overall provision based on a number of assumptions derived from a combination of past experience, estimated future experience, industry comparison and the exercise of judgement in the key areas identified. There remain risks and uncertainties in relation to these assumptions and consequently in relation to the ultimate costs of redress and related costs, including: (i) the number of PPI claims (and the extent to which this is influenced by the activity of claims management companies, the application of a time bar, Plevin, and FCA advertising); (ii) the number of those claims that ultimately will be upheld; (iii) the amount that will be paid in respect of those claims; (iv) any additional amounts that may need to be paid in respect to previously handled claims; (v) the response rates to the proactive customer contact; and (vi) the costs of administering the remediation programme.

As such, the factors discussed above mean there is a risk that existing provisions for PPI customer redress may not cover all potential costs. In light of this, the eventual costs of PPI redress and complaint handling may therefore differ materially from that estimated and further provision could be required.

The table below sets out the key assumptions and the effect on the provision at 30 September 2017 of future, potential, changes in key assumptions:

Assumptions

	Change in assumption	Sensitivity[(1)]
Number of expected future customer initiated complaints (73,000 cases)	+/-10%	£22m
Uphold rates:		
Future complaints	+/-1%	£3m
Pre August 2014 complaints review	+/-1%	£1m
Average redress costs[(2)]	+/-1%	£2m

(1) There are inter-dependencies between several of the key assumptions which add to the complexity of the judgements the Group has to make. This means that no single factor is likely to move independently of others, however, the sensitivities disclosed above assume all other assumptions remain unchanged. The sensitivities disclosed do not incorporate the impact, if any, on the administrative cost element of the provision.

(2) Sensitivity to a change in average redress across customer initiated complaints, pre August 2014 complaints review and PBR customer populations.

The number of complaints received is monitored against past experience and future expectations and the Group will continue to reassess the adequacy of the provision for this matter and the assumptions underlying the provision calculation based upon experience and other relevant factors as matters develop.

Customer redress and other provisions

In addition to PPI redress set out above, provision for customer redress is held in those instances where the Group expects to make payments to customers whether on an ex-gratia or compensatory basis. Provisions can arise as a result of legal or regulatory action and can incorporate the costs of skilled persons, independent reviewers, and where appropriate other elements of administration.

The Group has reassessed the level of provision considered necessary in light of the current and future expected claims for all of these matters and concluded that no additional provisions are required to cover the expected tail of new complaints received at this stage.

Other provisions also include amounts in respect of a number of other non-PPI conduct related matters, legal proceedings, and claims arising in the ordinary course of the Group's business. Over the course of the year, the Group has raised further provisions of £98m for these matters, but only 9.7% of the charge impacts the Group's income statement (£10m) as a result of the Capped Indemnity. The ultimate cost to the Group of other customer redress matters is driven by a number of factors relating to offers of redress, compensation, offers of alternative products, consequential loss claims and administrative costs. The matters are at varying stages of their life cycle and in certain circumstances, usually early in the life of a potential issue, elements of the potential exposure are contingent. These factors could result in the total cost of review and redress varying materially from the Group's estimate. The final amount required to settle the Group's potential liabilities in these matters is therefore uncertain and further provision could be required. During the year £Nil (30 September 2016: £1m) was also recognised for provisions not related to customer redress/conduct risk.

Conduct Indemnity Deed

The Group's economic exposure to the impact of historic conduct related liabilities is mitigated by a Capped Indemnity from NAB. The Company and NAB have an agreement under which NAB has provided the Company with a Capped Indemnity to meet the costs of dealing with conduct matters related to products sold in the period prior to the date of the Group's demerger from NAB (the Conduct Indemnity Deed). The legacy conduct matters covered by the Capped Indemnity are referred to as Relevant Conduct Matters. The Capped Indemnity provides the Group with economic protection against certain costs and liabilities (including financial penalties imposed by a regulator) resulting from conduct issues relating to:

a) PPI, standalone interest rate hedging products, voluntary scope tailored business loans and fixed rate tailored business loans; and

b) other conduct matters, subject to certain limitations and minimum financial thresholds.

Amounts payable under the Capped Indemnity include, subject to certain limitations, payments to customers to satisfy, settle or discharge a Relevant Conduct Matter and the direct costs and expenses of satisfying, settling, discharging or administering such Relevant Conduct Matter.

It has been agreed that NAB will meet 90.3% of Qualifying Conduct Costs claimed by the Company, up to the amount of the Capped Indemnity.

Claims under the Capped Indemnity are recognised in the consolidated income statement simultaneously with the charge for Relevant Conduct Matters. The conduct expense and associated reimbursement income are presented net within Other operating and administrative expenses. A reimbursement receivable is recognised on the consolidated balance sheet within Due from other banks; this receivable is periodically settled by NAB. The reimbursement receivable is not offset against the provision amount on the Group's consolidated balance sheet. The provision expense and reimbursement income are disclosed above.

No reimbursement income or receivable is recognised on the consolidated balance sheet in relation to contingent liabilities for Relevant Conduct Matters. Any possible future reimbursement income linked to contingent liabilities in respect of Relevant Conduct Matters is not disclosed as a contingent asset as the amounts cannot be reliably estimated and are not virtually certain to be received.

To the extent that it is no longer probable that provisions for a Relevant Conduct Matter previously raised will be required to settle conduct obligations and a provision for a Relevant Conduct Matter is released as unutilised, the related Capped Indemnity amounts received will become repayable to NAB.

Should the Qualifying Conduct costs exceed the Capped Indemnity, any excess cost will be borne by the Group.

To the extent that tax relief is expected in relation to provisions for which reimbursement income is applicable, amounts may become repayable to NAB. In the consolidated financial statements, deferred tax assets are only recognised in respect of the loss share proportion (9.7%) of unused tax losses on Relevant Conduct Matters, on the basis that the Group does not obtain the economic benefit of the future tax relief which is repayable to NAB.

Section 3: Assets and liabilities continued

3.14 Provision for liabilities and charges continued

The utilisation and undrawn balance of the Capped Indemnity is set out below:

	Conduct protection £m
Conduct protection provided by NAB	1,700
Capital injected into CYBI prior to demerger[1]	(120)
Drawn in the period to 30 September 2016[2]	(898)
Undrawn Conduct Indemnity as at 30 September 2016	682
Drawn in the year to 30 September 2017	(171)
Amount to be drawn relating to the year to 30 September 2017	(363)
Undrawn balance as at 30 September 2017	**148**

(1) £120m of the £670m of capital injected in CYBI on 24 September 2015 related to the Conduct Indemnity Deed.
(2) £465m of the £898m represents the pre-covered provision amount.

Duration and termination

The indemnity protection provided by NAB to the Company in respect of Relevant Conduct Matters under the Capped Indemnity is perpetual in nature, except in the following circumstances:

(a) it is fully utilised by the Group; or

(b) in the event that, at any time:

(i) the PRA determines that NAB's remaining exposure under the Capped Indemnity; or

(ii) the Unutilised Indemnity Amount,

is £100m or less, NAB will have the right (with the approval of the PRA (at its sole discretion)) to terminate the Capped Indemnity by subscribing for shares (at a price equivalent to the prevailing five-day average market price for the shares) in an amount equal to the Unutilised Indemnity Amount, provided that the maximum value of the shares to be subscribed for does not exceed a value equal to 9.9% of the issued share capital of the Group (on an undiluted basis) at such time (a '£100m Termination').

(c) NAB and the Group may also agree arrangements to terminate or replace the Capped Indemnity with the consent of the PRA. In particular, NAB and the Group have agreed that they will, on the fifth anniversary of the demerger (and, if relevant, each subsequent anniversary of the demerger), seek to agree arrangements to terminate the Capped Indemnity. If any such arrangements are agreed between NAB and the Group, they will be required to obtain the approval of the PRA (at its sole discretion) before commencing the implementation of such arrangements. In relation to proposals made by NAB to the Group in connection with such termination of the Capped Indemnity, the Group cannot unreasonably withhold its agreement to the Capped Indemnity being replaced by a payment equal to the Unutilised Indemnity Amount to be applied (in whole or in part) in subscribing for shares (at a price equivalent to the prevailing five-day average market price for the shares), provided that the maximum value of the shares to be subscribed for pursuant to such proposal would not exceed £200m or if lower, a value equal to 9.9% of the issued share capital of the Group (on an undiluted basis) at such time (a 'Post-5 Year Equity Subscription Termination').

If £100m Termination or Post-5 Year Equity Subscription Termination occurs, the Group will not be entitled to make any further claims under the Capped Indemnity, but will be entitled to retain in a designated account for a period of three years following such termination, any Unutilised Covered Amount and any amount to be withdrawn from a designated account in respect of conduct costs that fall within the scope of the Capped Indemnity which have been incurred and paid by the Group prior to such termination. The Company will be required to return to NAB any other amounts in a designated account and to release to NAB all amounts remaining in the collateral account. Following the expiry of such three-year period, the Group will be required to repay all remaining amounts in a designated account net of any amount to be withdrawn from a designated account in respect of conduct costs that fall within the scope of the Capped Indemnity which have been incurred and paid by Group prior to such anniversary.

Restructuring provision

Restructuring of the business is currently ongoing and a provision is held to cover redundancy payments, property vacation costs and associated enablement costs. During the year £67m (2016: £45m) was charged to the income statement, of which £9m (2016: £6m) was charged directly to the income statement and £58m (2016: £39m) was provided for in accordance with the requirements of IAS 37. £61m (2016: £31m) of the total provision was utilised in the year.

Included within the restructuring provision is an amount for committed rental expense on surplus lease space consistent with the expected exposure on individual leases where the property is unoccupied. This element of the provision will be utilised over the remaining life of the leases or until the leases are assigned, and is measured at present values by discounting anticipated future cash flows.

3.15 Debt securities in issue

Accounting policy

Debt securities comprise short- and long-term debt issued by the Group including commercial paper, medium-term notes, term loans, covered bonds and residential mortgage backed securities (RMBS).

Debt securities are initially recognised at fair value, being the issue proceeds, net of transaction costs incurred. These instruments are subsequently measured at amortised cost using the effective interest method resulting in premiums, discounts and associated issue costs being recognised in the income statement over the life of the instrument.

The breakdown of debt securities in issue is shown below:

	Medium-term notes	Subordinated debt	Securitisation	Covered bonds	2017 Total £m	2016 Total £m
Amortised cost	**297**	**476**	**3,242**	**698**	**4,713**	4,383
Fair value hedge adjustments	**–**	**–**	**–**	**50**	**50**	99
Total debt securities	**297**	**476**	**3,242**	**748**	**4,763**	4,482
Accrued interest payable	**3**	**3**	**6**	**10**	**22**	19
	300	**479**	**3,248**	**758**	**4,785**	4,501

There were no new issuances of covered bonds during the year. The following new issuances of securitised debt occurred:

- 5 July 2017 – GBP 350m Lanark 2017-1 1A.
- 5 July 2017 – GBP 400m Lanark 2017-1 2A.

The following securitised debt redemptions occurred during the year in line with the scheduled programme terms:

- 22 August 2017 – EUR 300m Lanark 2014-1 1A.

On 22 June 2017, the Group issued a £300m 8-year, callable, 3.125% fixed to floating medium term note with a final maturity of 22 June 2025.

Medium-term notes	2017 £m	2016 £m
8-year, 3.125% fixed to floating rate callable senior notes due 2025	**297**	–
Accrued interest payable	**3**	–
Total medium-term notes	**300**	–

Subordinated debt	2017 £m	2016 £m
10-year, non-call five years, with a final maturity of 9 February 2026 – fixed 5%	**476**	477
Accrued interest payable	**3**	3
Total subordinated debt	**479**	480

Section 3: Assets and liabilities continued

3.15 Debt securities in issue continued

Details of the terms and conditions of the notes issued under the securitisation and covered bond programmes as at 30 September 2017 were as follows:

Issue date	Currency	Carrying value £m	Coupon rate	Call date
Class A Lanark RMBS				
27 July 2012	GBP	**288**	3M GBP LIBOR + 1.63%	22 November 2017
20 March 2014	GBP	**265**	3M GBP LIBOR + 0.50%	22 November 2018
11 December 2014	EUR	**368**	3M EURIBOR + 0.40%	22 August 2018
11 December 2014	GBP	**274**	3M GBP LIBOR + 0.60%	22 February 2020
6 August 2015	GBP	**120**	3M GBP LIBOR + 0.50%	22 August 2018
6 August 2015	EUR	**247**	3M EURIBOR + 0.45%	22 May 2021
4 August 2016	GBP	**606**	3M GBP LIBOR + 1.00%	22 February 2019
5 July 2017	GBP	**349**	3M GBP LIBOR + 0.42%	22 November 2020
5 July 2017	GBP	**399**	3M GBP LIBOR + 0.55%	22 August 2022
Class A Lannraig RMBS				
30 September 2011	GBP	**326**	3M GBP LIBOR + 2.20%	19 November 2017
		3,242		
Covered bonds				
31 May 2012	GBP	**748**	4.63%	8 June 2026
Total securitised notes and covered bonds (note 3.7)		**3,990**		

3.16 Retirement benefit obligations

Accounting policy

The Group makes contributions to both defined benefit and defined contribution pension schemes which entitle employees to benefits on retirement or disability.

Defined contribution pension scheme

The Group recognises the obligation for contributions to the scheme as an expense in the income statement as incurred. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payment is available.

Defined benefit pension scheme

A liability or asset in respect of the defined benefit scheme is recognised on the balance sheet and is measured as the present value of the defined benefit obligation less the fair value of the defined benefit scheme assets at the reporting date. The present value of the defined benefit obligation for the scheme is discounted by high quality corporate bond rates that have maturity dates approximating to the terms of the Group's defined benefit obligation. Surpluses are only recognised to the extent that they are recoverable through reduced contributions in the future or through refunds from the scheme. In assessing whether a surplus is recoverable, the Group considers its current right to obtain a refund or a reduction in future contributions and does not anticipate any future acts by other parties that could change the amount of the surplus that may be ultimately recovered.

Pension expense attributable to the Group's defined benefit scheme comprises current service cost, net interest on the net defined benefit obligation/asset, past service cost resulting from a scheme amendment or curtailment, gains or losses on settlement and administrative costs incurred. Where actuarial remeasurements arise, the Group recognises such amounts directly in equity through the statement of comprehensive income in the period in which they occur. Actuarial remeasurements arise from experience adjustments (the effects of differences between previous actuarial assumptions and what has actually occurred) and changes in actuarial assumptions.

The Group operates both defined benefit and defined contribution arrangements. The Group's principal trading subsidiary, Clydesdale Bank PLC, is the sponsoring employer in one funded defined benefit pension scheme, the Yorkshire and Clydesdale Bank Pension Scheme ('the Scheme'). The Scheme was established under trust on 30 September 2009 as a result of the merger of the Clydesdale Bank Pension Scheme and the Yorkshire Bank Pension Fund. The assets of the Scheme are held in a trustee administered fund, with the Trustee responsible for the operation and governance of the Scheme, including making decisions regarding the Scheme's funding and investment strategy.

The Scheme is subject to the funding legislation outlined in the Pensions Act 2004 which came into force on 30 December 2005. This, together with documents issued by the Pensions Regulator, sets out the framework for funding defined benefit occupational pension plans in the UK.

The Group also provides post-retirement health care under a defined benefit scheme for pensioners and their dependant relatives for which provision has been made on a basis consistent with the methodology applied to the defined benefit pension scheme. This is a closed scheme and the provision will be utilised over the life of the remaining scheme members.

The following table provides a summary of the present value of the defined benefit obligation and fair value of plan assets for the Scheme:

	2017 £m	2016 £m
Active members' defined benefit obligation[1]	**(807)**	(1,264)
Deferred members' defined benefit obligation	**(1,549)**	(1,776)
Pensioner and dependant members' defined benefit obligation	**(1,618)**	(1,497)
Total defined benefit obligation	**(3,974)**	(4,537)
Fair value of Scheme assets	**4,181**	4,462
Net defined benefit pension asset/(liability)	**207**	(75)
Post-retirement medical benefits obligations	**(3)**	(4)

(1) Active members include current employees who became deferred members on 1 August 2017 as part of the Scheme closure exercise.

The Group has implemented a number of reforms to the Scheme to manage the liability. It closed the Scheme to new members in 2004 and since April 2006 has determined benefits accruing on a career average revalued earnings basis. On 1 August 2017, the Scheme was closed to future benefit accrual for the majority of current employees, with affected employees' future pension benefits being provided through the existing defined contribution scheme, 'Total Pension'. The Total Pension income statement charge for the year is shown in note 2.4. The closure of the Scheme for the majority of current employees has resulted in a reduction in the defined benefit obligation, recognised as a past service credit in the year.

During the year, Clydesdale Bank PLC reached agreement with the Trustee on the Scheme funding valuation at 30 September 2016, with a calculated deficit of £290m. In the recovery plan dated 31 July 2017 the Group agreed to contribute £50m per annum until 31 March 2022 and £55m in the year to 31 March 2023 to eliminate this deficit.

Reconciliation of the net defined benefit pension asset/(liability)

	2017 £m	2016 £m
Opening net defined benefit pension scheme (liability)/asset	**(75)**	52
Service credit/(cost)	**54**	(31)
Interest on net defined benefit (liability)/asset	**(1)**	3
Remeasurement effects recognised in SOCI	**154**	(179)
Employer contributions	**69**	84
Administrative expenses	**(7)**	(4)
Curtailments and settlements	**13**	–
Closing fair value of net defined benefit pension scheme asset/(liability)	**207**	(75)

Section 3: Assets and liabilities continued

3.16 Retirement benefit obligations continued

Reconciliation of the defined benefit pension scheme assets

	2017 £m	2016 £m
Opening fair value of defined benefit pension scheme assets	**4,462**	3,565
Interest income on Scheme assets at discount rate	**104**	135
Return on Scheme assets (less)/greater than discount rate	**(195)**	791
Employer contributions (note 5.3)	**69**	84
Benefits paid	**(102)**	(90)
Transfer payments	**(150)**	(19)
Administrative costs paid	**(7)**	(4)
Closing fair value of defined benefit pension scheme assets	**4,181**	4,462

Reconciliation of the defined benefit pension scheme obligations

	2017 £m	2016 £m
Opening defined benefit pension scheme obligations	**(4,537)**	(3,513)
Current service cost	**(26)**	(27)
Past service credit/(cost)	**80**	(4)
Interest expense on the defined benefit obligation	**(105)**	(132)
Actuarial gain – experience adjustments	**76**	51
Actuarial gain – demographic assumptions	**88**	–
Actuarial gain/(loss) – financial assumptions	**185**	(1,021)
Benefits paid from Scheme assets	**102**	90
Transfer payments	**150**	19
Curtailments and settlements	**13**	–
Closing defined benefit pension scheme obligations	**(3,974)**	(4,537)

The major categories of plan assets for the Scheme, stated at fair value, are as follows:

	2017 £m	2016 £m
Quoted		
Equities	**804**	784
Government bonds	**1,495**	1,640
Global sovereign bonds	**33**	38
Corporate bonds	**829**	968
Alternative credit	**97**	–
Infrastructure	**272**	254
Secure income alternatives	**209**	124
Derivatives(1)	**169**	440
Other	**4**	6
Cash	**124**	93
Unquoted		
Property	**145**	115
Fair value of defined benefit pension scheme assets	**4,181**	4,462

(1) Derivative financial instruments are used to modify the profile of the assets of the Scheme to better match the Scheme's liabilities. Derivative holdings may lead to increased or decreased exposures to the physical asset categories disclosed above.

The Scheme is not invested in any of the Group's own financial instruments.

Through its defined benefit pension plan and post-employment medical plan, the Group is exposed to a number of risks. The main risk to the Group is that additional contributions are required if the Scheme's assets are not sufficient to pay for the benefits (which will be influenced mainly by inflation and the longevity of members). The level of asset returns will be a key factor in the overall investment return. The investment portfolio is subject also to a range of risks typical of the assets held, in particular equity risk, credit risk on bonds and exposure to the property market.

The Trustee has implemented an investment structure (including physical assets and derivatives) that seeks to reduce the Scheme's exposure to inflation and interest rate risks. The current hedge ratio is around 60% of liabilities when measured on a self-sufficiency basis. This strategy reflects the Scheme's liability profile and the Trustee's and the Group's attitude to risk. The Trustee monitors the investment objectives and asset allocation policy on a regular basis.

Amounts recognised in the income statement

	2017 £m	2016 £m
Current service cost	**26**	27
Past service cost	**8**	4
Past service credit on closure of Scheme	**(88)**	–
Curtailment and settlement gains	**(13)**	–
Net interest on net defined benefit liability/(asset)	**1**	(3)
Defined benefit (income)/expense for the year	**(66)**	28
Administration costs incurred	**7**	4
(Credit)/cost recognised in the income statement (note 2.4)	**(59)**	32

The Group incurred a past service cost of £8m (2016: £4m) in relation to enhanced early retirement entitlements on redundancy; in both years these were fully offset in the income statement by a corresponding release from the restructuring provision. In contrast, the income statement benefited from a curtailment gain of £13m (2016: £Nil) due to a higher than normal level of redundancies in the current year with no enhancement entitlement; this gain has been offset against the related restructuring costs.

Amounts recognised in the statement of comprehensive income

	2017 £m	2016 £m
Opening cumulative actuarial losses	**(849)**	(670)
Actuarial gain due to liability experience adjustments	**76**	51
Actuarial gain/(loss) due to liability assumption changes	**185**	(1,021)
Actuarial gain due to demographic assumption changes	**88**	–
Return on Scheme assets (less)/greater than discount rate	**(195)**	791
Cumulative actuarial losses recognised in the statement of comprehensive income	**(695)**	(849)

Actuarial assumptions

	2017 % p.a.	2016 % p.a.
Financial assumptions		
Discount rate	**2.74**	2.38
Inflation (RPI)	**3.24**	3.02
Inflation (CPI)	**2.24**	2.02
Career average revalued earnings (CARE) revaluations:		
Pre 31 March 2012 benefits (RPI)	**3.24**	3.02
Post 31 March 2012 benefits (CPI capped at 5% per annum)	**2.24**	2.02
Pension increases (capped at 2.5% per annum)	**2.12**	2.05
Pension increases (capped at 5% per annum)	**3.10**	2.94
Rate of increase for pensions in deferment	**2.24**	2.02

Demographic assumptions Post-retirement mortality:	**2017 years**	2016 years
Current pensioners at 60 – male	**28.2**	27.7
Current pensioners at 60 – female	**29.7**	29.6
Future pensioners at 60 – male	**29.3**	29.2
Future pensioners at 60 – female	**30.9**	31.1

Section 3: Assets and liabilities continued

3.16 Retirement benefit obligations continued

Critical accounting estimates and judgements

The value of the Group's defined benefit pension scheme requires management to make several assumptions. The key areas of estimation uncertainty are:

- *The discount rate applied.* The discount rate is required to be set with reference to market yields at the end of the reporting period on high quality corporate bonds in the currency and with a term consistent with the Scheme's obligations. The average duration of the Scheme's obligations is approximately 20 years. The market for bonds with a similar duration is illiquid and, as a result, significant management judgement is required to determine an appropriate yield curve on which to base the discount rate.
- *Inflation assumptions.* Inflation is set with reference to market expectations of the RPI measure of inflation for a term consistent with the Scheme's obligations, based on data published by the BoE. Other measures of inflation (such as CPI, or inflation measures subject to an annual cap) are derived from this assumption.
- *Mortality assumptions.* The cost of the benefits payable by the Scheme will also depend upon the life expectancy of the members. The assumptions for mortality rates are based on standard mortality tables which allow for future improvements in life expectancies.

The table below sets out the sensitivity of the defined benefit obligation and pension cost to realistic changes in the key actuarial assumptions:

Assumption change

	Impact on defined benefit obligation £m	Impact on pension cost £m
Discount rate		
+0.25%	(186)	(6)
-0.25%	199	6
Inflation		
+0.25%	140	4
-0.25%	(135)	4
Life expectancy		
+1 year	136	4
-1 year	(139)	(4)

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, changes in some of the assumptions may be correlated.

The discounted mean term of the defined benefit obligation at 30 September 2017 is 20 years (2016: 22 years). The expected contributions for the year ending 30 September 2018 are £33m (2017: £Nil) and expected benefit payments for the year ending 30 September 2018 are £100m (2017: £85m).

During the current year, the Group and Trustee entered into a contingent security arrangement (the 'Security Arrangement') (note 5.3).

3.17 Other liabilities

	2017 £m	2016 £m
Notes in circulation	**2,197**	1,912
Accruals and deferred income	**163**	152
Other	**111**	146
	2,471	2,210

3.18 Fair value of financial instruments

Accounting policy
Fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants at the valuation date.

When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. Where no such active market exists for the particular asset or liability, the Group uses a valuation technique to arrive at the fair value, including the use of transaction prices obtained in recent arm's length transactions where possible, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. In doing so, fair value is estimated using a valuation technique that makes maximum possible use of market inputs and that places minimal possible reliance upon entity-specific inputs.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, which represents the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Group recognises profits or losses on the transaction date.

In certain limited circumstances the Group applies the fair value measurement option to financial assets including loans and advances where the inherent market risks (principally interest rate and option risk) are individually hedged using appropriate interest rate derivatives. The loan is designated as being carried at fair value through profit or loss to offset the movements in the fair value of the derivative within the income statement and therefore avoid accounting mismatch. When a loan is held at fair value, a statistical based calculation is used to estimate expected losses attributable to adverse movements in credit risk on the assets held. This adjustment to the credit quality of the asset is then applied to the carrying amount of the loan to arrive at fair value and recognised in the income statement.

Analysis of the fair value disclosures uses a hierarchy that reflects the significance of inputs used in measuring fair value. The level in the fair value hierarchy within which a fair value measurement is categorised is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. The fair value hierarchy is as follows:

– Level 1 fair value measurements – quoted prices (unadjusted) in active markets for an identical financial asset or liability;

– Level 2 fair value measurements – inputs other than quoted prices within Level 1 that are observable for the financial asset or liability, either directly (as prices) or indirectly (derived from prices); and

– Level 3 fair value measurements – inputs for the financial asset or liability that are not based on observable market data (unobservable inputs).

For the purpose of reporting movements between levels of the fair value hierarchy, transfers are recognised at the beginning of the reporting period in which they occur.

(a) Fair value of financial instruments recognised on the balance sheet at amortised cost
The tables overleaf show a comparison of the carrying amounts of financial assets and liabilities measured at amortised cost, as reported on the balance sheet, and their fair values where these are not approximately equal.

There are various limitations inherent in this fair value disclosure particularly where prices are derived from unobservable inputs due to some financial instruments not being traded in an active market. The methodologies and assumptions used in the fair value estimates are therefore described in the notes to the tables. The difference between carrying value and fair value is relevant in a trading environment, but is not relevant to assets such as loans and advances.

Section 3: Assets and liabilities continued

3.18 Fair value of financial instruments continued

	30 September 2017					30 September 2016				
			Fair value measurement using:					Fair value measurement using:		
	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets										
Loans and advances to customers	**31,293**	**31,088**	**–**	**1,009**	**30,079**	29,202	29,298	–	1,076	28,222
Financial liabilities										
Due to customers	**27,718**	**27,833**	**–**	**27,833**	**–**	27,090	27,114	–	27,114	–
Debt securities in issue	**4,785**	**4,910**	**795**	**4,115**	**–**	4,501	4,592	459	4,133	–

The Group's fair values disclosed for financial instruments at amortised cost are based on the following methodologies and assumptions:

(a) *Loans and advances to customers* – The fair values of loans and advances are determined by firstly segregating them into portfolios of similar characteristics. Contractual cash flows are then adjusted for expected credit losses and expectations of customer behaviour based on observed historic data. The cash flows are then discounted using current market rates for instruments of similar terms and maturity to arrive at an estimate of their fair value. Certain variable rate loan portfolios are discounted using market rates on similar loans offered by the Group at the valuation date.

(b) *Due to customers* – The fair value of deposits is determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity.

(c) *Debt securities in issue* – The fair value is taken directly from quoted market prices where available or determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity.

(b) Fair value of financial instruments recognised on the balance sheet at fair value
The following tables provide an analysis of financial instruments that are measured subsequent to initial recognition at fair value, using the fair value hierarchy described above.

	Fair value measurement as at 30 September 2017				Fair value measurement as at 30 September 2016			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets								
Derivative financial assets	**–**	**282**	**–**	**282**	–	585	–	585
AFS investments – listed	**2,066**	**–**	**–**	**2,066**	1,695	–	–	1,695
AFS investments – unlisted	**–**	**–**	**4**	**4**	–	–	29	29
AFS – other	**–**	**–**	**6**	**6**	–	–	7	7
Other financial assets at fair value	**–**	**–**	**477**	**477**	–	–	750	750
Total financial assets at fair value	**2,066**	**282**	**487**	**2,835**	1,695	585	786	3,066
Financial liabilities								
Derivative financial liabilities	**–**	**376**	**–**	**376**	–	598	–	598
Other financial liabilities at fair value	**–**	**–**	**26**	**26**	–	–	48	48
Total financial liabilities at fair value	**–**	**376**	**26**	**402**	–	598	48	646

There were no transfers between Level 1 and 2 in the year.

The Group's fair values for financial instruments that are measured subsequent to initial recognition at fair value are based on the following methodologies and assumptions:

(a) *Derivative financial assets and liabilities* – The fair values of derivatives, including foreign exchange contracts, interest rate swaps, interest rate and currency option contracts, and currency swaps, are obtained from discounted cash flow models or option pricing models as appropriate.

(b) *Available for sale investments*

- *Listed (Level 1)* – The fair values of listed investments are based on quoted closing market prices.
- *Unlisted (Level 3)* – Includes £2m of Visa Inc. preferred stock received as partial consideration for the sale of the Group's share in Visa Europe (note 2.3). The preferred stock is convertible into Visa Inc. common stock or its equivalent at a future date, subject to potential reduction for certain litigation losses that may be incurred by Visa Europe. The fair value of the preference shares has been calculated by taking the period end New York Stock Exchange share price for Visa Inc. and discounting for illiquidity and clawback related to contingent litigation. For other unlisted equity and debt investments, the Group's share of the net asset value or the transaction price respectively are considered the best representation of the exit price and are the Group's best estimates of fair value.
- *Available for sale – other (Level 3)* – The other available for sale financial asset represents deferred consideration receivable and consists of the rights to future commission. The valuation is determined from a discounted cash flow model incorporating estimated attrition rates and investment growth rates appropriate to the underlying funds under management.

(c) *Financial assets and liabilities at fair value through profit or loss* – fair values are derived from data or valuation techniques based upon observable market data and non-observable inputs as appropriate to the nature and type of the underlying instrument.

Assets and liabilities measured at fair value based on valuation techniques for which any significant input is not based on observable market data (Level 3):

Level 3 movement analysis:

	2017		
	Financial assets available for sale £m	**Other financial assets at fair value £m**	**Other financial liabilities at fair value £m**
Balance at the beginning of the year	**36**	**750**	**(48)**
Fair value gains/(losses) recognised(1)			
In profit or loss (unrealised)	**–**	**(39)**	**2**
In profit or loss (realised)	**1**	**2**	**–**
In available for sale reserve (unrealised)	**1**	**–**	**–**
Purchases	**–**	**–**	**–**
Sales(2)	**(26)**	**–**	**–**
Settlements	**(2)**	**(236)**	**20**
Balance at the end of the year	**10**	**477**	**(26)**

Level 3 movement analysis:

	2016		
	Financial assets available for sale £m	Other financial assets at fair value £m	Other financial liabilities at fair value £m
Balance at the beginning of the year	15	1,097	(67)
Fair value gains/(losses) recognised(1)			
In profit or loss (unrealised)	–	10	2
In profit or loss (realised)	8	–	–
In available for sale reserve (unrealised)	21	–	–
Purchases	2	–	–
Sales	(8)	–	–
Settlements(3)	(2)	(357)	17
Balance at the end of the year	36	750	(48)

(1) Net gains or losses were recorded in non-interest income, interest income or expense and impairment losses or within the available for sale reserve as appropriate.
(2) The sale principally relates to the disposal of the VocaLink investment during the year (note 2.3).
(3) Settlements for the year ended 30 September 2016 include a realised loss of £5m relating to financial assets that are measured at fair value at the end of each reporting period. Such fair value gains or losses are included in non-interest income (note 2.3).

There were no transfers into or out of Level 3 in the year ended 30 September 2017 (2016: £Nil).

Section 3: Assets and liabilities continued

3.18 Fair value of financial instruments continued

Quantitative information about significant unobservable inputs in Level 3 valuations

The table below lists key unobservable inputs to Level 3 financial instruments, and provides the range of those inputs as at 30 September 2017.

	Fair value £m	Valuation technique	Unobservable inputs	Low range	High range
Financial assets					
Other financial assets at fair value	**477**	Discounted cash flow	Portfolio lifetime probability of default	2.2%	11.3%
Available for sale – other	**6**	Discounted cash flow	Funds under management attrition rate	10%	20%
Available for sale – investments – unlisted	**4**	Discounted cash flow	Contingent litigation risk	0%	100%

The Group has £26m (2016: £48m) of financial liabilities at fair value classed as Level 3 which represent a portfolio of term deposits that are directly linked to the customer loans, which are also held at fair value and classed as Level 3. Their relationship to the fair value assets is such that should the liability be settled, the amount payable would be net of the fair value asset.

Sensitivity of Level 3 fair value measurements to reasonably possible alternative assumptions

Where valuation techniques use non-observable inputs that are significant to a fair value measurement in its entirety, changing these inputs will change the resultant fair value measurement.

The most significant exposure to Level 3 fair value measurements is in respect of the Group's fair value loan portfolio with the most significant input (other than interest rates) being the future expectations of credit losses. If lifetime expected losses were 20% greater than predicted, the carrying value of the loans would decrease by £2m and vice versa.

The most significant input impacting the fair value of the available for sale – other asset is the funds under management attrition rate. The Group currently assumes a 15% attrition rate. If this rate was 20% the fair value would reduce by £1m, if it was 10% the fair value would increase by £2m.

The most significant input impacting the fair value of the available for sale – investments is contingent litigation risk. If this risk crystallised, the fair value would reduce by £2m. In the event the litigation risk did not transpire the fair value would increase by £3m. Other than these significant Level 3 measurements, the Group has a limited remaining exposure to Level 3 fair value measurements, and changing one or more of the inputs for fair value measurements in Level 3 to reasonable alternative assumptions would not change the fair value significantly with respect to profit or loss, total assets, total liabilities or equity on these remaining Level 3 measurements.

Section 4: Capital

4.1 Equity

Accounting policy

Equity

The financial instruments issued by the Company are treated as equity (i.e. forming part of shareholders' funds) only to the extent that they meet the following two conditions:

(a) they include no contractual obligations upon the Company to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the Group; and

(b) where the instrument will or may be settled in the Company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the Company's own equity instruments or is a derivative that will be settled by the Company exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability.

Dividends

Incremental costs directly attributable to the issue of new shares or options or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds.

Final dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the Company's shareholders. Interim dividends are deducted from equity when they are no longer at the discretion of the Company.

Proposed final dividends for the year are disclosed as an event after the balance sheet date.

4.1.1 Share capital

	2017 Number of shares	2016 Number of shares	2017 £m	2016 £m
Ordinary shares – allotted, called up and fully paid				
Opening ordinary share capital	**881,531,852**	2,232,012,512	**88**	223
Share for share exchange	**–**	(1,352,697,256)	**–**	876
Share capital reduction	**–**	–	**–**	(1,011)
Issued under employee share schemes	**2,074,214**	2,216,596	**–**	–
Closing ordinary share capital	**883,606,066**	881,531,852	**88**	88

During the year 2,074,214 (2016: 2,216,596) ordinary shares were issued under employee share schemes with a nominal value of £0.2m (2016: £0.2m).

The share for share exchange in the year to 30 September 2016 arose on the Group's demerger from NAB and listing on the London Stock Exchange.

The holders of ordinary shares are entitled to dividends as declared from time to time and are entitled to one vote per share at meetings of the shareholders of the Company. All shares in issue at 30 September 2017 rank equally with regard to the Company's residual assets.

The Directors have recommended a final dividend in respect of the year ended 30 September 2017 of 1p per ordinary share in the Company (2016: Nil) to be paid on 16 February 2018. The payment of the final dividend is subject to approval of the shareholders at the 2018 Annual General Meeting. These financial statements do not reflect the recommended dividend.

With regards to utilisation of the Conduct Indemnity, note 3.14 sets out a number of circumstances where share capital in the Company could be subscribed for by NAB.

A description of the other equity categories included within the Consolidated statement of changes in equity, and significant movements during the year, is provided below.

4.1.2 Other equity instruments

Other equity instruments consists of Perpetual Contingent Convertible Notes (fixed 8%) which were issued on 8 February 2016 with a principal amount of £450m and an optional redemption on 8 December 2022.

AT1 distributions of £36m were paid in the year, £29m net of tax (2016: £35m paid, £28m net of tax).

Section 4: Capital continued

4.1.3 Capital reorganisation reserve
The capital reorganisation reserve of £839m was recognised on the issuance of CYBG PLC ordinary shares in February 2016 in exchange for the acquisition of the entire share capital of the Group's previous parent company, CYBI Limited. The reserve reflects the difference between the consideration for the issuance of CYBG PLC shares and CYBI Limited's share capital and share premium.

4.1.4 Merger reserve
A merger reserve of £633m was recognised on the issuance of CYBG PLC ordinary shares in February 2016 in exchange for the acquisition of the entire share capital of CYBI Limited. The merger reserve reflects the difference between the consideration for the issuance of CYBG PLC shares and the nominal value of the shares issued.

4.1.5 Other reserves
4.1.5.1 Asset revaluation reserve
The asset revaluation reserve includes the gross revaluation increments and decrements arising from the revaluation of land and buildings.

4.1.5.2 Available for sale reserve
The available for sale reserve records the gains and losses arising from changes in the fair value of available for sale financial assets. The principal movement in the reserve reflects the sale of VocaLink during the year as detailed in note 2.3.

4.1.5.3 Cash flow hedge reserve
The cash flow hedge reserve represents the cumulative post-tax gains and losses on derivatives designated as cash flow hedging instruments that will be recycled to the income statement when the hedged items affect profit or loss.

As at 30 September 2017, the cash flow hedge reserve reflected a cumulative loss of £1m (2016: £66m cumulative gain). The fair value of derivatives in cash flow hedges decreased by £84m in the year (2016: £105m increase), and a £4m gain (2016: £2m gain) was recycled to interest income in line with hedged items affecting profit or loss. A £0.3m loss (2016: £1m loss) was transferred to non-interest income due to ineffectiveness arising from cash flow hedges. These movements were offset by a deferred tax credit of £21m (2016: charge of £25m).

4.1.5.4 Equity-based compensation reserve
The Group's equity based compensation reserve records the value of equity settled share based payment benefits provided to the Group's employees as part of their remuneration that has been charged through the income statement and adjusted for deferred tax.

4.2 Equity based compensation

Accounting policy
The Group operates a number of equity settled share based compensation plans in respect of services received from certain of its employees. The fair value of the services received is recognised as an expense. The total amount to be expensed is measured by reference to the fair value of the Company's shares, performance options or performance rights granted, including, where relevant, any market performance conditions and any non-vesting conditions. The impacts of any service and non-market performance vesting conditions are not included in the fair value and instead are included in estimating the number of awards or options that are expected to vest.

The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. A corresponding credit is recognised in the equity based compensation reserve, adjusted for deferred tax. In some circumstances employees may provide services in advance of the grant date and therefore the grant date fair value is estimated for the purposes of recognising the expense during the period between the start of the service period and the grant date.

At the end of each reporting period, the Group revises its estimates of the number of shares, performance options and performance rights that are expected to vest based on the non-market and service vesting conditions. The impact of the revision to original estimates, if any, is recognised in the income statement, with a corresponding adjustment to the equity based compensation reserve.

The equity settled share based payment charge for the year is £6m (2016: £5m).

In the prior year, the figures include awards under the Group's and NAB share plans. The charges under the NAB share plans were classified as equity settled share based payments up to the demerger date of 8 February 2016 and are included in the total above. Following the demerger these plans no longer meet the definition of share based payments under IFRS 2 'Share based payments', accordingly, the total above excludes NAB share plan costs after 8 February 2016. Details of these plans are included within the Directors' remuneration report.

CYBG awards

The Group made a number of awards under its share plans:

Plan	Eligible employees	Nature of award	Vesting conditions[1]	Grant dates[2]
Deferred Equity Plan[3]	Selected employees	Conditional rights to shares	Continuing employment or leaving in certain limited circumstances	2016 and 2017
Long Term Incentive Plan	Selected senior employees	Conditional rights to shares	Continuing employment or leaving in certain limited circumstances and achievement of delivery of the Group's strategic goals and growth in shareholder value.	2017
Share Incentive Plan	All employees	Non-conditional share award	Continuing employment	2016

(1) All awards are subject to vesting conditions and therefore may or may not vest.
(2) The year in which grants have been made under the relevant plan.
(3) Grants made under the Deferred Equity Plan are made the year following the financial year to which they relate.

Further detail on each plan is provided below:

Deferred Equity Plan (DEP)

Under the plan employees were awarded conditional rights to CYBG PLC shares. The shares are subject to forfeiture conditions including forfeiture as a result of resignation, termination by the Group or failure to meet compliance requirements. Awards include:

– The upfront and deferred elements of bonus awards where required to comply with the PRA Remuneration Code or the Group's deferral policy.

– Buyout of equity from previous employment for senior new hires.

– Demerger awards which are also subject to the achievement of performance conditions over a three-year period. Details of the performance conditions are set out in the Directors' remuneration report.

Long Term Incentive Plan (LTIP)

Under the plan employees were awarded conditional rights to CYBG PLC shares. The shares are subject to forfeiture conditions including forfeiture as a result of resignation, termination by the Group or failure to meet compliance requirements.

The performance conditions of the plan must be met over a three-year period. The measures reflect a balanced approach between financial and non-financial performance and are aligned to the organisation's strategic goals. Measures, relative weightings and the quantum for assessing performance are outlined in the Directors' remuneration report section.

Share Incentive Plan (SIP)

Eligible employees at the date of the award, were awarded Group shares, which are held in the Share Incentive Plan Trust (SIP Trust). Awards are not subject to performance conditions and participants are the beneficial owners of the shares granted to them, but not the registered owners. Voting rights over the shares are normally exercised by the registered owner at the direction of the participants. For the 2015 Demerger award, leavers (with the exception of gross misconduct) retain their awards but they must withdraw their shares from the SIP Trust.

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Section 4: Capital continued

4.2 Equity based compensation continued

Awards/rights made during the year

Plan	Number outstanding at 1 October 2016	Number awarded	Number forfeited	Number released	**Number outstanding as 30 September 2017**	Average fair value of awards at grant pence
Deferred Equity Plan						
2015 Demerger	2,235,204	–	(197,152)	–	**2,038,052**	196.96
2015 Bonus	1,489,390	–	(7,370)	(1,346,425)	**135,595**	195.17
2015 Commencement	111,127	–	–	(46,059)	**65,068**	194.67
2016 Bonus	–	1,193,700	(6,776)	(643,729)	**543,195**	266.03
2016 Commencement	–	169,997	–	(38,001)	**131,996**	266.03
Long Term Incentive Plan						
2016 LTIP	–	2,261,948	(18,561)	–	**2,243,387**	266.03
Share Incentive Plan						
2015 Demerger	1,822,976	–	(2,560)(1)	(337,408)(2)	**1,483,008**	194.67

(1) Forfeited shares remain in the SIP Trust.
(2) Shares withdrawn from SIP Trust on leaving the Group.

Determination of grant date fair values

Participants of the DEP and LTIP plans are not entitled to dividends until the awards vest, but the number of shares which vest may be increased to reflect the value of dividends that would have been paid up to the end of the holding period for the awards, subject to the extent permitted under the relevant remuneration regulation. Accordingly, the grant date fair value of the awards with only service conditions and/or non-market performance conditions has been taken as the market value of the Company's ordinary shares at the grant date. Where awards are subject to non-market performance conditions, an estimate is made of the number of awards expected to vest in order to determine the overall share-based payment charge to be recognised over the vesting period.

The Group has not issued awards under any CYBG plan with market performance conditions.

Section 5: Other notes

5.1 Contingent liabilities and commitments

Accounting policy

Financial guarantees

The Group provides guarantees in the normal course of business on behalf of its customers. Guarantees written are conditional commitments issued by the Group to guarantee the performance of a customer to a third party and are primarily issued to support direct financial obligations such as commercial bills or other debt instruments issued by a counterparty. The rating of the Group as a guarantee provider enhances the marketability of the paper issued by the counterparty in these circumstances. Financial guarantee contracts are initially recorded at fair value which is equal to the premium received, unless there is evidence to the contrary.

Operating lease commitments

The leases entered into by the Group are primarily operating leases; with operating lease rentals charged to the income statement on a straight line basis over the period of the lease. The Group discloses its obligations for future minimum payments under non-cancellable leases.

Contingent liabilities

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

The table below sets out the amounts of financial guarantees and commitments which are not recorded on the balance sheet. Financial guarantees and commitments are credit-related instruments which include acceptances, letters of credit, guarantees and commitments to extend credit. The amounts do not represent the amounts at risk at the balance sheet date but the amounts that would be at risk should the contracts be fully drawn upon and the customer default. Since a significant portion of guarantees and commitments is expected to expire without being drawn upon, the total of the contract amounts is not representative of future liquidity requirements.

Financial guarantees

	2017 £m	2016 £m
Guarantees and assets pledged as collateral security:		
Due in less than 3 months	**19**	19
Due between 3 months and 1 year	**40**	44
Due between 1 year and 3 years	**7**	9
Due between 3 years and 5 years	**3**	3
Due after 5 years	**42**	48
No specified maturity	**–**	–
	111	123
Other credit commitments		
Undrawn formal standby facilities, credit lines and other commitments to lend at call	**8,408**	7,690

Capital commitments

The Group had future capital expenditure which had been contracted for but not provided for at 30 September 2017 of £1m (2016: £2m).

Section 5: Other notes continued

5.1 Contingent liabilities and commitments continued

Operating lease commitments

	2017 £m	2016 £m
Leases as lessor		
Future minimum lease payments under non-cancellable operating leases are:		
Within 1 year	**1**	2
Between 1 year and 5 years	**4**	4
Over 5 years	**–**	1
	5	7
Leases as lessee		
Future minimum lease payments under non-cancellable operating leases are:		
Within 1 year	**30**	29
Between 1 year and 5 years	**100**	94
Over 5 years	**137**	117
	267	240

Other contingent liabilities

Financial Services Compensation Scheme (FSCS)

The FSCS provides compensation to depositors in the event that a financial institution is unable to repay amounts due. Following the failure of a number of financial institutions, claims were triggered against the FSCS, initially to pay interest on borrowings which the FSCS has raised from the UK Government to support the protected deposits. During 2015, the FSCS levy was also invoiced to institutions for the third of three annual levies to cover capital repayments to the UK Government. The principal of these borrowings, which remains after the three annual levies have been paid, is anticipated to be repaid from the realisation of the assets of the defaulted institutions. The FSCS has however confirmed that the size of the future levies will be kept under review in light of developments from the insolvent estates.

The FSCS has estimated levies due to 31 March 2018 for the interest on borrowings and an accrual of £2m (30 September 2016: £8m) is held for the Group's calculated liability to that date. The ultimate FSCS levy as a result of the failures is uncertain.

Conduct risk related matters

There continues to be significant uncertainty and thus judgement is required in determining the quantum of conduct risk related liabilities, with note 3.14 reflecting the Group's current position in relation to redress provisions including those for PPI. The final amount required to settle the Group's potential liabilities for these, and other conduct related matters, is materially uncertain. Contingent liabilities include those matters where redress is likely to be paid and costs incurred but the amounts cannot currently be estimated. The financial exposure to the Group related to legacy conduct risks is mitigated by the Capped Indemnity provided by NAB (note 3.14). The Group will continue to reassess the adequacy of provisions for these matters and the assumptions underlying the calculations at each reporting date based upon experience and other relevant factors at that time.

Legal claims

The Group is named in and is defending a number of legal claims arising in the ordinary course of business. No material adverse impact on the financial position of the Group is expected to arise from the ultimate resolution of these legal actions.

5.2 Notes to the statement of cash flows

	2017 £m	2016 £m
Adjustments included in profit before tax		
Interest receivable	**(1,075)**	(1,101)
Interest payable	**231**	295
Depreciation and amortisation (note 2.4)	**87**	88
Net gain on capital and debt restructure	**–**	(1)
Transfer from cash flow hedge reserve	**–**	1
Derivative financial instruments fair value movements	**(6)**	(10)
Impairment losses on credit exposures (note 3.6)	**48**	39
Impairment losses on software (note 2.4)	**–**	45
Fair value movement on investment properties	**1**	1
Equity based compensation	**6**	–
Gain on disposal of VocaLink	**(20)**	–
	(728)	(643)
Changes in operating assets		
Net (increase)/decrease in:		
Balances with supervisory central banks	**(1)**	1
Due from other banks	**(221)**	(826)
Derivative financial instruments	**280**	(63)
Financial assets at fair value through profit or loss	**237**	346
Loans and advances to customers	**(2,140)**	(1,758)
Other assets	**(12)**	15
	(1,857)	(2,285)
Changes in operating liabilities		
Net increase/(decrease) in:		
Due to other banks	**608**	960
Derivative financial instruments	**(221)**	60
Financial liabilities at fair value through profit or loss	**(21)**	(19)
Due to customers	**699**	672
Provisions for liabilities and charges	**(298)**	(154)
Defined benefit pension obligations	**(128)**	(52)
Other liabilities	**280**	120
	919	1,587

For the purposes of the statement of cash flows, cash and cash equivalents comprise the following balances with less than three months maturity from the date of acquisition. This includes cash and liquid assets and amounts due to other banks (to the extent less than 90 days).

	2017 £m	2016 £m
Cash and balances with central banks (note 3.1)	**6,893**	5,912
Other assets	**99**	111
Due to other banks	**(12)**	(25)
Other liabilities	**(28)**	(48)
	6,952	5,950

Section 5: Other notes continued

5.3 Related party transactions

Compensation of key management personnel (KMP)

KMP comprises Directors of the Company and members of the Executive Leadership Team.

	2017 £m	2016 £m
Salaries and short-term benefits	**8**	8
Other long-term employee benefits	**–**	1
Termination benefits	**–**	2
Equity based compensation(1)	**1**	4
	9	15

(1) Basis of the expense recognised in the year in accordance with IFRS 2 'Equity based compensations', including associated employers' NIC.

The following information regarding Directors' remuneration is presented in accordance with the Companies Act 2006.

	2017 £m	2016 £m
Aggregate remuneration	**5**	6

In addition to the above, £0.2m (2016: £Nil) was expensed relating to long-term incentive plans. None of the Directors were members of the Group's defined contribution pension scheme during 2017 (2016: none). One of the Directors was a member of the Group's defined benefit pension scheme during 2017 (2016: one). None of the Directors hold share options and none were exercised during the year (2016: none).

Transactions with KMP

KMP, their close family members and any entities controlled or significantly influenced by the KMP have undertaken the following transactions with the Group in the normal course of business. The transactions were made on the same terms and conditions as applicable to other Group employees, or on normal commercial terms.

	2017 £m	2016 £m
Loans and advances	**2**	8
Deposits	**4**	3

No provisions have been recognised in respect of loans provided to the KMP (2016: £Nil). There were no debts written off or forgiven during the year to 30 September 2017 (2016: £Nil). Included in the above are three (2016: six) loans totalling £1m (2016: £7.4m) made to Directors. In addition to the above, there are guarantees of £Nil (2016: £0.4m) made to Directors and their related parties.

Other related party transactions

During the current year, the Group and Trustee entered into a contingent Security Arrangement. The Security Arrangement provides additional support to the Scheme by underpinning recovery plan contributions and some additional investment risk. The security is in the form of a pre-agreed maximum level of assets that are set aside for the benefit of the Pension Scheme in certain trigger events. These assets are held by Red Grey Square Funding LLP, an insolvency remote consolidated structured entity.

The Group incurred costs in relation to pension scheme administration. These costs, which amounted to £0.3m in the year ended 30 September 2017 (2016: £0.5m), were charged to the Group sponsored scheme. The Group has deposits of £20.3m (2016: £31.7m) at the year end placed by the Scheme at market rates.

Pension contributions of £69m (2016: £84m) were made during the year to the Yorkshire and Clydesdale Bank Pension Scheme sponsored by the Group (note 3.16).

5.4 Pillar 3 disclosures

Basel III Capital Requirements Directive IV

Pillar 3 disclosure requirements are set out in Part Eight of the CRR. The consolidated disclosures of the Group, for the 2017 financial year, will be issued concurrently with the Annual Report and Accounts and will be found at www.cybg.com/investor-centre/financial-results/.

Company balance sheet

as at 30 September	Note	2017 £m	2016 £m
Assets			
Due from related entities	6.6	**803**	498
Due from other banks		**364**	7
Current tax assets		**1**	3
Investments in controlled entities	6.2	**2,249**	2,193
Deferred tax assets		**–**	1
Total assets		**3,417**	2,702
Liabilities			
Due to other banks		**91**	36
Due to related entities	6.6	**366**	7
Debt securities in issue	6.3	**779**	480
Other liabilities		**2**	2
Total liabilities		**1,238**	525
Equity			
Share capital		**88**	88
Other equity instruments	6.5	**450**	450
Merger reserve	6.5	**633**	633
Other reserves	6.5	**6**	3
Retained earnings	6.5	**1,002**	1,003
Total equity		**2,179**	2,177
Total liabilities and equity		**3,417**	2,702

The Company made a profit of £24m (2016: loss of £3m) during the year.

The notes on pages 244 to 248 form an integral part of these financial statements.

Company statement of changes in equity

for the year ended 30 September	Note	Share capital £m	Merger reserve £m	Other equity instru-ments £m	Other reserves: Equity based compen-sation reserve £m	Other reserves: Cash flow hedge reserve £m	Retained earnings £m	Total equity £m
At 1 October 2015	6.5	–	–	–	–	–	–	–
Loss for the year		–	–	–	–	–	(3)	(3)
Other comprehensive losses, net of tax		–	–	–	–	(3)	–	(3)
Total comprehensive losses for the year		–	–	–	–	(3)	(3)	(6)
AT1 distributions paid (net of tax)		–	–	–	–	–	(9)	(9)
Insertion of new parent company		1,099	633	–	–	–	–	1,732
Share capital reduction		(1,011)	–	–	–	–	1,011	–
Capital note issued		–	–	450	–	–	–	450
Transfer from equity based compensation reserve		–	–	–	(4)	–	4	–
Equity based compensation		–	–	–	10	–	–	10
As at 30 September 2016	6.5	88	633	450	6	(3)	1,003	2,177
Profit for the year		–	–	–	–	–	24	24
Other comprehensive income, net of tax		–	–	–	–	1	–	1
Total comprehensive income for the year		–	–	–	–	1	24	25
AT1 distributions paid (net of tax)		–	–	–	–	–	(29)	(29)
Transfer from equity based compensation reserve		–	–	–	(4)	–	4	–
Equity based compensation		–	–	–	6	–	–	6
As at 30 September 2017	6.5	**88**	**633**	**450**	**8**	**(2)**	**1,002**	**2,179**

The notes on pages 244 to 248 form an integral part of these financial statements.

Company statement of cash flows

for the year ended 30 September	2017 £m	2016 £m
Operating activities		
Profit/(loss) on ordinary activities before tax	**29**	(3)
Adjustments for:		
Changes in operating assets		
Due from other banks	**(357)**	(7)
Changes in operating liabilities		
Due to other banks	**55**	36
Other liabilities	**–**	2
Interest receivable	**(25)**	(15)
Interest payable	**27**	16
Net increase in amounts due to related entities	**359**	7
Tax received – Group relief	**3**	–
Net cash provided by operating activities	**91**	36
Cash flows from investing activities		
Investment in controlled entities	**(49)**	(2,184)
Net cash used in investing activities	**(49)**	(2,184)
Cash flows (used in)/from financing activities		
Interest received	**22**	11
Interest paid	**(24)**	(12)
Insertion of a new parent company	**–**	1,732
Issuance of medium-term notes/subordinated debt	**298**	474
Proceeds for issue of other equity instruments	**–**	450
Net decrease in amounts due from related entities	**(296)**	(480)
AT1 distributions	**(36)**	(12)
Net cash (used in)/provided by financing activities	**(36)**	2,163
Net increase in cash and cash equivalents	**6**	15
Cash and cash equivalents at the beginning of the year	**15**	–
Cash and cash equivalents at the end of the year	**21**	15

Cash and cash equivalents comprise the following balances with less than three months' maturity from the date of acquisition.

	2017 £m	2016 £m
Due from related parties (note 6.6)	**21**	15

The notes on pages 244 to 248 form an integral part of these financial statements.

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Section 6: Notes to the Company financial statements

6.1 Company basis of preparation

The Company is incorporated in the UK and registered in England and Wales.

The Company financial statements of CYBG PLC, the Parent Company (the Company), which should be read in conjunction with the Group Directors' Report, have been prepared on a going concern basis in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. No individual income statement or statement of comprehensive income is presented for the Company, as permitted by Section 408 of the Companies Act 2006.

Basis of measurement

The financial information has been prepared under the historical cost convention. The preparation of the financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

The accounting policies of the Company are the same as those of the Group which are set out in the notes to the consolidated financial statements except that the Company has no policy in respect of consolidation. These accounting policies have been applied consistently to all periods presented in these financial statements.

6.2 Company investments in controlled entities

Accounting policy

The Company's investments in controlled entities are valued at cost or valuation less any provision for impairment. Such investments are reviewed annually for potential evidence of impairment, or more frequently when there are indications that impairment may have occurred. Losses relating to impairment in the value of shares in controlled entities are recognised in the income statement.

	2017 £m	2016 £m
At 30 September	**2,249**	2,193

As disclosed in note 3.14 to the consolidated financial statements, the Company has entered into a Conduct Indemnity Deed with NAB. Claims under the Conduct Indemnity Deed are made by the Company, while the provisions in respect of the qualifying conduct costs are raised and incurred by its principal trading subsidiary, Clydesdale Bank PLC. As a consequence, the recognition and measurement basis of the Capped Indemnity in the Company differs from that of the Group. For the Company, the substance of the indemnity agreement is that of variable consideration in relation to its investment in controlled entities.

When a claim is raised under the Capped Indemnity, the Company recognises a receivable from NAB (presented within amounts due from other banks) with a corresponding decrease in the cost of the Company's investments in controlled entities. The Company does not recognise any income or expense in relation to claims under the Capped Indemnity. It is intended that upon collection of the claim proceeds from NAB the capital impact of providing for Relevant Conduct Matters in Clydesdale Bank PLC is mitigated by the Company using the proceeds to subscribe for share capital. During the year ended 30 September 2017 the Company's investments in controlled entities was reduced by £536m (2016: £433m) in relation to Conduct Indemnity adjustments and the Company subscribed for £179m (2016: £426m) of additional share capital in its controlled entities.

Where provisions for Relevant Conduct Matters are increased in respect of a reporting period, but proceeds from that claim are not received from NAB prior to the reporting date, the Company has put in place an agreement with Clydesdale Bank PLC in order to mitigate the effect of capital losses at the end of the reporting period. Upon raising a provision for a Relevant Conduct Matter, the Company indemnifies Clydesdale Bank PLC for the Qualifying Conduct Costs (excluding the Group's loss share) until it subscribes for an equivalent amount of capital in Clydesdale Bank PLC. The Company recognises a capital contribution within investments in controlled entities and a liability in amounts due to other entities in respect of these amounts. This totalled £364m at 30 September 2017 (2016: £7m).

The table below represents the wholly owned subsidiary undertakings of the Group and Company as at 30 September 2017:

Wholly owned subsidiary undertakings	Nature of business	Class of share held	Proportion held	Country of incorporation	Registered office
Direct holdings					
Clydesdale Bank PLC	Banking	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
CYB Investments Limited	Holding company	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
Indirect holdings					
CGF No 9 Limited	Leasing	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
Clydesdale Bank Asset Finance Limited	Leasing	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
Clydesdale Bank (Head Office) Nominees Limited	In liquidation	Limited by guarantee	100%	Scotland	Saltire Court, 20 Castle Terrace, Edinburgh, EH1 2DB
Craig Yr Haul Management Company Limited	Property management	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
CYB Intermediaries Holdings Limited	In liquidation	Ordinary	100%	England	15 Canada Square, London, E14 5GL
CYB Intermediaries Limited	Insurance intermediary	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
CYB Services Limited	In liquidation	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
St Vincent (Equities) Limited	Investment company	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
Yorkshire Bank Home Loans Limited	Mortgage finance	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
11 Tudor Hill Residential Management Company Limited	Dormant	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
CB Nominees Limited	Dormant	Limited by guarantee	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
CYB SSP Trustee Limited	Dormant	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
Linton Springs Residential Management Company Limited	Dormant	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
St Johns Place Residential Management Company Limited	Dormant	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
YCB DC Trustee Limited	Dormant	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
YCBPS Property Nominee Company Limited	Dormant	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
Yorkshire and Clydesdale Bank Pension Trustee Limited	Dormant	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
Yorkshire Bank PLC	Dormant	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ

The Company also has an interest in the Yorkshire and Clydesdale Bank Foundation, a charitable foundation registered in Scotland as a company limited by guarantee. Clydesdale Bank PLC acts as a guarantor for £10 and is the main donor.

Section 6: Notes to the Company financial statements continued

6.2 Company investments in controlled entities continued

All subsidiaries have a 30 September year end with the exception of the following entities:

Wholly owned subsidiary undertakings	Accounting reference date
Craig Yr Haul Management Company Limited	31 January
11 Tudor Hill Residential Management Company Limited	31 December
Linton Springs Residential Management Company Limited	31 December
St Johns Place Residential Management Company Limited	31 December

In addition to the above, the Company also has an interest in a number of structured entities:

Other controlled entities as at 30 September 2017	Nature of business	Country of incorporation	Registered office
Clydesdale Covered Bonds No. 2 LLP	Acquisition of mortgage loans	England	20 Merrion Way, Leeds LS2 8NZ
Lanark Holdings Limited	Holding company	England	Winchester House, Mail Stop 429, 1 Great Winchester Street, London EC2N 2DB
Lanark Trustees Limited	Mortgages trustee	England	Winchester House, Mail Stop 429, 1 Great Winchester Street, London EC2N 2DB
Lanark Funding Limited	Funding company	England	Winchester House, Mail Stop 429, 1 Great Winchester Street, London EC2N 2DB
Lanark Master Issuer PLC	Issuer of securitised notes	England	Winchester House, Mail Stop 429, 1 Great Winchester Street, London EC2N 2DB
Lannraig Holdings Limited	Holding company	England	35 Great St. Helen's, London EC3A 6AP, United Kingdom
Lannraig Trustees Limited	Mortgages trustee	Jersey	44 Esplanade, St Helier, Jersey JE4 9WG, Channel Islands
Lannraig Funding Limited	Funding company	England	35 Great St. Helen's, London EC3A 6AP, United Kingdom
Lannraig Master Issuer PLC	Issuer of securitised notes	England	35 Great St. Helen's, London EC3A 6AP, United Kingdom
Red Grey Square Funding LLP(1)	Security provider	England	35 Great St. Helen's, London EC3A 6AP, United Kingdom

(1) During the year, the Bank sponsored the formation of Red Grey Square Funding LLP for the purpose of entering into the Security Arrangement with the Clydesdale and Yorkshire Bank Pension Scheme (note 5.3).

All of the above structured entities have a financial year end of 30 September.

Details of the Group's interests in consolidated structured entities associated with securitisation and covered bond arrangements are set out in note 3.7.

6.3 Company debt securities in issue

	2017 £m	2016 £m
Subordinated debt	**479**	480
Medium term notes	**300**	–
	779	480

Information on subordinated debt and medium term notes is provided in note 3.15 to the consolidated financial statements.

6.4 Company fair value of financial instruments

Analysis of the fair value disclosures uses a hierarchy that reflects the significance of inputs used in measuring the fair value. The level in the fair value hierarchy within which a fair value measurement is categorised is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. The fair value hierarchy is as follows:

- Level 1 fair value measurements – quoted prices (unadjusted) in active markets for identical financial assets or liabilities.
- Level 2 fair value measurements – inputs other than quoted prices within Level 1 that are observable for the financial asset or liability, either directly (as prices) or indirectly (derived from prices).
- Level 3 fair value measurements – inputs for the financial asset or liability that are not based on observable market data (unobservable inputs).

Fair value of financial instruments carried at amortised cost

The tables below show a comparison of the carrying amounts of financial assets and liabilities measured at amortised cost as reported on the balance sheet and their fair values where these are not approximately equal.

There are various limitations inherent in this fair value disclosure particularly where prices may not represent the underlying value due to dislocation in the market. Not all of the Company's financial instruments can be exchanged in an active trading market.

	30 September 2017					30 September 2016				
			Fair value measurement using:					Fair value measurement using:		
Company	**Carrying value £m**	**Fair value £m**	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets										
Due from related entities	**803**	**819**	**–**	**819**	**–**	498	480	–	480	–
Financial liabilities										
Debt securities in issue	**779**	**795**	**795**	**–**	**–**	480	459	459	–	–

Notes

The Company's fair values disclosed for financial instruments at amortised cost are based on the following methodologies and assumptions:

Amounts due from related entities – The fair value of subordinated debt due from related entities is derived from quoted market prices of the debt security in issue after accounting for differences in credit spread. All other amounts due from related entities are redeemable at call and therefore carrying value approximates fair value.

Debt securities in issue – The fair value of subordinated debt is taken directly from quoted market prices.

6.5 Company reserves

6.5.1 Cash flow hedge reserve

As at 30 September 2017, the cash flow hedge reserve comprised crystallised fair value losses arising from a matured cash flow hedge of £2.5m (2016: £3.3m). This hedge relationship was entered into to mitigate the interest rate risk exposure prior to the issuance of the subordinated debt. The hedge matured at the date of issue. The balance on the cash flow hedge reserve within the statement of changes in equity is net of tax.

The crystallised fair value losses will be amortised from the cash flow hedge reserve to the income statement over the life of the subordinated debt. In respect of this, a £0.8m loss (2016: £0.5m loss) was recycled into the income statement during the year.

6.5.2 Other equity instruments and reserves

Information on other equity instruments and other reserves is provided in note 4.1 to the Group's consolidated financial statements. Included within retained earnings is the profit for the year ended 30 September 2017 of £24m (2016: loss of £3m).

6.5.3 Available distributable items

Distributable reserves are determined as required by the Companies Act 2006 by reference to a company's individual financial statements. At 30 September 2017, the Company had accumulated distributable reserves of £1,002m (2016: £1,003m).

Section 6: Notes to the Company financial statements continued

6.6 Company related party transactions

During the year there have been transactions between the Company, controlled entities of the Company, and other related parties.

The Company receives and provides a range of services from/to its principal subsidiary undertaking, including loans and deposits.

Amounts due from controlled entities of the Company

	2017 £m	2016 £m
Cash and cash equivalents	**21**	15
Subordinated debt	**482**	483
Medium term notes	**300**	–
Total amounts due from related entities	**803**	498

On 22 June 2017, the Company purchased £300m of 8-year, callable, fixed 3.125% medium term notes with a final maturity date of 22 June 2025 from Clydesdale Bank PLC. Medium term notes comprise dated, unsecured loans and are issued by Clydesdale Bank PLC. These securities will, in the event of the winding-up of the issuer, be subordinated to the claims of depositors and all other creditors of the issuer, other than creditors whose claims rank junior to the claims of the holders of the medium term loan liabilities, including those of subordinated debt holders.

On 8 February 2016, the Company purchased £475m of 10-year, callable, fixed 5% subordinated debt with a final maturity date of 9 February 2026 from Clydesdale Bank PLC. Subordinated debt comprises dated, unsecured loan capital and is issued by Clydesdale Bank PLC. These securities will, in the event of the winding-up of the issuer, be subordinated to the claims of depositors and all other creditors of the issuer, other than creditors whose claims rank junior to the claims of the holders of subordinated liabilities.

Amounts due to controlled entities of the Company

	2017 £m	2016 £m
Amounts due in relation to conduct indemnity	**364**	7
Other payables	**2**	–
Total amounts due to related entities	**366**	7

Other related party transactions

As discussed in note 4.2 to the consolidated financial statements, the Group provides share based compensation to employees through a number of schemes, all in relation to shares in the Company. The cost of providing these benefits is recharged to the employing company, Clydesdale Bank PLC. Recharges are calculated based on the fair value of awards expensed in the period in accordance with IFRS 2: 'Share based payments'. The key management personnel of the Company are the key management personnel of the Group, with relevant disclosures given in note 5.3 to the consolidated financial statements. The Company has no employees (2016: Nil).

ADDITIONAL INFORMATION

Measuring financial performance – glossary

Financial performance measures

As highlighted in the Strategic report, the Financial results section and the Risk report, the Group utilises a range of performance measures[1] to assess the Group's performance. These can be grouped under the following headings:

- Profitability;
- Asset quality; and
- Capital optimisation.

The performance measures used are a combination of statutory, regulatory and alternative performance measures; with the type of performance measure used dependent on the component elements and source of what is being measured.

Statutory performance measures (S)
These are used when the basis of the calculation is derived from a measure that is required under generally accepted accounting principles (GAAP). An example of this would be references to earnings per share.

Regulatory performance measures (R)
These are used when the basis of the calculation is required and specified by the Group's regulators. Examples of this would be the leverage ratio and the Tier 1 ratio.

Alternative performance measures (A)
These are used when the basis of the calculation is derived from a non-GAAP measure – also referred to as APMs. Examples of this would be the cost to income ratio and the return on tangible equity.

Where a performance measure refers to an 'underlying' metric, the detail on how this measure is arrived at, along with management's reasoning for excluding the item from the Group's current underlying performance rationale, can be found on page 252, directly following this section. These adjustments to the Group's statutory results made by management are necessary to provide a more meaningful underlying basis.

Descriptions of the performance measures used, including the basis of calculation where appropriate, are set out below:

Profitability:

Term	Type	Definition
Net interest margin **(NIM)**	**A**	Net interest income as a percentage of average interest earning assets for a given period. Net interest income of £844m (2016: £806m) is divided by average interest earning assets for a given period of £37,697m (2016: £36,257m) (which is then adjusted to exclude short-term repos used for liquidity management purposes, amounts received under the Conduct Indemnity and not yet utilised, and any associated income). As a result of the exclusions noted above, average interest earning assets used as the denominator have reduced by £491m (2016: £698m) and the net interest income numerator has reduced by £1.1m (2016: £2.6m).
Underlying return on tangible equity **(RoTE)**	**A**	Underlying profit after tax less preference share and other distributions as a percentage of average tangible equity (total equity less intangible assets and AT1) for a given period.
Underlying cost to income ratio **(CIR)**	**A**	Underlying total operating expenses as a percentage of underlying total operating income for a given period.
Underlying basic earnings per share **(EPS)**	**A**	Underlying profit/(loss) attributable to ordinary equity shareholders including tax relief on any distributions made to other equity holders divided by the weighted average number of ordinary shares in issue for a given period.
Statutory RoTE	**A**	Statutory profit/(loss) after tax less preference share and non-controlling interest distributions as a percentage of average tangible equity (total equity less intangible assets and AT1) for a given period.
Statutory CIR	**A**	Statutory total operating expenses as a percentage of total operating income for a given period.
Statutory basic EPS	**S**	Statutory profit/(loss) attributable to ordinary equity shareholders including tax relief on any distributions made to other equity holders divided by the weighted average number of ordinary shares in issue for a given period.

(1) The term 'financial performance measure' covers all metrics, ratios and percentage calculations used to assess the Group's performance and is interchangeable with similar terminology used in the Annual Report and Accounts such as highlights, key metrics, key performance indicators (KPIs) and key credit metrics.

Asset quality:

Term	Type	Definition
Impairment charge to average customer loans **(cost of risk)**	**A**	Impairment losses on credit exposures plus credit risk adjustment on fair value loans to average customer loans (defined as loans and advances to customers, other financial assets at fair value and due from customers on acceptances).
90+ days past due **(DPD)** plus impaired assets to customer loans	**A**	Customer loans that are either impaired or where the repayment is more than 90 days overdue as a percentage of total customer loans at a given date.
Specific provision to gross impaired assets	**A**	The specific impairment provision on credit exposures as a percentage of gross impaired assets at a given date.
Total provision to customer loans	**A**	Total impairment provision on credit exposures as a percentage of total customer loans at a given date.
Indexed loan to value **(LTV)** of the mortgage portfolio	**A**	The mortgage portfolio weighted by balance and indexed using the MIAC Acadametrics indices at a given date.
Net write offs to customer loans	**A**	Net write offs, including loans at fair value, as a percentage of total customer loans at a given date.

Capital optimisation:

Term	Type	Definition
Common Equity Tier 1 **(CET1)** ratio	**R**	CET1 capital divided by RWAs at a given date.
Tier 1 ratio	**R**	Tier 1 capital as a percentage of risk-weighted assets.
Total capital ratio	**R**	Total capital resources divided by risk-weighted assets at a given date.
Leverage ratio	**R**	This is a regulatory standard ratio proposed by the Basel III as a supplementary measure to the risk based capital requirements. It is intended to constrain the build-up of excess leverage in the banking sector and is calculated by dividing Tier 1 capital resources by a defined measure of on and off-balance sheet items plus derivatives.
Modified leverage ratio	**R**	The Group's leverage ratio on a modified basis, excluding qualifying central bank claims from the exposure measure in accordance with the policy statement issued by the PRA in October 2017.
Tangible net asset value **(TNAV)** per share	**A**	Tangible equity as at the period end divided by the closing number of ordinary shares.
Loan to deposit ratio **(LDR)**	**R**	Customer loans as a percentage of customer deposits at a given date.
Liquidity coverage ratio **(LCR)**	**R**	Measures the surplus (or deficit) of the bank's high quality liquid assets relative to weighted net stressed cash outflows over a 30 day period. It assesses whether the bank has sufficient liquid assets to withstand a short-term liquidity stress based on cash outflow assumptions provided by regulators.
Net stable funding ratio **(NSFR)**	**R**	The total amount of available stable funding divided by the total amount of required stable funding, expressed as a percentage. The Group monitors the NSFR based on its own interpretations of current guidance available for CRD IV NSFR reporting. Therefore, the reported NSFR may change over time with regulatory developments. Due to possible differences in interpretation of the rules, the Group's ratio may not be directly comparable with those of other financial institutions.

The Group no longer reports Return on Assets (statutory and underlying basis) as a financial performance measure. Other measures presented, such as RoTE, are considered more relevant and useful for assessing profitability.

Measuring financial performance – glossary

Underlying adjustments to the statutory view of performance

In arriving at an underlying basis, the effects of certain items that do not promote an understanding of historical or future trends of earnings or cash flows are removed; with management believing this presents a set of results that provide a more reflective year-on-year comparison. These items are:

Item	FY2017 £m	FY2016 £m	Description	Reason for exclusion from the Group's current underlying performance
Conduct charges	(58)	(51)	These are customer redress and associated costs arising from legacy products and past sales practices.	These costs are historical in nature and are not indicative of the Group's current underlying performance.
Restructure expense	(67)	(45)	Restructuring of the business is currently ongoing with costs including redundancy payments, property vacation costs and associated enablement costs.	These costs are significant and are part of the Group's strategic objective in simplifying and streamlining operations and processes to enhance productivity. Consequently, this expense is not viewed as a normal ongoing operating cost to the Group.
Separation costs	(8)	(11)	Costs incurred directly relating to the demerger from NAB.	Specific costs relating to the demerger from NAB are historic and not indicative of the Group's current underlying performance.
Net gains on debt restructuring	–	1	These are the net gains arising on the repurchase of subordinated debt from NAB at the time of the demerger.	Losses or gains from one-off or infrequent transactions, such as those rising from debt restructures, are not indicative of the Group's current underlying performance.
Impairment of intangible assets	–	(45)	This relates to the impairment of historic development costs and legacy software developed pre demerger.	Specific costs (or gains) relating to the demerger from NAB are historic and not indicative of the Group's current underlying performance. This includes the impact on the impairment of legacy intangible assets where post demerger, the Group had greater flexibility in its digital direction.
Gain on disposal of VocaLink/ Visa share	20	7	A one-off gain recognised on the disposal of the Group's VocaLink and Visa Europe Limited share.	Losses or gains from one-off or infrequent transactions are not indicative of the Group's current underlying performance.
Gain on DB pension scheme reforms	88	–	A one-off gain on the closure of the defined benefit pension scheme to future accrual for the majority of members	Losses or gains from one-off or infrequent transactions are not indicative of the Group's current underlying performance.

Glossary

Term	Definition
Additional Tier 1 securities **(AT1)**	Securities that are considered additional Tier 1 capital in the context of CRD IV.
Arrears	A customer is in arrears when they fail to adhere to their contractual payment obligations resulting in an outstanding loan that is unpaid or overdue.
Average assets	Represents the average of assets over the year adjusted for any disposed operations.
B	The Group's digital application suite, offering Retail customers money management capabilities across Web, Android and Apple platforms.
Bank	Clydesdale Bank PLC.
Bank levy	Applicable to certain UK financial institutions and UK operations of foreign banks from 1 January 2011. The amount due is based on a percentage of the chargeable equity and liabilities for each applicable entity as at the balance sheet date.
Bank surcharge	Introduced by the Finance Act (No2) 2015 for the Group's banking entity from 1 January 2016 and is an 8% charge on taxable profits over £25m before the offset of brought forward losses or Group relief.
Basel II	The capital adequacy framework issued by the BCBS in June 2006 defining how firms should calculate their regulatory capital requirements.
Basel III	Reforms issued by the BCBS in December 2010 to strengthen global capital and liquidity rules with the goal of promoting a more resilient banking sector. In Europe the new requirements were implemented by 'CRD IV', on a phased basis from 1 January 2014 with full implementation by 1 January 2019.
Basis points **(bps)**	One hundredth of a percent (0.01%); meaning that 100 basis points is equal to 1%. This term is commonly used in describing interest rate movements.
Board	Refers to the CYBG PLC Board or the Clydesdale Bank PLC Board as appropriate.
Capped Indemnity	The indemnity from NAB in favour of CYBG PLC in respect of certain qualifying conduct costs incurred by CYBG Group, which is capped at the 'Capped Indemnity Amount', subject to the 'Loss Sharing Arrangement', under the terms of the 'Conduct Indemnity Deed'.
Capped Indemnity Amount	An amount equal to £1.58bn less any 'Pre Covered provision amount'.
Carrying value (also referred to as carrying amount)	The value of an asset or a liability in the balance sheet based on either amortised cost or fair value principles.
Collateral	The assets of a borrower that are used as security against a loan facility.
Collateral Account	A cash deposit with the BoE in an amount equal to the Unutilised Indemnity Amount from time to time used to collateralise certain obligations of NAB under the Capped Indemnity.
Collective impairment provision	Impairment assessment on a collective basis for homogeneous groups of loans that are not considered individually significant and to cover losses which have been incurred but have not yet been identified on loans subject to individual assessment.
Commercial paper	An unsecured promissory note issued to finance short-term credit requirements. These instruments have a specified maturity date and stipulate the face amount to be paid to the investor on that date.
Common Equity Tier 1 capital **(CET1)**	The highest quality form of regulatory capital that comprises total shareholders' equity and related non-controlling interests, less goodwill and intangible assets and certain other regulatory adjustments.
Company	CYBG PLC.
Conduct Indemnity Deed	The deed between NAB and CYBG PLC setting out the terms of: – The 'Capped Indemnity'; and – Certain arrangements for the treatment and management of certain 'Conduct Matters'.
Conduct Matters	In the context of the 'Conduct Indemnity Deed', conduct issues relating to PPI, standalone 'IRHP', voluntary scope TBLs and FRTBLs and other conduct matters in the period prior to the demerger date whether or not known at the 'demerger date'.
Conduct risk	The risk of treating customers unfairly and/or delivering inappropriate outcomes resulting in customer detriment, regulatory fines, compensation, redress costs and reputational damage.
Contractual maturities	The date on which the final payment of any financial instrument is due to be paid or received, at which point all the remaining outstanding principal and interest have been repaid in full.

Glossary

Term	Definition
Counterparty	The other party that participates in a financial transaction, with every transaction requiring a counterparty in order for the transaction to complete.
Covered bonds	A corporate bond with primary recourse to the institution and secondary recourse to a pool of assets that act as security for the bonds on issuer default. Covered bonds remain on the issuer's balance sheet and are a source of term funding for the Group.
CRD IV	European legislation to implement Basel III. It replaces earlier European capital requirements directives with a revised package consisting of a new Capital Requirements Directive and a new Capital Requirements Regulation. CRD IV sets out capital and liquidity requirements for European banks and harmonises the European framework for bank supervision. See also 'Basel III'.
CRD V	A set of proposals issued by the European Commission including amendments of (among other things) the existing Capital Requirements Directive and Capital Requirements Regulation. See also 'CRD IV'.
Credit risk adjustment/credit valuation adjustment	An adjustment to the valuation of financial instruments held at fair value to reflect the creditworthiness of the counterparty.
Customer deposits	Money deposited by individuals and corporate entities that are not credit institutions, and can be either interest bearing, non-interest bearing or term deposits.
Default	A customer is in default when either they are more than 90 days past due on a credit obligation to the Group, or are considered unlikely to pay their credit obligations in full without recourse to actions such as realisation of security (if held).
Delinquency	See 'Arrears'.
Demerger	The demerger of CYBG Group from NAB pursuant to which all of the issued share capital of CYBI Limited was transferred to CYBG PLC by NAB in consideration for the issue and transfer of CYBG shares to NAB in part for the benefit of NAB (which NAB subsequently sold pursuant to the IPO) and in part for the benefit of NAB shareholders under a scheme of arrangement.
Demerger date	8 February 2016
Derivative	A financial instrument that is a contract or agreement whose value is related to the value of an underlying instrument, reference rate or index.
Earnings at risk **(EaR)**	A measure of the quantity by which net interest income might change in the event of an adverse change in interest rates.
Effective interest rate method	The method used to measure the carrying value of certain financial instruments which amortises the relevant fees over the expected life of the instrument.
Effective tax rate	The tax charge in the statutory income statement as a percentage of the statutory profit before tax.
Encumbered assets	Assets that have been pledged as security, collateral or legally 'ring fenced' in some other way which prevents those assets being transferred, pledged, sold or otherwise disposed.
Exposure	A claim, contingent claim or position which carries a risk of financial loss.
Fair value	The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions.
Fair value adjustment	An adjustment to the fair value of a financial instrument which is determined using a valuation technique (Level 2 and Level 3) to include additional factors that would be considered by a market participant that are not incorporated within the valuation model.
Financial Ombudsman Service **(FOS)**	An independent body set up by the UK Parliament to resolve individual complaints between financial businesses and their customers.
Financial Services Compensation Scheme **(FSCS)**	The UK's compensation fund of last resort for customers of authorised financial services firms and is funded by the financial services industry. The FSCS may pay compensation if a firm is unable, or likely to be unable, to pay claims against it. This is usually because it has stopped trading or has been declared in default.
FINREP	A standardised Financial Reporting framework mandated by the EBA. Its aim is to establish a single rule book to ensure a robust and uniform regulatory framework.

Term	Definition
Forbearance	The term generally applied to the facilities provided or changes to facilities provided to assist borrowers, both retail and SME, who are experiencing, or are about to experience, a period of financial stress.
Forborne non-performing loans	Loans to which forbearance measures have been granted and which are more than 90 DPD, or where the debtor is assessed as unlikely to pay its credit obligations in full without realisation of collateral, regardless of the existence of any past-due amount or of the number of DPD.
Forborne performing loans	Loans to which forbearance measures have been granted and which are up to 90 DPD and do not otherwise meet the criteria of forborne non-performing loans.
Funding risk	A form of liquidity risk arising when the liquidity needed to fund illiquid asset positions cannot be obtained at the expected terms and when required.
Group	CYBG and its controlled entities.
Hedge ineffectiveness	Represents the extent to which the income statement is impacted by changes in fair value or cash flows of hedging instruments not being fully offset by changes in fair value or cash flows of hedged items.
Housing lending	Mortgages secured by residential properties as collateral.
iB	The Group's IT digital platform, built on an open architecture framework providing integration and connectivity for our customer systems, applications and technology partners.
IFRS 9	The new financial instrument accounting standard which is applicable for accounting periods beginning on or after 1 January 2018, which the Group will adopt from 1 October 2018.
Impaired loans	Loans in arrears with insufficient security to cover principal and arrears of interest revenue or where there is sufficient doubt about the ultimate collectability of principal and interest.
Impairment allowances	A provision held on the balance sheet to recognise that a loan is impaired. This can be calculated at either the individual or collective level.
Impairment losses	Where an asset's recoverable amount is less than its carrying value and the difference is recognised in the income statement with the carrying value of the asset reduced by creating an impairment allowance. This can be assessed at either the individual or collective level.
Interest rate hedging products **(IRHP)**	This incorporates: (i) standalone hedging products identified in the Financial Services Authority (FSA) 2012 notice; (ii) the voluntary inclusion of certain of the Group's more complex tailored business loan (TBL) products; and (iii) the Group's secondary review of all fixed-rate tailored business loans (FRTBLs) complaints which were not in scope for the FSA notice.
Internal Capital Adequacy Assessment Process **(ICAAP)**	The Group's assessment of the levels of capital that it needs to hold through an examination of its risk profile from regulatory and economic capital viewpoints.
Internal Liquidity Adequacy Assessment Process **(ILAAP)**	The Group's assessment and management of balance sheet risks relating to funding and liquidity.
Internal ratings-based approach **(IRB)**	A method of calculating credit risk capital requirements using internal, rather than supervisory, estimates of risk parameters.
Investment grade	The highest possible range of credit ratings, from 'AAA' to 'BBB', as measured by external credit rating agencies.
'Jaws'	The net difference between movements in total income and underlying costs for the period expressed as a percentage.
Level 1 fair value measurements	Financial instruments whose fair value is derived from unadjusted quoted prices for identical instruments in active markets.
Level 2 fair value measurements	Financial instruments whose fair value is derived from quoted prices for similar instruments in active markets and financial instruments valued using models where all significant inputs are observable.
Level 3 fair value measurements	Financial instruments whose fair value is derived from valuation techniques where one or more significant inputs are unobservable.

Glossary

Term	Definition
Listing Rules	Regulations applicable to any company listed on a United Kingdom stock exchange, subject to the oversight of the UK Listing Authority (UKLA). The Listing Rules set out mandatory standards for any company wishing to list its shares or securities for sale to the public.
Loan to value ratio **(LTV)**	A ratio that expresses the amount of a loan as a percentage of the value of the property on which it is secured.
Loss Share	The percentage of a provision raised or an increase in a provision which CYBG PLC will be responsible for under the 'Conduct Indemnity Deed'. Fixed at 9.7% at the demerger date.
Loss Sharing Arrangement	The arrangement relating to the 'Capped Indemnity' pursuant to which CYBG PLC will be responsible for the 'Loss Share'.
Medium Term Notes	Debt instruments issued by corporates, including financial institutions, across a range of maturities.
Minimum requirement for own funds and eligible liabilities **(MREL)**	MREL is a minimum requirement for institutions to maintain equity and eligible debt liabilities, to help ensure that when an institution fails the resolution authority can use these financial resources to absorb losses and recapitalise the continuing business. The BoE set out its approach to setting banks' MREL in November 2016.
Net interest income	The amount of interest received or receivable on assets, net of interest paid or payable on liabilities.
Net promoter score **(NPS)**	This is an externally collated customer loyalty metric that measures loyalty between a Provider, who in this context is the Group, and a consumer.
Non-impaired assets 90+ DPD	Consist of well-secured assets that are more than 90 DPD and portfolio-managed facilities that are not well secured and are between 90 and 180 DPD.
Operational risk	The risk of loss resulting from inadequate or failed internal processes, people strategies and systems or from external events.
Overall Liquidity Adequacy Rule **(OLAR)**	An FCA and PRA rule that firms must at all times maintain liquidity resources which are adequate both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due. This is included in the Group's 'Risk Appetite' and subject to approval by the Board as part of the 'ILAAP'.
Past due loans and advances	Loans and advances on which repayments are overdue.
Pension risk	The risk that, at any point in time, the available assets to meet pension liabilities are at a value below current and future scheme obligations.
PPI redress	Includes PPI customer redress and all associated costs excluding fines.
Pre Covered provision amount	The amount of any provision(s) relating to 'Conduct Matters' raised or increased by CYBG Group between 31 March 2015 and the 'demerger date' in respect of which NAB has provided specific support at any time after 31 March 2015 but before the 'demerger date'. This was £465m at the 'demerger date'.
Probability of default **(PD)**	The probability that a customer will default (usually within a one-year time horizon); although the time horizon will change on 1 October 2018 in line with IFRS 9 requirements.
Property revaluation	Represents revaluation increments and decrements of land and buildings based on Directors' valuations to reflect fair value.
Regulatory capital	The capital which the Group holds, determined in accordance with rules established by the PRA.
Residential mortgage-backed securities **(RMBS)**	Securities that represent interests in groups or pools of underlying mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and principal).

Term	Definition
Restructured loans	A restructured loan is where the terms and conditions of a loan contract have been varied that may involve one or both of the following: – the original scheduled repayment contract has been re-written by changing the frequency and pattern of repayments with a lengthening of the final repayment/ maturity profile on a non-commercial basis (e.g. non-market extension of principal repayment period); – the Group has previously made a specific provision for the customer and written off the debt in part or converted the debt to a changed obligation in exchange for realisable assets not previously held or a debt for equity swap. See also 'forbearance'.
Retail lending	Lending to individuals rather than institutions. This includes both secured and unsecured lending such as personal loans, residential and BTL mortgages, overdrafts and credit card balances.
Ring fencing	A new regime of rules which require banks to change the way that they are structured by separating retail banking services from investment and international banking. This is to ensure the economy and taxpayers are protected in the event of any future financial crises.
Risk appetite	The level and types of risk the Group is willing to assume within the boundaries of its risk capacity to achieve its strategic objectives.
Risk-weighted assets **(RWA)**	On and off balance sheet assets of the Group are allocated a risk weighting based on the amount of capital required to support the asset.
Sale and repurchase agreement ('repo')	A short-term funding agreement that allows a borrower to create a collateralised loan by selling a financial asset to a lender. As part of the agreement, the borrower commits to repurchase the security at a date in the future repaying the proceeds of the loan. For the counterparty (buying the security and agreeing to sell in the future) it is a reverse repurchase agreement or a reverse repo.
Scheme of arrangement	A scheme of arrangement under Part 5.1 of the Australian Corporations Act between NAB and NAB shareholders to effect the demerger.
Scheme	The Groups defined benefit pension scheme, the Yorkshire and Clydesdale Bank Pension Scheme.
Secured lending	Lending in which the borrower pledges some asset (e.g. property) as collateral for the lending.
Securitisation	The practice of pooling similar types of contractual debt and packaging the cash flows from the financial asset into securities that can be sold to institutional investors in debt capital markets. It provides the Group with a source of secured funding than can achieve a reduction in funding costs by offering typically 'AAA' rated securities secured by the underlying financial asset.
SME lending	Lending to non-retail customers, including overdrafts, asset and lease financing, term lending, bill acceptances, foreign currency loans, international and trade finance, securitisation and specialised finance.
Sovereign exposures	Exposures to governments, ministries, departments of governments, embassies, consulates and exposures on account of cash balances and deposits with central banks.
Specific impairment provision	A specific provision relates to a specific loan, and represents the estimated shortfall between the carrying value of the asset and the estimated future cash flows, including the estimated realisable value of securities after meeting securities realisation costs.
Standardised approach	In relation to credit risk, a method for calculating credit risk capital requirements using External Credit Assessment Institutions (ECAI) ratings and supervisory risk weights. In relation to operational risk, a method of calculating the operational capital requirement by the application of a supervisory defined percentage charge to the gross income of eight specified business lines.
Stress testing	The term used to describe techniques where plausible events are considered as vulnerabilities to ascertain how this will impact the own funds or liquidity which a bank holds.

Glossary

Term	Definition
Structured entities **(SE)**	An entity created to accomplish a narrow well-defined objective (e.g. securitisation of financial assets). An SE may take the form of a corporation, trust, partnership or unincorporated entity. SEs are often created with legal arrangements that impose strict limits on the activities of the SE. May also be referred to as an SPV.
Subordinated debt	Liabilities which rank after the claims of other creditors of the issuer in the event of insolvency or liquidation.
Term Funding Scheme **(TFS)**	Launched in 2016 by the BoE to allow banks and building societies to borrow from the BoE at rates close to base rate. This is designed to increase lending to businesses by lowering interest rates and increasing access to credit.
Tier 1 capital	A measure of a bank's financial strength defined by CRD IV. It captures Common Equity Tier 1 capital plus other Tier 1 securities in issue, subject to deductions.
Tier 2 capital	A component of regulatory capital, including qualifying subordinated debt, eligible collective impairment allowances and other Tier 2 securities as defined by CRD IV.
Unaudited/unverified	Financial information that has not been subject to validation by the Group's external auditor.
Unsecured lending	Lending in which the borrower pledges no assets as collateral for the lending (such as credit cards and current account overdrafts).
Unutilised Covered Amount	The amount of any unutilised accounting provision in the accounts of a member of the Group for matters covered by the Capped Indemnity to the extent indemnified by NAB pursuant to the Capped Indemnity or covered by an amount of a released or reduced provision, interest or tax deduction applied or required to be applied against such provision pursuant to the Conduct Indemnity.
Unutilised Indemnity Amount	The amount of support available pursuant to the Capped Indemnity at any given time following the demerger of the Group from NAB.
Value at risk **(VaR)**	A measure of the loss that could occur on risk positions as a result of adverse movements in market risk factors (e.g. rates, prices, volatilities) over a specified time horizon and to a given level of confidence.
Write down	A reduction in the carrying value of an asset due to impairment or adverse fair value movements.

Abbreviations

ALCO	Assets and Liabilities Committee
ASX	Australian Securities Exchange
AT1	Additional Tier 1
BCBS	Basel Committee on Banking Supervision
BoE	Bank of England
bps	Basis points
BTL	Buy-to-let mortgages
CAGR	Compound Annual Growth Rate
CCB	Capital Conservation Buffer
CCyB	Countercyclical Capital Buffer
CET1	Common Equity Tier 1 Capital
CIR	Cost to income ratio
CMA	Competition and Markets Authority
CPI	Consumer Prices Index
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
DB	Defined benefit
DPD	Days past due
DTR	Disclosure and Transparency Rules
EAD	Exposure at Default
EaR	Earnings at risk
eCRS	electronic Customer Rating System
EPS	Earnings per share
FCA	Financial Conduct Authority.
FPC	Financial Policy Committee
FRC	Financial Reporting Council
FSCS	Financial Services Compensation Scheme
FTE	Full time equivalent
GHG	Greenhouse Gases
HMRC	Her Majesty's Revenue and Customs
IAS	International Accounting Standards
IASB	International Accounting Standards Board
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standards
ILAAP	Internal Liquidity Adequacy Assessment Process
IPO	Initial Public Offering
IRB	Internal ratings-based
IRHP	Interest rate hedging products
IRRBB	Interest rate risk in the banking book
ISDA	International Swaps and Derivatives Association
LCR	Liquidity coverage ratio
LDR	Loan to deposit ratio
LGD	Loss Given Default
LIBOR	London Interbank Offered Rate.
LSE	London Stock Exchange
LTIP	Long term incentive plan
LTV	Loan to value
MREL	Minimum Requirement for Own Funds and Eligible Liabilities
MRT	Material Risk Takers
NAB	National Australia Bank
NIM	Net interest margin
NPS	Net promoter score
NSFR	Net stable funding ratio
OLAR	Overall liquidity adequacy rule
PBT	Profit before tax
PCA	Personal current accounts
PD	Probability of Default
PPI	Payment protection insurance
PRA	Prudential Regulation Authority
RAS	Risk Appetite Statement
RMBS	Residential mortgage-backed securities
RMF	Risk Management Framework
RoTE	Return on Tangible Equity
RPI	Retail Price Index
RWA	Risk weighted assets
SME	Small or medium sized enterprises
SRB	Systemic Risk Buffer
TCC	Transactional Credit Committee
TFS	Term Funding Scheme
TNAV	Tangible net asset value
TSA	Transitional Services Agreements
VaR	Value at risk

Country by country reporting

The Capital Requirements (Country-by-Country Reporting) Regulations 2013 came into effect on 1 January 2014 and place certain reporting obligations on financial institutions that are within the scope of the European Union's Capital Requirements Directive (CRD IV). The purpose of the Regulations is to provide clarity on the source of the Group's income and the locations of its operations.

The vast majority of entities that are consolidated within the Group's financial statements are UK registered entities. The activities of the Group are described in the Strategic report.

The total operating income and the average number of FTE employees during the year to 30 September 2017 were:

	2017 UK
Average FTE employees (number)	**6,040**
Total operating income (£m)	**1,036**
Profit before tax (£m)	**268**
Corporation tax paid (£m)	**–**
Public subsidies received (£m)	**–**

The only other non-UK registered entity of the Group is a Trustee company that is part of the Group's securitisation vehicles (Lanark and Lannraig). Lannraig Trustees Limited is registered in Jersey. This entity plays a part in the overall securitisation process by having the beneficial interest in certain mortgage assets assigned to it. This entity has no assets or liabilities recognised in its financial statements with the securitisation activity taking place in other UK registered entities of the structures. This entity does not undertake any external economic activity and has no employees. The results of this entity as well as those of the entire Lanark and Lannraig securitisation structures are consolidated in the financial statements of the Group.

Shareholder information

Annual general meeting (AGM)

The AGM of the Company will be held at 10am (GMT) on Wednesday 31 January 2018 at the offices of Pinsent Masons LLP, 30 Crown Place, Earl Street, London, EC2A 4ES, United Kingdom. The Notice of AGM can be found on the CYBG PLC website www.cybg.com.

Shareholder enquiries

The Company's share register is maintained by the Company's Registrar, Computershare. Shareholders with queries relating to their shareholding should contact Computershare directly using one of the methods below:

Registrar

Computershare UK
Computershare Investor Services PLC
The Pavilions
Bridgwater Road
Bristol
United Kingdom BS99 6ZZ

Tel within UK – 0370 707 1172
Tel outside UK – +44 370 707 1172
Email: www.investorcentre.co.uk/contactus
Web: www.investorcentre.co.uk

Computershare Australia
Computershare Investor Services Pty Limited
Yarra Falls
452 Johnston Street
Abbotsford VIC 3067
Australia

Tel within Australia – 1800764308
Tel outside Australia – 03 9415 4142
Email: www.investorcentre.com/contact
Web: www.investorcentre.com/au

Duplicate shareholder accounts

If you receive more than one copy of Company mailings this may indicate that more than one account is held in your name on the register. This happens when the registration details of separate transactions differ slightly. If you believe more than one account exists in your name you may contact the Company's Registrar, Computershare, to request that the accounts are combined. There is no charge for this service.

Electronic communications

CYBG PLC uses its website (www.cybg.com) as its primary means of communication with its shareholders provided that the shareholder has agreed or is deemed to have agreed that communications may be sent or supplied in that manner. Electronic communications allow shareholders to access information instantly as well as helping the Company reduce its costs and its impact on the environment. Shareholders who have consented or are deemed to have consented to electronic communications can revoke their consent at any time by contacting the Company's Registrar, Computershare.

Shareholders can sign up for electronic communications online via the following links:

Holders of shares on the London Stock Exchange:
www.investorcentre.co.uk/ecomms

Holders of CDIs on the Australian Securities Exchange:
www.investorcentre.com/au

Corporate website

Information on the Company is available at the CYBG PLC website (www.cybg.com) including:

- Financial information – annual and half-yearly reports as well as trading updates;
- Share price information – current trading details and historical charts;
- Shareholder information – investor presentations and share register profile;
- News releases – current and historical.

Unsolicited telephone calls and communication

Shareholders are advised to be wary of any unsolicited advice, offers to buy shares at a discount, or offers of free reports about the Company. These are typically from overseas based 'brokers' who target shareholders, offering to sell them what often turns out to be worthless or high risk shares. These operations are commonly known as 'boiler rooms' and the 'brokers' can be very persistent and extremely persuasive.

Shareholders are advised to deal with only financial services firms that are authorised by the FCA. You can check a firm is properly authorised by the FCA before getting involved by visiting www.fca.org.uk/register. If you do deal with an unauthorised firm, you will not be eligible to receive payment under the Financial Services Compensation Scheme if anything goes wrong. For more detailed information on how you can protect yourself from an investment scam, or to report a scam, go to www.fca.org.uk/consumers/report-scam-unauthorised-firm.

Shareholder information

Shareholder interests as at 30 September 2017

By size of holding

Range	No. of shareholders	%	No. of shares	%
1–1,000	164,561	82.66	55,671,494	6.3
1,001–5000	29,868	15	58,880,465	6.66
5,001–10,000	2,863	1.44	19,986,937	2.26
10,001–100,000	1,611	0.81	35,298,906	3.99
100,001–999,999,999	187	0.09	713,768,264	80.78
Totals	199,090	100.00	883,606,066	100.00

Proposed financial calendar

Q1 Trading update	30 January 2018
Annual General Meeting	31 January 2018
Interim results announcement	15 May 2018
Q3 Trading update	2 August 2018
Full year results announcement	20 November 2018

Forward-looking statements

The information in this document may include forward looking statements, which are based on assumptions, expectations, valuations, targets, estimates, forecasts and projections about future events. These can be identified by the use of words such as 'expects', 'aims', 'targets', 'seeks', 'anticipates', 'plans', 'intends', 'prospects' 'outlooks', 'projects', 'believes', 'estimates', 'potential', 'possible', and similar words or phrases. These forward looking statements, as well as those included in any other material discussed at any presentation, are subject to risks, uncertainties and assumptions about the Group and its securities, investments and the environment in which it operates, including, among other things, the development of its business and strategy, trends in its operating industry, changes to customer behaviours and covenant, macroeconomic and/or geopolitical factors, changes to its board and/or employee composition, exposures to terrorist activity, IT system failures, cyber-crime, fraud and pension scheme liabilities, changes to law and/or the policies and practices of the BoE, the FCA and/or other regulatory bodies, inflation, deflation, interest rates, exchange rates, changes in the liquidity, capital, funding and/or asset position and/or credit ratings of the Group, the repercussions of the UK's referendum vote to leave the European Union, and future capital expenditures and acquisitions.

In light of these risks, uncertainties and assumptions, the events in the forward looking statements may not occur. Forward looking statements involve inherent risks and uncertainties. Other events not taken into account may occur and may significantly affect the analysis of the forward looking statements. No member of the Group or their respective directors, officers, employees, agents, advisers or affiliates gives any assurance that any such projections or estimates will be realised or that actual returns or other results will not be materially lower than those set out in this document and/or discussed at any presentation. All forward looking statements should be viewed as hypothetical. No representation or warranty is made that any forward looking statement will come to pass. No member of the Group or their respective directors, officers, employees, agents, advisers or affiliates undertakes any obligation to update or revise any such forward looking statement following the publication of this document nor accepts any responsibility, liability or duty of care whatsoever for (whether in contract, tort or otherwise) or makes any representation or warranty, express or implied, as to the truth, fullness, fairness, merchantability, accuracy, sufficiency or completeness of, the information in this document.

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WE ARE PROUD TO HAVE
BEEN SERVING OUR
CUSTOMERS AND COMMUNITIES
FOR OVER 175 YEARS

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