PILLAR 3 DISCLOSURES

2016

Our first year as an
independent company

30 SEPTEMBER 2016

CYBG PLC

CONTENTS

1.1 Introduction

This document presents the consolidated Pillar 3 disclosures of CYBG PLC (formerly known as Pianodove PLC) and its controlled entities ("the Group") as at 30 September 2016. On 8 February 2016, CYBG PLC became the new holding company for the CYB Investments Limited ("CYBI") Group and listed on the London Stock Exchange ("LSE") and the Australian Securities Exchange ("ASX"). As a result we became an independent company for the first time since the 1920s.

This report should be read in conjunction with the CYBG PLC Annual Report and Accounts. The Group comparative figures provided are those of the CYBI Group.

The analysis provided within the Pillar 3 disclosures provide detail on aspects of the Group's risk profile and, along with detail on the Risk Management Framework ("RMF") supports the Group's position as a strongly capitalised firm which employs robust systems and processes in order to assess, manage and mitigate risk.

1.2 Our business model and strategic priorities

Our business model

Our strategy is clear and its execution allows us to create value for our stakeholders through:

- Life-long customer relationships built on trust and confidence.
- Segment and value-led approach to new customer acquisition and proposition development.
- Holistic balance sheet management approach, focus on sustainable growth within prudent risk appetite.
- Capturing increasing organisational efficiencies: rightsizing our network, automation of processes, digitisation of customer journeys, increasing operating model productivity.
- Optimisation of capital allocation within an improved risk management framework.

...by offering customers:

- Full service retail and SME banking propositions to a growing customer franchise, supported by well established, respected brands.
- Simple, straightforward financial products supported by great customer service.
- An increasingly integrated omni-channel distribution model that provides customers with seamless access to relevant information, services and products via mobile, online telephone banking and across our branch and advisor network.

...leveraging our competitive advantages:

- Established, trusted brands that resonate in our core regions.
- Highly engaged colleagues focused on customer service.
- New, highly experienced and energised leadership team and Board members.
- Strong and enduring relationships with customers and intermediary brokers.
- Resilient customer deposit franchise providing low cost, sustainable funding.
- New cutting edge, scalable digital platform underpinning distribution plans.
- Scale and scope of large incumbent players with the agility of much smaller UK challenger banks.

Our strategy is underpinned by the Group's core business strengths:

- Long established franchise in core regional and selected national markets;
- Standalone, scalable and full service operating platform;
- Simple, low risk banking model;
- High-quality balance sheet, set within a strong risk management framework;
- Resilient and strongly capitalised balance sheet;
- Clear strategy to drive growth and returns;
- Sector expertise; and
- Experienced Executive Leadership Team.

Our strategic priorities

The Group is committed to delivering a strong, customer centric banking proposition in the UK.

We believe customers want straightforward and transparent products combined with the ability to access their products and services through the channel of their choice. Service remains one of the key drivers of customer satisfaction with customers increasingly less forgiving of poor service. Demand for omni-channel banking is established and customers expect to be able to manage their finances whenever and wherever is most suitable for them, whether by telephone, online, or by using their mobile device.

Our strategy is simple:

- drive sustainable customer growth
- improve efficiency
- optimise capital

Drive sustainable customer growth:

- The Group's goal is to be a strong, customer-centric bank that proactively responds to changes in customers' needs and builds long-standing relationships, delivering customer-driven product and service propositions across both retail and business banking.
- A "deposit first" philosophy – we aim to secure the primary account relationship to drive increased product penetration and low cost sustainable funding.
- We are focused on the acquisition of customers in key target segments for example, a younger, more affluent customer demographic.
- We aim to deliver an agile approach to product proposition development, targeted at our key customer segments.
- We will ruthlessly focus on simplifying operational processes to drive customer experience which is "brilliantly simple". Progress is monitored through a number of metrics including surveys, resolution of complaints and Net Promoter Scores.
- We will drive stronger performance – and a focus on end to end product profitability – through an integrated product, portfolio and balance sheet management capability.
- Further integration of product and service across channels will drive enhanced customer experience and efficiency.

Improve efficiency:

- Significant opportunities remain to improve the cost structure of the Group.
- In September 2016, management announced detailed plans to reduce the Group's cost structure, focusing on four areas: Customer Banking transformation; Improved customer service; Right model; and Getting more for less.
- We will build on the progress made in 2016 - during the year, the outlook for underlying costs was reduced by £33m, from a previously announced £762m cost base (4% reduction).
- Efficiency improvements will be viewed from a customer perspective. We are targeting sustainable cost improvements, while supporting our growth ambitions, which are aligned with our risk appetite.
- We have clear accountability for delivery.

Capital optimisation:

- The Group has established a programme to progress an internal ratings based ("IRB") capital approach to modelling risk, subject to regulatory approval.
- Moving to IRB will improve our competitive positioning, enhance our risk management capabilities and strategy and also lower the intensity of our risk weighted asset ("RWA") and future bail-in debt requirement (Minimum Requirement for Own Funds and Eligible Liabilities ("MREL")).
- Our initial focus is firstly on achieving IRB accreditation for our mortgage portfolio which we currently anticipate to be during FY2018, subject to regulatory approval. Our subsequent focus will be IRB treatment of other retail asset portfolios and SME book, with the remainder of the bank moving to IRB approximately one year later.
- As an IRB accredited bank the PRA will continue to determine our ultimate capital requirements through supervisory processes.
- The Group also continues to have two portfolios that are in 'run off'. The first portfolio relates to tracker mortgages while the second is a cohort of low yielding SME lending. Both portfolios are high quality, but low returning. Running these portfolios down will enable capital tied up supporting these loans to be recycled over time into higher returning assets.

Through omni-channel delivery:

- Our strategy is underpinned by our omni-channel approach.
- We are focused on delivering seamless end to end customer journeys across different distribution channels – "anytime, any place, anywhere".
- Our omni-channel distribution model will allow us to differentiate on customer experience.
- Our digital strategy is an important part of our growth agenda driving efficiency, process simplification and customer acquisition.
- This will be supported by an investment programme to extend our digital platform, simplify our IT architecture and enhance our platform resilience, as well as support growth and improved efficiency, and ensure we keep our business safe and secure.

1.3 Summary of risk profile

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 implemented significant changes to strengthen its risk capabilities since becoming stand alone and continues to develop in line with industry developments and best practice.

The Board is responsible for determining the nature and extent of the risks it is willing to take in order to achieve its strategic objectives. As part of its viability assessment under UK Corporate Governance 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 and the Group's key ratios are described below. Further information on the Board's assessment is provided in the Risk Overview section of the Strategic Report in the Group's Annual Report and Accounts.

Principal risks	Key mitigating actions
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.	- Significant credit risk strategies, credit risk appetite and tolerances for credit risk are approved and reviewed by the Board and Board's Risk Committee, and are inherent in the Group's business model. - The credit portfolio is closely monitored including risk sensitivity analysis with reviews of asset quality metrics with actions initiated where required.
Balance Sheet and Prudential Regulation Risks cover 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 employees (pension) and the need to withstand severe unexpected losses (capital). The Group may face changes in values of asset and liabilities as a result of movements in market factors such as interest rates, foreign exchange rates, volatility and credit spreads which may give rise to losses (market risks). Balance sheet risks are subject to rules and guidance (prudential regulation) and these are subject to a high level of change. There is a risk of failing to understand and comply with relevant rules or inadequate change management.	- Liquidity is managed in accordance with standards that are approved by the Board and supported by annual Funding and Contingency Funding Plans. - Liquidity is managed on a daily basis ensuring normal daily cash requirements are met and adequate sources of liquidity are available to support unforeseen cash outflows. - The Group completes a formal annual assessment of Liquidity Adequacy which is shared with the PRA. This includes analysis of key risks with consideration of stress scenarios. - Capital is forecast and monitored on a monthly basis by Treasury overseen by the Asset and Liability Committee ("ALCO"). - The Group completes a formal annual assessment of its capital requirements which is shared with the PRA, the outcome of the process influences the allocation and quantum of capital and feeds directly into risk appetite. - The Group has a designated Prudential Risk team who independently monitor, oversee and challenge balance sheet risks. - The Group undertakes a detailed assessment of the capital requirements inherent in its strategy including consideration of the impact of significant loss scenarios in order to inform the Board of potential areas of weakness in the Group's business model and also to ensure an appropriate level of capital is held in both business as usual and stressed environments.
Regulatory and Compliance Risk 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 Group proactively assesses the impacts of legal and regulatory developments, liaises with the various regulatory bodies and participates in industry fora. - Continued and significant senior management focus and levels of business resource are directed towards maintaining full regulatory compliance and this is considered when setting risk appetite. - The Board or Executive Risk Committee approves all material changes to regulatory policy and protocols. The Group's governing principles include the management and maintenance of regulatory policies and regulatory engagement.

Principal risks	Key mitigating actions
Conduct Risk is defined as the risk of treating customers unfairly and / or delivering inappropriate outcomes resulting in regulatory fines, compensation, redress costs and / or reputational damage.	- The Group has a Conduct Framework, with supporting target outcomes and operating principles. - Products are designed to meet customer needs and expectations, with governance processes embedded to ensure those objectives are met.
Operational Risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Impacts from operational risks arise from the day to day activities of the Group, which may result in direct or indirect losses and could adversely impact the Group's financial performance and position.	- 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. - Supplier relationships are categorised based on criticality of the support provided. Contingency planning focuses on alternative options and management approaches in the event of an outage with regular scenario tests performed. - Regular reviews and oversight of the Group's systems and infrastructure including the risk of cyber-attack.
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, or circumvent existing controls.	- The Group has an established Financial Crime Framework supporting ongoing management, monitoring and mitigation of Financial Crime Risk. - The Group completes ongoing risk assessments, monitoring and reporting, with appropriate Know Your Customer ("KYC") procedures. - The Group operates zero tolerance for internal fraud and has a control framework in place to mitigate against 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.	- The Board approves and oversees the execution of the Strategic Plan and associated strategic risk following the recommendations of the Chief Executive Officer ("CEO") and Executive Leadership Team. - A consolidated report outlining the triggers and exposure to strategic risk is independently prepared and presented to the Board's Risk Committee by the Chief Risk Officer ("CRO").
People Risk is the risk of not having sufficiently skilled and motivated employees who are clear on their responsibilities and accountabilities and who behave in an ethical way. This could lead to inappropriate decision making that is detrimental to customers, other employees or shareholders and could ultimately lead to Regulatory sanction.	- Roles, responsibilities and performance expectations and 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. - Decisioning authorities and delegations are clearly articulated and approved at least annually by the Board. - A robust and proportionate employment screening policy is applied at the point of recruitment. - A mandatory suite of compliance learning is assigned to all employees.

The key ratios for the Group are presented below.

Table 1: Key ratios

	2016	2015
Common Equity Tier 1 ("CET1") ratio	**12.6%**	13.2%
Tier 1 capital ratio	**15.0%**	15.7%
Total capital ratio	**18.2%**	18.9%
Leverage ratio	**6.8%**	7.1%
LCR	**140%**	131%
	£m	£m
Risk Weighted Assets	**19,029**	18,227
Total Assets	**39,929**	38,705

Whilst RWAs increased by £802m, driven by growth in mortgages, underlying capital generation of 123bps (defined on page 54 of the Annual Report and Accounts) ensured the CET1 ratio remained robust at 12.6%.

The Group's leverage ratio is 6.8% which exceeds the Basel Committee's proposed minimum of 3%, applicable from 2018. The Group will continue to closely monitor the leverage ratio against emerging rules and minimum calibration.

Further details on the Group's capital ratios, RWAs and leverage ratio are presented in section 4 of this document. Required disclosures for Clydesdale Bank PLC are presented in Appendix 1.

2.1 Basis of preparation and frequency of disclosures

This document sets out the 2016 Pillar 3 disclosures for the Group, comprising CYBG PLC ("the Company") and its controlled entities, including Clydesdale Bank PLC ("the Bank") in accordance with the rules laid out in the Capital Requirements Regulation ("CRR") (Part 8). The disclosures may differ from similar information in the Annual Report and Accounts for the year ended 30 September 2016, which are prepared in accordance with International Financial Reporting Standards. The information in these disclosures is prepared in accordance with regulatory requirements and may therefore not be directly comparable with that information.

The Group uses the standardised approach for credit risk, operational risk, market risk and credit valuation adjustment. This approach uses standard risk weighting percentages prescribed within the CRR and PRA implementing rules. The disclosures in this document are based on these approaches.

Throughout the document, unless otherwise specified, credit risk exposures are defined as the aggregate of drawn (on balance sheet) balances, undrawn (off balance sheet) commitments and contingent liabilities prior to the application of credit risk mitigation and prior to the application of credit conversion factors.

Unless otherwise stated, all figures are as at 30 September 2016, the Group's financial year end, with comparative figures as at 30 September 2015 where relevant. The Group comparative figures provided are those of the CYB Investments Limited Group.

The Group has a policy for complying with Pillar 3 disclosures, in line with the European Banking Authority ("EBA") guidelines on materiality, proprietary and confidential information and on disclosure frequency. These disclosures are published annually, and concurrently with the Annual Report and Accounts in accordance with regulatory guidelines. The Group publishes specific information more frequently where it is required under EBA guidelines. No disclosures have been omitted on the basis of them being regarded as proprietary or confidential.

Omissions of disclosures within this report on grounds of materiality are:

- disclosures relating to 'Exposures in equities not included in the trading book'. See notes 13 and 37 in the Annual Report and Accounts for further information on valuation and key assumptions and methodologies used in valuation;
- separate disclosure of the geographical distribution of lending credit risk exposures to areas outside of the United Kingdom ("UK") and disclosure of the EBA's Countercyclical Capital Buffer template. Such exposures are not material and have been classified as 'other' within table 14; and
- additional credit risk mitigation and credit risk adjustment disclosures in relation to the Bank on an individual consolidated basis. These disclosures are materially the same as those provided for the Group. Further information is provided in Appendix 1.

The Group's remuneration disclosures can be found within the Directors' Remuneration Report in the Group's Annual Report and Accounts.

In June 2016 the EBA launched a consultation on amended disclosure requirements for the EU banking sector, proposing to implement the revised international BCBS Pillar 3 requirements (issued January 2015). The disclosure framework enhancements proposed by the BCBS in March 2016 will be incorporated in due course. Globally and Other Systemically Important Institutions ("G-SII" and "O-SII") were recommended to implement a limited subset of the disclosures for year-end 2016. The Group is not a G-SII or O-SII but will give due consideration to the Guidelines once final UK requirements are known.

2.2 Scope of disclosures

The Pillar 3 disclosures in this document relate to the Group, with the exception of Appendix 1 which contains the disclosures required for the Bank (PRA firm reference number 121873), the Group's principal subsidiary.

There is a requirement to calculate and maintain regulatory capital ratios on both a Group basis and on an Individual Consolidated (or Solo) basis for the Bank. There are no differences between the bases of consolidation of the Group for accounting and prudential purposes. All of the Group's subsidiary undertakings are included in the data provided in the Pillar 3 disclosures. Full details of the Group's subsidiaries are provided in note 42 of the Annual Report and Accounts for the year ended 30 September 2016 (cybg.com/annualreport).

The subsidiaries included on the Individual Consolidation basis are:

- Yorkshire Bank Home Loans Limited;
- Clydesdale Bank Asset Finance Limited;
- CGF No. 9 Limited;
- CB Nominees Limited;
- CYB Intermediaries Limited;
- CYB Intermediaries Holdings Limited (in liquidation); and
- CYB Services Limited (in liquidation).

The Group's capital resources are presented in section 4 of this document and the Bank's Individual Consolidated capital resources are presented in Appendix 1 to this document.

The differences between the Group and the Bank are primarily due to:

- reserves held by entities that sit outside of the scope of the Bank's Individual Consolidation that are included in the Group consolidation;
- amounts included in the Bank's results in relation to transactions with the Group's securitisation vehicles which are eliminated on consolidation;
- a small impact from the RWAs of those entities outside of the scope of the Bank's Individual Consolidation; and
- the conduct indemnity deed[1] between the Group's former parent National Australia Bank ("NAB") and the Company which results in different accounting treatment to the Bank but a consistent economic outcome on total capital.

As a result of these differences, the Group's capital requirements at 30 September 2016 exceeded the Bank's Individual Consolidated capital requirements.

The following companies are securitisation vehicles established in connection with the Group's securitisation programme. Although the share capital of these securitisation vehicles is not owned by the Group, these vehicles are included in the consolidated financial statements as they are controlled by the Group:

- Lanark Holdings Limited;
- Lanark Trustees Limited (incorporated in England);
- Lanark Trustees Limited (incorporated in Jersey);
- Lanark Funding Limited;
- Lanark Master Issuer plc
- Lanark Options Limited;
- Lannraig Holdings Limited;
- Lannraig Funding Limited;
- Lannraig Master Issuer plc; and
- Lannraig Trustees Limited.

There are no current or foreseen material practical or legal impediments to the transfer of capital resources or the repayment of liabilities between consolidated entities within the Group, with the exception of assets and liabilities of the Group's securitisation vehicles (including the covered bond vehicle) which are not immediately available to other members of the Group.

2.3 Key matters arising during the year

The following significant events, which had an impact on the Group's capital and risk management, took place during the year ended 30 September 2016:

In February 2016, concurrently with the successful demerger and initial public offering ("IPO"), the Group restructured and simplified its capital base to reflect the fact that CYBG PLC is the 'Single Point of Entry' for the purposes of Recovery and Resolution Planning ("RRP") and MREL requirements. To achieve this, CYBG PLC repurchased £450m of existing Additional Tier 1 ("AT1") and £475m of existing Tier 2 ("T2") capital issued by the Bank and replaced this with new Capital Requirements Directive IV ("CRD IV") compliant issuances £450m AT1 and £475m of T2, both issued by CYBG PLC to NAB. CYBG simultaneously down-streamed the proceeds in substantially the same form to the Bank.

In September 2016, NAB and CYBG PLC successfully marketed, to a wide range of investors, the £450m of AT1 and £475m of T2 capital instruments issued by CYBG PLC to NAB at demerger. Accordingly at 30 September 2016 none of these instruments are held by NAB.

In February 2016, following the demerger and IPO, CYBG PLC successfully completed a court-approved reduction in its share capital resulting in the nominal value of each ordinary share in the company being reduced from £1.25 to £0.10 per share and a corresponding increase in retained earnings.

On 30 September 2016 CYBG PLC acquired the issued share capital of the Bank from its subsidiary CYBI for consideration of £1. The purpose of the transaction was to eliminate the requirement to retain CYBI as an intermediate holding company, with a view to ultimately liquidating the company and simplifying the Group's structure.

As noted in Section 1, during 2016, a programme has been initiated to support the Group's objective of securing regulatory approval to adopt an IRB capital approach to modelling credit RWAs. This programme is also supporting changes in the Collective Provision calculations required by IFRS9. (For further information on IFRS 9, please refer to note 2 of the Group's Annual Report and Accounts).

2.4 Review and challenge

These disclosures have been subject to internal verification and are reviewed by the Board's Risk Committee ("Risk Committee") on behalf of the Board. The disclosures have not been, and are not required to be, subject to independent external audit and do not constitute any part of the Group's Annual Report and Accounts.

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 Financial Reporting Council and compliant with the requirements of 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.

1 A Conduct Indemnity Deed exists where National Australia Bank Limited ("NAB") has agreed to provide the Group with a capped indemnity in respect of certain historic liabilities relating to conduct in the period prior to the demerger date.

In addition, a Control Effectiveness Review was completed 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.

Over the past year, the Group has refreshed the RMF, simplifying and improving the risk categories and impact classification. The control environment remains stable with the 2016 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.

For further information on the Group's approach to risk management refer to the Risk Report section of the Group's Annual Report and Accounts.

3.1 The Group's approach to risk

Risk exists in every aspect of the Group's business, throughout its operating environment and is a core consideration within the Strategic Plan. The Group's approach to risk management is based on a principle that risk management capability must be embedded within the businesses' front-line teams to be effective. This overriding principle embodies the following concepts:

- Commercial decisions are made on the basis of proactive consideration of risk and the impact on customers;
- Business managers use the RMF which assists in the appropriate balancing of both the risk and reward components; and
- Employees are responsible for risk management in their day to day activities.

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;
- A clearly articulated and risk appetite which influences the Group's strategic plan;
- A clearly defined risk culture which emphasises risk management throughout all areas of the business whilst 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, the Group's risk appetite and helps communicate it to stakeholders. This is important as it provides the definitive view on the broad direction 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.

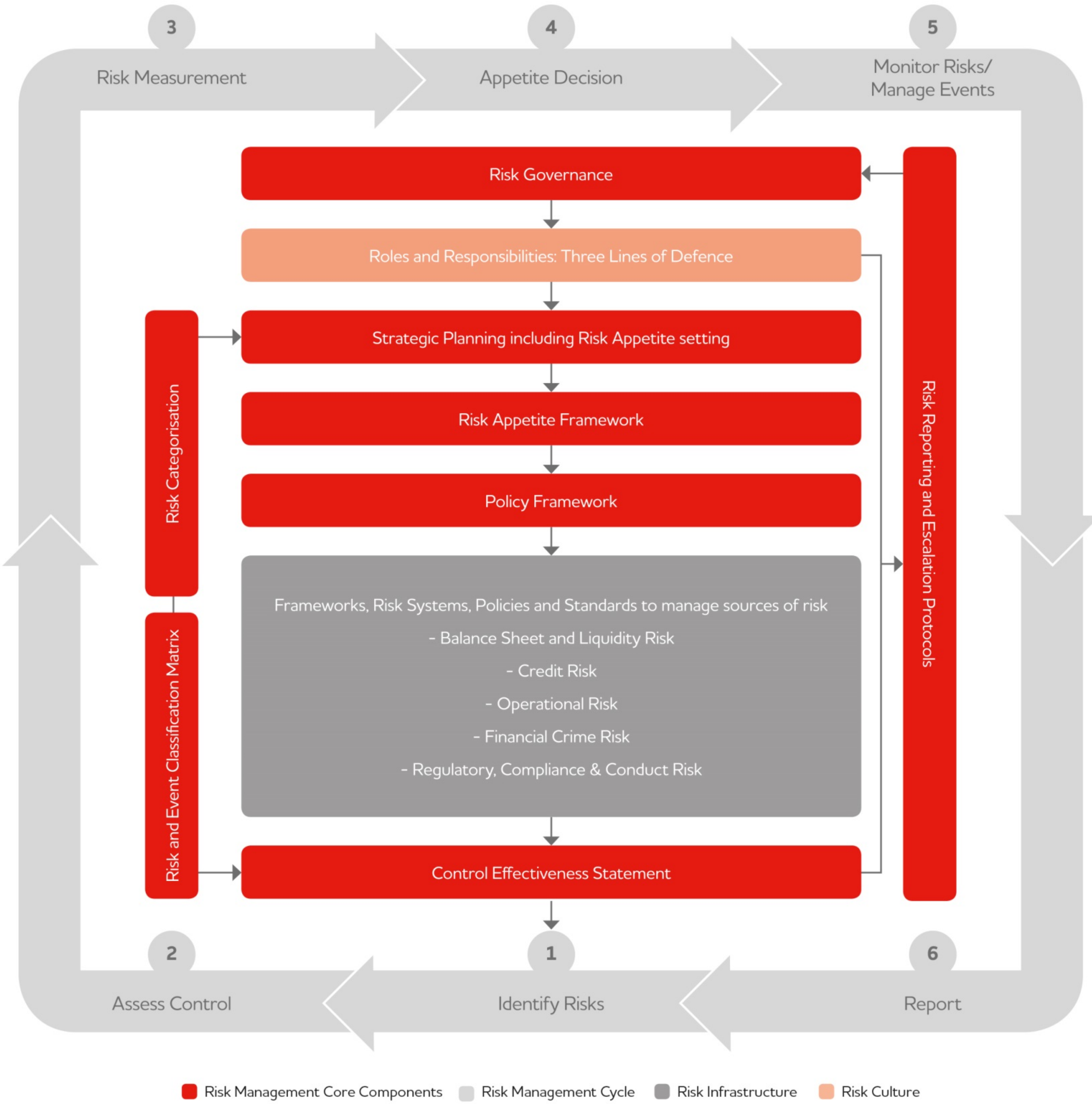
The RAS aligns to the risks identified and defined in the RMF. The design and structure of the RAS has taken into consideration best practice recently articulated by the European Central Bank which is aimed at ensuring Boards should be strongly involved in the validation process and monitoring of the RAS.

The Group's RAS is prepared by the CRO with consideration of the strategic objectives and business model of the Group as well as the environment in which it operates. Monthly reporting to Executive Committees and Board includes details of performance against relevant RAS settings, breaches and trends.

Risk Management Framework

The Group identifies and manages risk using the RMF (see following diagram), 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.

Chart 1: Risk Management Framework



Risk culture

Central to the Group's risk culture is the fair treatment of customers and meeting obligations to stakeholders, including shareholders and employees. 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; escalation procedures encouraging employees to raise concerns; 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 employees are able to make risk based decisions.

Risk management

Effective management of risk is a key capability for a successful financial services provider and is fundamental to the Group's strategy. Board oversight of risk management is facilitated by the Boards' Risk and Audit Committees; the Board approves the Group's overall governance, risk and control frameworks and risk appetite.

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 aims to set a tone that demonstrates the risk culture expected across the organisation.
This aligns with the behavioural expectations for all employees which form a core part of our performance management approach. Policies and supporting standards define the minimum control requirements which must be observed across the Group to manage material sources of risk within risk appetite.

3.2 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. Refer to the Group's website (www.cybg.com) for further information on Board committees. The Group's risk management is governed via a series of committees as represented within the diagram which follows:

Chart 2: Governance Committee Framework

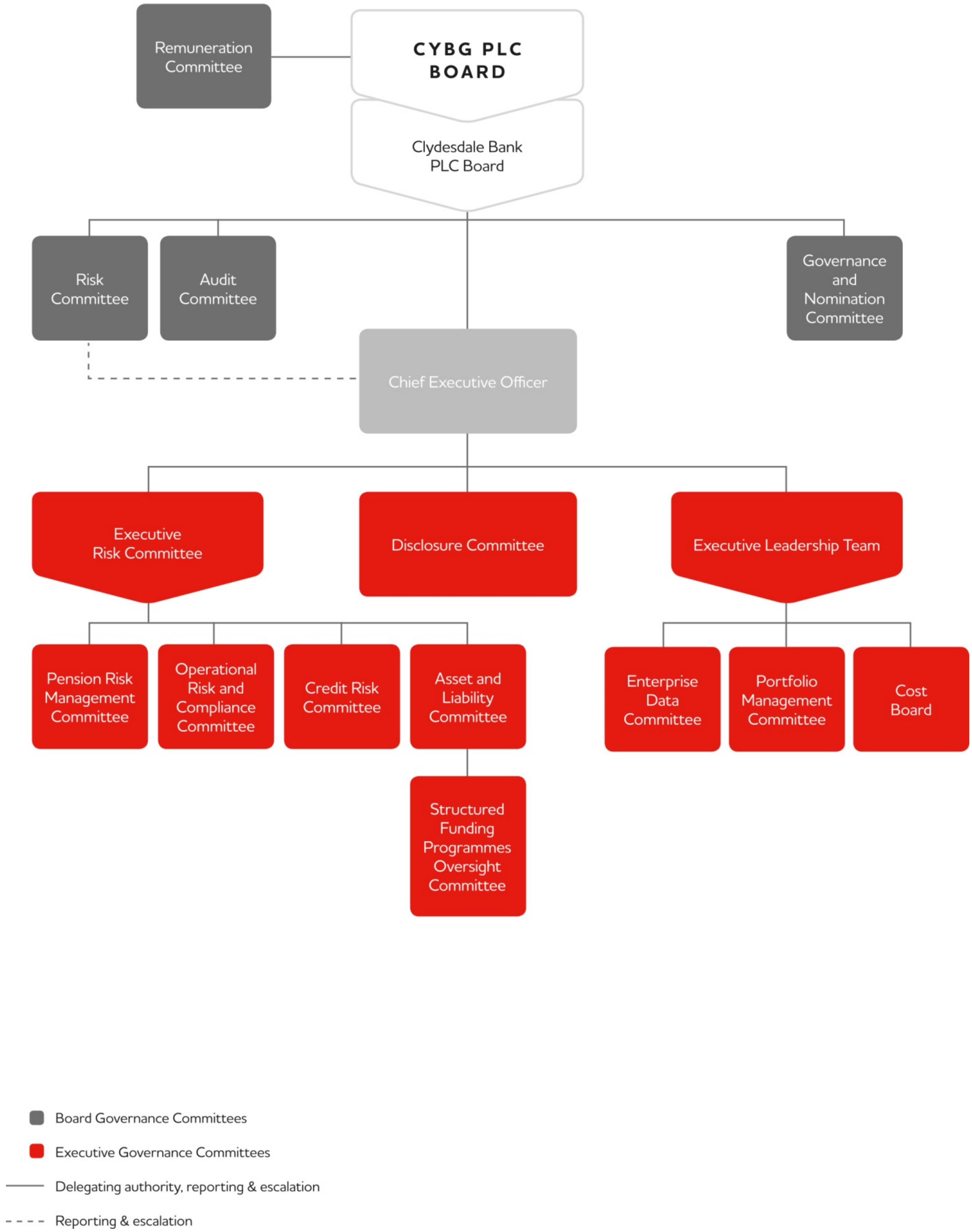


Table 2: Governance Committees

The following Executive level Committees have been established under the authority of the Chief Executive Officer (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 the exchange(s) 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 Defined Benefit Scheme.
Credit Risk Committee	The Credit Risk Committee is responsible for ensuring that the credit risk management framework 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.
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.
Asset & Liability Committee	The Asset and Liability Committee ("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.

The Executive Leadership Team is supported by the following Committees:

Enterprise Data Committee	The Enterprise Data Committee is responsible for providing direction and oversight of information and data practices, including oversight of management's resolution of data issues.
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.

3.3 The Board and governance

The number of directorships held by Executive and Non-Executive Directors are shown below. In line with the relevant rules[2], directorships in organisations which don't pursue predominantly commercial objectives have been excluded. In addition, where a Director has a number of directorships within one group these are counted as a single directorship.

Table 3: Directorships Held

Name	Directorships Held
James Pettigrew	4
David Duffy	1
Debbie Crosbie	1
Ian Smith	2
Richard Gregory	2
Clive Adamson	4
David Bennett[3]	5
Paul Coby	2
Adrian Grace	2
David Browne	2
Fiona MacLeod	3
Teresa Robson-Capps	2
Tim Wade[4]	5

Board recruitment

When considering the recruitment of a new Director, the Committee adopts a formal, rigorous and transparent procedure with due regard to diversity, including gender. Prior to 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.

Where the Committee appoints external advisers to facilitate the Director search process, it ensures that the firm has a specialism in financial services appointments and has no other connection with the Company.

Board diversity

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. The Board's commitment is set out in the Board Composition and Renewal Policy. A separate Diversity at Work Standard applies to all colleagues across the Group. In 2016 the Board continued to focus on improving diversity and will continue to do so. The percentage of female representation on the Board at the date of this report is 23% (based on three female Directors and ten male Directors), slightly short of the recommendation of Lord Davies for 25% female representation by 2015.

2 PRA Rulebook 'General Organisational Requirements' 5.5 (having regard to 'General Organisational Requirements' 5.6) and FCA Handbook 'Senior Management Arrangements, Systems and Controls' ("SYSC") 4.3A.6R (having regard to SYSC 4.3A.7R).

3 The Prudential Regulation Authority and the Financial Conduct Authority jointly approved a modification of 'General Organisation Requirements' 5.5 and SYSC 4.3A.6R in relation to Mr Bennett's directorship portfolio, effective from 14 December 2016 to 13 December 2017. The modification is published on the Financial Services Register.

4 The Prudential Regulation Authority and the Financial Conduct Authority jointly approved a modification of 'General Organisation Requirements' 5.5 and SYSC 4.3A.6R in relation to Mr Wade's directorship portfolio, effective from 23 November 2016 until 22 November 2017. The modification is published on the Financial Services Register.

3.4 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 an 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 employees 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.

Chart 3: Three Lines of Defence

The Group's risk management function as at 30 September 2016 is represented below:

Chart 4: Group Risk Management Function

3.5 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, 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 at 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 including, but not limited to:

- Finance who manage the macroeconomic scenario process and prepare and review stressed business plans;
- Credit Risk who prepare and review credit stress outputs, including impairment charges, RWAs and write offs;
- Treasury who provide funding and liquidity impacts and construct capital plans based on the outcomes of stress testing; and
- Products and Customer Banking who 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 and are recognised as a required risk management tool in the form of an early warning indicator framework.

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 Internal Capital Adequacy Assessment Process ("ICAAP"). The Group runs a number of adverse macroeconomic stresses in order to determine the impacts on the Group's financial and capital position, taking account of 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 Internal Liquidity Adequacy Assessment Process ("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 and strategic 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.

Prior to Board submission, ALCO reviews the scenarios, assumptions and results of liquidity and capital stress testing and provides initial review and challenge of outputs.

3.6 Principal risks

The Group's principal risks are summarised in section 1. Further information on these risks are included in the Risk Report within the Group's Annual Report and Accounts.

3.6.1 Credit risk

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 groups 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 Chief Credit Officer ("CCO") and Credit Risk Committee provides a policy framework that 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 lent 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 which 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.

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.

3.6.2 Balance sheet & prudential regulation risks

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 risks 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 and oversight of balance sheet risks is to maintain the risk profile within approved risk appetite and limits, while implementing strategies that 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 on-going strength and resilience of the balance sheet.

Risk appetite is approved for balance sheet risks by the Group's 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 Common Equity Tier 1, leverage and minimum holdings of capital. Measures for funding and liquidity risks consider the structure of the balance sheet and include, amongst 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 a volume of high quality liquid assets that is sufficient to accommodate outflows of funds in a range of stress scenarios over a 3 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.

Further information on capital risk management is provided in section 5.1.

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 requirement which covers all regulatory and internal liquidity requirements. In addition the Group has a liquidity standard which details, amongst other items, the control standards and risk measurement requirements for liquidity and 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 and gap 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 Group's Treasury division 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 act 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 timeframe 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:

- Retail, SME and corporate deposits;
- Commercial paper programme;
- Access to money markets through cash deposits and certificates of deposit;
- "Lanark" residential mortgage securitisation programme (owner occupied);
- "Lannraig" BTL mortgage securitisation programme;
- RCB programme; and
- Access to the facilities within the BoE Sterling Monetary Framework which include the Term Funding Scheme announced in August 2016.

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 Group's Treasury division 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.

Key risks

An assessment of a number of key risk drivers for funding and liquidity risks has been completed as part of the ILAAP and a summary of the most material key risks is shown in the table below.

Risk	Rationale for assessment
Wholesale Funding	While wholesale borrowing is largely medium term and the Group has proven access to term debt markets there is residual refinancing risk around the medium term funding transactions.
Funding Tenors	Funding Tenors are an additional component of wholesale funding risk. The Group must maintain an appropriate mix by tenor in order to manage maturity concentrations.
Retail Funding	While the overall assessment of the retail funding key risk driver is low, the potential impact if this risk were to crystallise is high. This is reflective of the shape of the Group's balance sheet and an appropriate reliance on Customer deposits as a retail driven bank. The Group holds a portfolio of high quality liquid assets in order to act as a buffer against the effects of liquidity risk.

At 30 September 2016, 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. 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 Loan to Deposit Ratio ("LDR") increased from 109% to 112% in the year to 30 September 2016 due to growth in customer lending combined with a managed reduction in short term corporate deposits which provided little liquidity benefit to the Group.

Market risks

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.

Pension risk

The Group operates a Defined Benefit ("DB") pension scheme, the Yorkshire and CB Pension Scheme ("the Scheme"). The Bank is the Scheme's principal employer and there are no other participating employers.

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'). The Scheme provides members with pensions based primarily on years of service and salary. As such, there are significant risks associated with managing a DB scheme, both in terms of benefits already built up and future benefit accrual. 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, according to 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 main focus is directed on mitigating the impact on capital and earnings through working with the trustee to implement risk reduction initiatives. A number of activities have been implemented since 2003 with the specific aim of reducing risk in the Scheme, including a derisking journey plan and a number of benefit reforms.

Further information on pension risk is provided in note 29 of the Group's Annual Report and Accounts.

3.6.3 Regulatory, compliance & conduct risk

Regulatory and Compliance risk consists of regulatory strategy and change risk and regulatory relationship risk. Regulatory strategy and change risk is the risk of failing to identify and monitor changes in the regulatory environment and of failing to take opportunities to help shape the development of emerging legislative frameworks and / or to effectively implement the required changes. Regulatory relationship risk is the risk of damaging the Group's relationship with regulators through non-compliance with regulatory requirements, not keeping regulators informed of relevant issues impacting (or which may potentially impact) the Group, and not meeting the information requests and review findings of 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 regulatory breaches.

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 employees 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 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 the 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 treating customers unfairly and / or delivering inappropriate outcomes resulting in customer detriment, regulatory fines, compensation, redress costs and reputational damage.

Risk appetite

The Group has a conservative appetite for conduct risk.

Exposures

As part of the demerger from NAB, 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 27 to the Annual Report and Accounts.

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 27 of the Group's Annual Report and Accounts reflecting the Group's current position in relation to redress provisions for PPI, 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.

Consideration of customer outcomes is embedded within the Group's operating processes, and metrics are regularly monitored to help ensure outcomes are appropriate.

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 incorporates target outcomes and operating principles to ensure the Group's business model and supporting business practices achieve fair treatment of customers and the avoidance of customer detriment.

Products are subject to a product governance framework methodology and are designed and sold to meet customer needs and expectations with governance processes embedded to ensure those objectives are met.

Monitoring

This is a principal focus of the Board, senior management and regulators, and the Group seeks to ensure customers are treated fairly, products are designed and sold to meet their needs, 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.

3.6.4 Operational risk

Operational risk (including strategic, business, financial performance and 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 risk management framework are defined in an overarching operational risk policy and related minimum standards, and reflect the Group's appetite for operational risk.

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.

Further information on operational risk is provided in section 7.

3.6.5 Financial crime risk

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 relative 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 & 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 are performed as part of the formal oversight plan and embedded activities take place throughout the year. Key performance metrics relative to the critical financial crime systems (sanctions / politically exposed persons screening for customers and payments, transaction monitoring, account opening performance) are discussed at a regular, formal calibration meeting. Performance of systems is also measured using a third party tool to ensure effectiveness is not being eroded or diminishing. Training completion and compliance is subject to annual oversight. All standards are reflected in the Group policies 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 Risk 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 / 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.

4.1 Own funds

The table below shows the composition of the Group's regulatory capital position as at 30 September 2016 on a CRD IV basis. The table includes 2015 comparatives prepared on the same basis. The table follows the disclosure format required by the EBA Implementing Technical Standard on Disclosure for Own Funds, however only items applicable to the Group are shown. Some line items have been presented in an expanded format compared to the prior year to show additional detail. The comparative line items have been similarly expanded.

The capital resources of the Bank are presented in Appendix 1 of this document.

Table 4: Capital composition

As at 30 September		2016 £m	2015 £m
	Common Equity Tier 1 (CET1) capital: Instruments and reserves		
1	Capital instruments and the related share premium accounts	88	893
1a	Of which: Ordinary Shares	88	893
2	Retained earnings	2,771	2,339
3	Accumulated other comprehensive income (and other reserves)	94	1
6	Common Equity Tier 1 (CET1) capital before regulatory adjustments	2,953	3,233
	Common Equity Tier 1 (CET1) capital: regulatory adjustments		
7	Additional value adjustments	(7)	(5)
8	Intangible assets	(256)	(265)
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences	(35)	(273)
11	Fair value reserves related to gains or losses on cash flow hedges	(66)	-
15	Defined benefit pension fund assets	-	(42)
25a	Losses and distributions for the current financial year (negative amount)	(192)	(243)
28	Total regulatory adjustments to Common Equity Tier 1 (CET1)	(556)	(828)
29	Common Equity Tier 1 (CET1) capital	2,397	2,405
	Additional Tier 1 (AT1) capital: instruments		
30	Capital instruments and the related share premium accounts	450	450
31	of which: classified as equity under applicable accounting standards	450	450
36	Additional Tier 1 (AT1) capital before regulatory adjustments	450	450
44	Additional Tier 1 (AT1) capital	450	450
45	Tier 1 Capital	2,847	2,855
	Tier 2 (T2) capital: Instruments and provisions		
46	Capital instruments and the related share premium accounts	474	-
48	Qualifying own funds instruments included in consolidated T2 capital issued by subsidiaries and held by third parties	-	460
49	*Of which: instruments issued by subsidiaries subject to phase out*	-	*175*
50	Credit risk adjustments	151	138
51	Tier 2 (T2) capital before regulatory adjustment	625	598
58	Tier 2 (T2) capital	625	598
59	Total Capital	3,472	3,453
60	Total risk weighted assets	19,029	18,227
	Capital Ratios		
61	Common Equity Tier 1	12.6%	13.2%
62	Tier 1	15.0%	15.7%
63	Total Capital	18.2%	18.9%

64	Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements plus a systemic risk buffer, plus systemically important institution buffer expressed as a percentage of total risk exposure amount)	**5.1%**	4.5%
65	of which: capital conservation buffer requirement	**0.6%**	0%
66	of which: countercyclical buffer requirement	**0%**	0%
67	of which: systemic risk buffer requirement	**0%**	0%
67a	of which: Global Systemically Important Institution (G-SII) or Other Systemically Important Institution (O-SII) buffer	**0%**	0%
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	**8.1%**	8.7%
	Applicable caps on the inclusion of provisions in Tier 2		
76	Credit risk adjustments included in T2 in respect of exposures subject to standardised approach (prior to the application of the cap)	**151**	138
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach	**214**	205

Significant movements in capital and related deductions are described below at section 4.2.

Tier 1 capital

Tier 1 capital comprises:

- ordinary shares;
- share premium;
- retained earnings;
- accumulated other comprehensive income (and other reserves);
- AT1 instruments; and
- adjustments as set out by the regulatory requirements governing capital resources.

Accumulated other comprehensive income (and other reserves) represents adjustments for asset revaluation, cash flow hedge and available for sale reserves. The inclusion of available for sale asset reserves became a requirement under CRR with effect from 1 January 2015.

Additional details of the perpetual capital notes are included in Appendix 2 and note 32 to the Annual Report & Accounts for the year ended 30 September 2016.

Tier 2 capital

Tier 2 capital comprises:

- subordinated loan debt;
- eligible collective impairment allowances; and
- adjustments as set out by the regulatory requirements governing capital resources.

Subordinated loan debt is unsecured and ranks below the claims of all depositors and other ordinary creditors. Additional details of the subordinated notes are included in Appendix 2 and in note 28 to the Annual Report and Accounts for the year ended 30 September 2016. Full terms and conditions for the Group's marketed debt securities are available on the Group's website (cybg.com/investor-centre/debt-investors/capital-instruments).

Under the regulatory rules, the percentage of subordinated loan debt permitted to be included as qualifying regulatory capital is limited to a maximum of 25% of total capital.

4.2 Movements in capital

Whilst RWAs increased by £802m, driven by growth in mortgages, underlying capital generation of 123bps (defined on page 54 of the Annual Report and Accounts) ensured the CET1 ratio remained robust at 12.6%.

In February 2016, following the demerger and IPO, CYBG PLC successfully completed a court-approved reduction in its share capital resulting in the nominal value of each ordinary share in the company being reduced from £1.25 to £0.10 per share and the increase in retained earnings seen in the table below.

Table 5: Capital flow statement

	2016 £m	2015 £m
CET1 capital		
CET1 capital at 1 October	**2,405**	1,747
Share capital: ordinary share new issuance	**-**	350
Share for share exchange and nominal reduction	**(135)**	-
Share premium	**(670)**	670
Share capital: redenomination	**-**	(2,009)
Retained earnings and other reserves	**525**	1,998
Prudent valuation adjustment	**(2)**	(3)
Intangible assets	**9**	(52)
DTAs relying on future profitability	**238**	(50)
Defined benefit pension fund assets	**42**	(3)
Fair value reserves related to gains or losses on cash flow hedges	**(66)**	-
Losses for the current financial year	**51**	(243)
	2,397	2,405
Tier 1 capital		
Tier 1 capital at 1 October	**450**	300
Share capital repurchased: perpetual non-cumulative preference shares	**(450)**	-
Share capital issued: Perpetual Subordinated Contingent Convertible Notes	**450**	-
Share capital issued: Additional Tier 1 capital perpetual notes	**-**	150
	450	450
Total Tier 1 capital	**2,847**	2,855
Tier 2 capital		
Tier 2 capital at 1 October	**598**	1,260
Subordinated debt repurchase	**(475)**	(665)
Capital instruments issued: Subordinated debt	**474**	-
Credit risk adjustments	**13**	3
Removal of minority interest deduction of Subordinated Debt	**15**	-
	625	598
Total capital at 30 September	**3,472**	3,453

A number of deductions are applied in calculating regulatory capital under CRD IV. These include deductions for: intangible assets, deferred tax assets ("DTAs") that rely on future profitability, defined benefit pension scheme IAS19 surpluses, prudent valuation adjustments and certain investments in other financial institutions.

The most significant of these are:

- The IAS19 valuation of defined benefit pension schemes is included in accounting reserves. This means that an IAS19 deficit position is automatically reflected in regulatory capital. If the IAS19 valuation is a surplus, the regulatory rules do not permit this to contribute towards regulatory capital and this figure must be deducted. At 30 September 2015, the IAS19 valuation was a surplus of £52m. At 30 September 2016, the IAS19 valuation was a deficit of £75m, resulting in the net of tax movement of £42m seen in the table above.
- The regulatory adjustment required in respect of DTAs that rely on future profitability and intangible assets (computer software and other IT development which has been capitalised). At 30 September 2016, £35m was deducted from CET1 capital in respect of DTAs and £256m was deducted in respect of intangible assets, resulting in movements of £238m and £9m respectively, seen in the table above.
- The deduction for fair value reserves related to gains or losses on cash flow hedges has increased during the year following market volatility arising from the UK's referendum vote to leave the EU.

Table 6 shows the capital position on a transitional CRD IV basis. The transitional provisions in relation to some of the Group's Subordinated Debt instruments, including the recognition of qualifying T2 capital instruments issued by a subsidiary to outside the consolidated group, which applied at 30 September 2015 have been superseded by the issuances under the Group's capital restructure at demerger in February 2016. As such, the Group capital position is now calculated and presented on a "fully loaded" CRD IV basis, other than in respect of transitional capital buffers. Some line items have been presented in an expanded format compared to the prior year to show additional detail. The comparative line items have been similarly expanded.

Table 6: CRD IV end-point vs transitional comparison

		Current Rules		Full Impact	
As at 30 September		**2016**	2015	**2016**	2015
		£m	£m	**£m**	£m
	Common Equity Tier 1 (CET1) capital: Instruments and reserves				
1	Capital instruments and the related share premium accounts	**88**	893	**88**	893
1a	Of which: Ordinary Shares	**88**	893	**88**	893
2	Retained earnings	**2,771**	2,339	**2,771**	2,339
3	Accumulated other comprehensive income (and other reserves)	**94**	1	**94**	1
6	Common Equity Tier 1 (CET1) capital before regulatory adjustments	**2,953**	3,233	**2,953**	3,233
	Common Equity Tier 1 (CET1) capital: regulatory adjustments				
7	Additional value adjustments	**(7)**	(5)	**(7)**	(5)
8	Intangible assets	**(256)**	(265)	**(256)**	(265)
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences	**(35)**	(273)	**(35)**	(273)
11	Fair value reserves related to gains or losses on cash flow hedges	**(66)**	-	**(66)**	-
15	Defined benefit pension fund assets	**-**	(42)	**-**	(42)
25a	Losses and distributions for the current financial year (negative amount)	**(192)**	(243)	**(192)**	(243)
28	Total regulatory adjustments to Common Equity Tier 1 (CET1)	**(556)**	(828)	**(556)**	(828)
29	Common Equity Tier 1 (CET1) capital	**2,397**	2,405	**2,397**	2,405
	Additional Tier 1 (AT1) capital: instruments				
30	Capital instruments and the related share premium accounts	**450**	450	**450**	450
31	of which: classified as equity under applicable accounting standards	**450**	450	**450**	450
36	Additional Tier 1 (AT1) capital before regulatory adjustments	**450**	450	**450**	450
44	Additional Tier 1 (AT1) capital	**450**	450	**450**	450
45	Tier 1 Capital	**2,847**	2,855	**2,847**	2,855
	Tier 2 (T2) capital: Instruments and provisions				
46	Capital instruments and the related share premium accounts	**474**	-	**474**	-
48	Qualifying own funds instruments included in consolidated T2 capital issued by subsidiaries and held by third parties	**-**	460	**-**	263
49	*Of which: instruments issued by subsidiaries subject to phase out*	**-**	175	**-**	-
50	Credit risk adjustments	**151**	138	**151**	138
51	Tier 2 (T2) capital before regulatory adjustment	**625**	598	**625**	401

58	Tier 2 (T2) capital	**625**	598	**625**	401
59	Total Capital	**3,472**	3,453	**3,472**	3,256
60	Total risk weighted assets	**19,029**	18,227	**19,029**	18,227
	Capital Ratios				
61	Common Equity Tier 1	**12.6%**	13.2%	**12.6%**	13.2%
62	Tier 1	**15.0%**	15.7%	**15.0%**	15.7%
63	Total Capital	**18.2%**	18.9%	**18.2%**	17.9%
64	Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements plus a systemic risk buffer, plus systemically important institution buffer expressed as a percentage of total risk exposure amount)	**5.1%**	4.5%	**7.0%**	4.5%
65	of which: capital conservation buffer requirement	**0.6%**	0%	**2.5%**	0%
66	of which: countercyclical buffer requirement	**0%**	0%	**0%**	0%
67	of which: systemic risk buffer requirement	**0%**	0%	**0%**	0%
67a	of which: Global Systemically Important Institution (G-SII) or Other Systemically Important Institution (O-SII) buffer	**0%**	0%	**0%**	0%
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	**8.1%**	8.7%	**8.1%**	8.7%
	Applicable caps on the inclusion of provisions in Tier 2				
76	Credit risk adjustments included in T2 in respect of exposures subject to standardised approach (prior to the application of the cap)	**151**	138	**151**	138
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach	**214**	205	**214**	205

4.3 Reconciliation of statutory equity to regulatory capital

Table 7: Reconciliation of Statutory Equity to Regulatory Capital

As at 30 September	**2016 £m**	2015 £m
Statutory Total Equity	**3,211**	3,443
Less pension regulatory adjustments	**-**	(42)
Less Additional Value Adjustment	**(7)**	(5)
Less intangible assets	**(256)**	(265)
Less share option reserve	**-**	(3)
Less deferred tax assets relying on future profitability	**(35)**	(273)
Less cash flow hedge	**(66)**	-
Regulatory Tier 1 capital	**2,847**	2,855
Statutory Tier 2 subordinated debt	**477**	475
Less unamortised hedge on issuance	**(3)**	-
Minority interest deduction of Subordinated Debt	**-**	(15)
Regulatory Tier 2 subordinated debt	**474**	460

4.4 Leverage ratio

Management of excessive leverage

The leverage ratio is monitored against a Board set RAS and ALCO has responsibility for oversight of the ratio which is monitored on a monthly basis.

The leverage ratio is the ratio of Tier 1 capital to total exposure. Tier 1 capital is defined according to CRD IV and, for this purpose, the full impact of CRD IV requirements on Tier 1 capital are assumed to be in force. Exposures are defined as the total on- and off-balance sheet exposures (after application of credit conversion factors). This follows the definition given in the Delegated Act amending CRR article 429, and includes deductions applied to Tier 1 capital.

Table 8 below shows the leverage ratio disclosures template required by the EBA's Implementing Technical Standards on disclosure of the leverage ratio. Included within the 2016 figures is a deduction of receivables assets for cash variation margin. If the 2015 leverage ratio was shown on this basis, the leverage ratio would be 7.2%.

Table 8: Leverage Ratio

As at 30 September	2016 £m	2015 £m
Total Tier 1 capital for the leverage ratio		
Total Common Equity Tier 1 (CET1) capital	**2,397**	2,405
Additional Tier 1 (AT1) capital	**450**	450
Total Tier 1	**2,847**	2,855
Exposures for the leverage ratio		
Total statutory assets per the published financial statements	**39,929**	38,705
Adjustments for off balance sheet items	**1,982**	1,998
Adjustments for derivative financial instruments	**(399)**	19
Adjustments for securities financing transactions (SFTs)	**601**	-
Other regulatory adjustments	**(364)**	(585)
Leverage ratio exposure	**41,749**	40,137

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.

	2016 £m	2015 £m
On-balance sheet exposures (excluding derivatives and SFTs)		
On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	**39,344**	38,420
Asset amounts deducted in determining Tier 1 capital	**(364)**	(585)
Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets)	**38,980**	37,835
Derivative exposures		
Replacement cost associated with *all* derivatives transactions	**396**	81
Add-on amounts for PFE associated with *all* derivatives transactions (mark-to-market method)	**127**	223
(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	**(337)**	-
Total derivatives exposures	**186**	304
SFT exposures		
Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions	**1,827**	-
(Netted amounts of cash payables and cash receivables of gross SFT assets)	**(1,226)**	-
Total securities financing transaction exposures	**601**	-
Other off-balance sheet exposures		
Off-balance sheet exposures at gross notional amount	**7,813**	7,910
Adjustments for conversion to credit equivalent amounts	**(5,831)**	(5,912)
Other off-balance sheet exposures	**1,982**	1,998

Capital and total exposure measure		
Tier 1 capital	**2,847**	2,855
Leverage ratio total exposure measure	**41,749**	40,137
Leverage ratio		
Leverage ratio	**6.8%**	7.1%
Choice on transitional arrangements and amount of derecognised fiduciary items		
Choice on transitional arrangements for the definition of the capital measure	**Full Impact**	Full impact
Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures)		
Total on-balance sheet exposures (excluding derivatives, SFTs & exempted exposures), of which:	**39,344**	38,420
Banking book exposures, of which:		
-Covered bonds	**191**	-
-Exposures treated as sovereigns	**6,170**	6,576
-Exposures to regional governments, MDBs, international organisations & PSE not treated as sovereigns	**12**	12
-Institutions	**762**	850
-Secured by mortgages of immovable properties	**25,807**	24,560
-Retail exposures	**1,124**	1,169
-Corporates	**2,833**	2,551
-Exposures in default	**337**	352
-Other exposures (e.g. equity, securitisations, & other non-credit obligation assets)	**2,108**	2,350

The Group's leverage ratio is 6.8% which exceeds the Basel Committee's proposed minimum of 3%, applicable from 2018. The movement in the year has been driven by an increase in total exposures as a result of balance sheet growth during the period. The Group will continue to closely monitor the leverage ratio against emerging rules and minimum calibration.

5.1 Capital management

The Group's Capital Policy Standard provides the framework for the manner in which capital is managed within the Group (at both Group and solo consolidated levels). The objectives of the standard are to efficiently manage the capital base to optimise shareholder returns whilst maintaining robust capital adequacy, meeting regulators' requirements, managing the ratings agencies' assessments 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 apply for a waiver to utilise IRB methods for the calculation of credit risk capital.

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: CCB; CCyB; Global Systemically Important Institution Buffer ("G-SIIB"); and, 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 Bank of England ("BoE") view of credit conditions in the economy. In March 2016 the Financial Policy Committee ("FPC") raised the rate to 0.5% for UK exposures (with effect from 29 March 2017).

As a result of increased concerns around the prospects for the UK economy following the UK's vote to leave the EU the decision to raise the CCyB to 0.5% has been reversed. The BoE noted that "absent any material change in the outlook, and given the need to give banks the clarity necessary to facilitate their capital planning, the FPC expects to maintain a 0% UK CCyB rate until at least June "2017" (the FPC reaffirmed the Group's position on 22 September 2016). The BoE commented that this action reinforces their expectation that all elements of the substantial capital and liquidity buffers that have been built up by banks are able to be drawn on, as necessary.

Beyond June 2017 the future path of the CCyB is less certain. It is anticipated that the CCyB will move gradually to 1% in a neutral risk environment.

The Group's capital planning considers the impact of all relevant capital buffers.

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, the Bank 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.

As noted in section 2 foreign credit exposures are not material for the Group. These exposures represent less than 2% of the aggregate risk weighted exposures of the Group therefore all exposures are shown against the UK, which currently has a countercyclical capital buffer rate of 0%. The EBA's Countercyclical Capital Buffer template has therefore not been shown.

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.

5.2 Minimum capital requirement

To determine minimum capital requirements under the CRD IV Framework, the Group applies the standardised approach to measure credit risk and for operational risk. Under the approach the Group calculates its Pillar 1 capital requirement based on 8% of total RWAs. This covers credit risk, operational risk, counterparty credit risk and credit valuation adjustment ("CVA").

The table below shows the Group's RWAs and capital requirements under Pillar 1.

Table 9: Pillar 1 Capital Requirements

	2016		2015	
Pillar 1 Capital Requirements	RWA £m	Capital £m	RWA £m	Capital £m
Regional Government or Local Authority	**20**	**2**	22	2
Public Sector Entities	**5**	**-**	3	-
Institutions	**234**	**19**	222	18
Corporates	**3,533**	**283**	3,264	262
Retail	**897**	**72**	930	74
Secured by Mortgages on Immovable Property	**11,242**	**897**	10,862	869
Exposures in Default	**408**	**33**	427	34
Items associated with particularly high risk	**15**	**1**	-	-
Covered bonds	**19**	**2**	-	-
Claims in the Form of CIU	**3**	**-**	3	-
Equity Exposures	**11**	**1**	16	1
Other Items	**519**	**42**	545	44
Total Credit Risk	**16,906**	**1,352**	16,294	1,304
Credit Counterparty Risk	**214**	**17**	138	11
Credit Valuation Adjustment	**286**	**23**	206	16
Operational Risk	**1,623**	**130**	1,589	127
	19,029	**1,522**	18,227	1,458

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 DTAs which have not been deducted.

The Group's capital requirements are set by the PRA, consisting of Individual Capital Guidance plus Capital Buffer Requirements and the Group had a surplus to these requirements at 30 September 2016. This included a Pillar 2A requirement set at 5.7% of RWAs, 3.2% of which must be met by CET1 capital. In October the PRA updated the Group's capital requirements which included a revised Pillar 2A requirement to 4.6% of RWAs, 2.6% of which must be met by CET1 capital.

6.1 Credit risk exposure: analysis by exposure class

As at 30 September 2016, the total credit risk exposures of the Group amounted to £48.6 billion (2015: £46.2 billion). The overall capital requirement for credit risk has increased by 3.7% from £1,304 million in 2015 to £1,352 million in 2016.

The table below shows movements in credit risk RWAs from 1 October 2015 to 30 September 2016, with movements ascribed to changes in book size and book quality.

Table 10: Credit Risk RWAs

	Credit Risk RWAs £m
RWAs at 1 October 2015	16,294
Book Size growth	585
Book Quality deterioration	27
RWAs at 30 September 2016	**16,906**

Total credit risk exposure has increased with a smaller increase in credit risk RWAs. This is in line with the continued growth of the Group's mortgage portfolio. Credit risk exposures by exposure class are provided in the table below, together with the associated average credit risk exposure.

Table 11: Credit Risk Exposure by Exposure Class[5]

The credit risk exposures at 30 September 2016 and the average for the year are summarised as follows:

	2016		2015	
	Credit Risk Exposure	**Average Credit Risk Exposure**	Credit Risk Exposure	Average Credit Risk Exposure
Exposure Class	**£m**	**£m**	£m	£m
Central Governments or Central Banks	**7,003**	**6,613**	6,477	6,645
Regional Government or Local Authority	**527**	**580**	594	582
Public Sector Entities	**63**	**29**	16	16
Multilateral Development Banks	**195**	**174**	100	88
Institutions	**1,345**	**1,064**	841	1,136
Corporates	**6,114**	**6,051**	5,914	6,136
Retail	**3,053**	**3,126**	3,125	3,161
Secured by Mortgages on Immovable Property	**28,046**	**27,750**	26,823	26,402
Exposures in Default	**346**	**368**	367	412
Items associated with particularly high risk	**15**	**10**	-	-
Covered bonds	**191**	**48**	-	-
Claims on Institutions and Corporates with a Short-term Credit Assessment	**-**	**-**	-	5
Claims in the Form of CIU	**4**	**4**	4	4
Equity Exposure	**9**	**11**	10	9
Other Items	**1,650**	**1,970**	1,905	2,023
Total	**48,561**	**47,798**	46,176	46,619

Total exposure value for credit risk as at 30 September 2016 was 5.2% higher compared to 30 September 2015. The increase in the Central Governments and Central Bank and Institutions credit risk exposure classes between reporting periods is due to increased repo transactions outstanding at 30 September 2016. There were no repo transactions outstanding at 30 September 2015.

The exposure amounts disclosed are pre-application of credit risk mitigation and pre-application of credit conversion factors, unless otherwise stated. This contrasts with the exposures disclosed within the Risk Report in the Annual Report and Accounts for the year ended 30 September 2016, which are disclosed before any relevant credit risk mitigation and after credit conversion factors have been applied.

5 Average Credit Risk Exposure is calculated using the previous four quarters exposure per the EBA's Common Reporting 'Credit Risk Standardised Approach' returns.

Table 12: Credit Risk Exposure by Industry

The table below shows credit risk exposure by the customer industry classification, including SME exposures. The regulatory SME definition is based on customers with an annual turnover not exceeding EUR 50 million. This is consistent with the SME definition in CRR article 501, which states that among the criteria listed in Commission Recommendation 2003/361/EC (concerning the definition of micro, small and medium-sized enterprises) only the annual turnover is to be taken into account. The table below is based on the customer industry identifier used for credit risk purposes and may differ from classifications used for other external reporting.

As at 30 September 2016

`Exposure Type	Government and public authorities	Agriculture forestry, fishing and mining	Financial, investment and insurance	Real estate - construction	Manufacturing	Personal Lending	Real estate – mortgage	Asset and lease financing	Other commercial and industrial	Non-customer assets	**Total**
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	**£m**
Governments or Central Banks	1,333	-	5,670	-	-	-	-	-	-	-	**7,003**
Regional Government or Local Authority	527	-	-	-	-	-	-	-	-	-	**527**
Public Sector Entities	45	-	-	-	-	-	-	-	18	-	**63**
Multilateral Development Banks	-	-	195	-	-	-	-	-	-	-	**195**
Institutions	-	-	1,345	-	-	-	-	-	-	-	**1,345**
Corporates	-	460	314	269	1,069	-	-	283	3,719	-	**6,114**
Retail	-	-	-	-	-	3,053	-	-	-	-	**3,053**
Secured by Mortgages on Immovable Property	-	1,646	24	53	274	-	23,501	16	2,532	-	**28,046**
Exposures in Default	-	33	1	3	5	14	162	-	128	-	**346**
Items associated with particularly high risk	-	-	-	-	-	-	-	-	15	-	**15**
Covered bonds	-	-	191	-	-	-	-	-	-	-	**191**
Claims in the Form of CIU	-	-	-	-	-	-	-	-	4	-	**4**
Equity Exposures	-	-	-	-	-	-	-	-	9	-	**9**
Other Items	121	-	1,312	-	-	-	1	-	81	135	**1,650**
Total Exposure	2,026	2,139	9,052	325	1,348	3,067	23,664	299	6,506	135	**48,561**
Of which: SME	-	1,905	102	178	872	-	-	179	3,831	-	**7,067**

As at 30 September 2015

Exposure Type	Government and public authorities	Agriculture forestry, fishing and mining	Financial, investment and insurance	Real estate – construction	Manufacturing	Personal Lending	Real estate – mortgage	Asset and lease financing	Other commercial and industrial	Non-customer assets	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Central Governments or Central Banks	1,282	-	5,195	-	-	-	-	-	-	-	6,477
Regional Government or Local Authority	594	-	-	-	-	-	-	-	-	-	594
Public Sector Entities	-	-	-	-	-	-	-	-	16	-	16
Multilateral Development Banks	-	-	100	-	-	-	-	-	-	-	100
Institutions	-	-	841	-	-	-	-	-	-	-	841
Corporates	-	504	225	275	1,055	-	-	232	3,623	-	5,914
Retail	-	-	-	-	-	3,125	-	-	-	-	3,125
Secured by Mortgages on Immovable Property	-	1,652	19	59	280	-	22,212	21	2,580	-	26,823
Exposures in Default	-	29	-	8	7	16	151	-	156	-	367
Items associated with particularly high risk	-	-	-	-	-	-	-	-	-	-	-
Covered bonds	-	-	-	-	-	-	-	-	-	-	-
Claims in the Form of CIU	-	-	-	-	-	-	-	-	4	-	4
Equity Exposures	-	-	-	-	-	-	-	-	10	-	10
Other Items	106	-	1,519	-	-	-	1	-	75	204	1,905
Total Exposure	1,982	2,185	7,899	342	1,342	3,141	22,364	253	6,464	204	46,176
Of which: SME	-	1,862	77	181	807	-	-	145	3,694	-	6,766

6.2 Credit risk exposure: analysis by residual maturity

Table 13: Credit Risk Exposure by Residual Maturity

Exposure Type	At 30 September 2016 <= 1 year £m	>1 year, <= 5 years £m	>5 years £m	Undated £m	**Total £m**
Central Governments or Central Banks	5,630	21	1,285	67	**7,003**
Regional Government or Local Authority	515	1	11	-	**527**
Public Sector Entities	63	-	-	-	**63**
Multilateral Development Banks	-	170	25	-	**195**
Institutions	180	600	2	563	**1,345**
Corporates	3,372	2,333	295	114	**6,114**
Retail	2,399	566	88	-	**3,053**
Secured by Mortgages on Immovable Property	2,561	2,875	22,610	-	**28,046**
Exposures in Default	120	85	141	-	**346**
Items associated with particularly high risk	10	5	-	-	**15**
Covered bonds	20	145	26	-	**191**
Claims in the Form of CIU	-	-	4	-	**4**
Equity Exposures	9	-	-	-	**9**
Other Items	-	-	-	1,650	**1,650**
Total	14,879	6,801	24,487	2,394	**48,561**

Exposure Type	At 30 September 2015 <= 1 year £m	>1 year, <= 5 years £m	>5 years £m	Undated £m	Total £m
Central Governments or Central Banks	5,154	-	1,279	44	6,477
Regional Government or Local Authority	582	1	11	-	594
Public Sector Entities	16	-	-	-	16
Multilateral Development Banks	-	100	-	-	100
Institutions	173	1	-	667	841
Corporates	3,299	2,176	346	93	5,914
Retail	2,419	599	107	-	3,125
Secured by Mortgages on Immovable Property	2,657	2,702	21,464	-	26,823
Exposures in Default	109	113	145	-	367
Claims in the Form of CIU	-	4	-	-	4
Equity Exposures	10	-	-	-	10
Other Items	-	-	-	1,905	1,905
Total	14,419	5,696	23,352	2,709	46,176

The maturity of exposures is shown on a contractual basis rather than the actual redemptions experienced by the Group. Undrawn values have been allocated to the contractual maturity of the underlying exposure. 2015 figures have been restated to reallocate £37m within the corporates exposure class from '1-5 years' to 'more than 5 years' for consistency with the refined 2016 approach.

6.3 Credit risk exposure: analysis by geography

Table 14: Credit Risk Exposure by Geography

Exposure Type	At 30 September 2016 UK £m	Other £m	Total £m
Central Governments or Central Banks	6,982	21	**7,003**
Regional Government or Local Authority	527	-	**527**
Public Sector Entities	63	-	**63**
Multilateral Development Banks	-	195	**195**
Institutions	1,315	30	**1,345**
Corporates	6,113	1	**6,114**
Retail	3,040	13	**3,053**
Secured by Mortgages on Immovable Property	28,005	41	**28,046**
Exposures in Default	346	-	**346**
Items associated with particularly high risk	15	-	**15**
Covered bonds	191	-	**191**
Claims in the Form of CIU	4	-	**4**
Equity Exposures	9	-	**9**
Other Items	1,650	-	**1,650**
Total Exposure	48,260	301	**48,561**

Exposure Type	At 30 September 2015 UK £m	Other £m	Total £m
Central Governments or Central Banks	6,477	-	6,477
Regional Government or Local Authority	594	-	594
Public Sector Entities	16	-	16
Multilateral Development Banks	-	100	100
Institutions	841	-	841
Corporates	5,913	1	5,914
Retail	3,110	15	3,125
Secured by Mortgages on Immovable Property	26,772	51	26,823
Exposures in Default	366	1	367
Claims in the Form of CIU	4	-	4
Equity Exposures	10	-	10
Other Items	1,905	-	1,905
Total Exposure	46,008	168	46,176

Credit risk exposures outside of the UK arising on lending are not material and have been classified as 'Other'. The geographical location is based on the physical location of the counterparty with which the Group deals. In some cases this may differ from the location of the counterparty's ultimate parent company. Exposures arising on supranational bonds issued by multilateral development banks are held as part of the Group's liquidity buffer. In line with guidance issued by the EBA, these have been classified to the geographical area 'Other' irrespective of the location of the issuer.

6.4 Impaired lending and provisions

6.4.1 Definition

The following definitions are employed:

- 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.
- impairment provisions: a provision held on balance sheet to recognise that a loan is impaired. This can be at either the individual or collective level.
- a collective impairment provision: an 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.
- 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.

6.4.2 Managing impaired exposures and impairment provisions

Provisioning policy

The management of impaired assets, the setting of impairment provisions and the write-off of impaired assets are included with the Group's Credit Policy and Procedures, and are reviewed on an annual basis. The treatment of impaired assets is determined by the Risk function and the calculation of impairment provisions aligns with current accounting policy, as agreed with the Finance function.

Accounting policy

The Group first assesses whether objective evidence of impairment exists individually for loans and advances that are individually significant, and individually or collectively for loans and advances that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed loan, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment.

Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment. The amount of impairment loss is 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 amount of the loss is recognised using an allowance account and the amount of the loss is included in the income statement.

For the purposes of a collective evaluation of impairment, loans and advances are grouped on the basis of similar risk characteristics, taking into account asset type, industry, geographical location, collateral type, past-due status and other relevant factors. These characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the counterparty's ability to pay all amounts due according to the contractual terms of the assets being evaluated. The Group uses historical loss experience and its experienced judgement to estimate the amount of an impairment loss. This incorporates amounts calculated to overcome model deficiencies and systemic risks where appropriate and supported by historic loss experience data. The use of such judgements and reasonable estimates is considered by management to be an essential part of the process.

Adequacy reviews

All impaired lending assets are reviewed on a continual basis and must be formally reviewed at least quarterly.

All non-impaired lending is subject to a collective assessment for pools of assets with similar credit risk characteristics where no objective evidence of impairment exists. The provisioning policy requires impairment losses to be based on events which have already taken place and prevailing economic conditions.

Reporting

The formal reporting of impaired lending, provisions and associated relevant asset quality metrics and trends are completed on a monthly basis and distributed to the appropriate portfolio managers, Senior Managers, Executive Committees, Risk Committee and Board.

The Group reviews, at least bi-annually, its provision reserves against actual experience to identify whether its policies have resulted in over or under provisioning across the economic cycle. The responsibility for the review rests with the Risk function which reports its findings and recommendations to the Risk Committee, and the Board.

Management of customers experiencing financial difficulties

Information and analysis on the measures adopted by the Group to support customers experiencing financial difficulties are detailed in the Risk Report section of the Group's Annual Report and Accounts.

6.5 Analysis of past due and impaired loans and advances to customers

As at 30 September 2016, past due but not impaired exposures in respect of loans and advances to customers amounted to £473m (2015: £483m). Impaired exposures in respect of loans and advances to customers amounted to £233m (including £19m of fair value loans) (2015: £263m (including £25m of fair value loans)). In the tables that follow the process to allocate provision overlays between line items has been refined in 2016. 2015 values have been restated to show allocation on a consistent basis.

6.6 Analysis by industry sector

An analysis of past due but not impaired loans and advances to customers and impaired loans and advances to customers, by industry sector, is provided in the table below:

Table 15: All Past Due and Impaired Loans and Advances to Customers by Industry

As at 30 September	2016 Past due but not impaired £m	2016 Impaired £m	2015 Past due but not impaired £m	2015 Impaired £m
Agriculture, forestry, fishing and mining	**64**	**20**	63	13
Asset and lease financing	**5**	**3**	2	3
Financial, investment and insurance	**2**	**-**	2	-
Personal Lending	**33**	**-**	37	-
Manufacturing	**6**	**22**	6	4
Other commercial and industrial	**76**	**121**	100	175
Real estate - construction	**2**	**1**	5	2
Real estate - mortgage	**285**	**66**	268	66
Total	**473**	**233**	483	263

6.7 Analysis by geography

All past due but not impaired loans and advances to customers and impaired loans and advances to customers are categorised as being in the United Kingdom. All closing impairment provisions, the net charge to the income statement, and advances written off in respect of loans and advances to customers are categorised as being in the United Kingdom.

6.8 Analysis of impairment provisions in respect of loans and advances to customers

The movement in impairment provisions, from 1 October 2015 to 30 September 2016, is provided below:

Table 16: The Movement in Impairment Provisions (Includes Fair Value)

	Specific Provisions		Collective Provisions		Total Provisions	
	2016 £m	2015 £m	**2016 £m**	2015 £m	**2016 £m**	2015 £m
Opening balance	**103**	141	**165**	178	**268**	319
Other adjustments[6]	**(3)**	(2)	**-**	(8)	**(3)**	(10)
Advances written off	**(71)**	(113)	**-**	-	**(71)**	(113)
Recoveries of advances written off in previous years	**18**	12	**-**	-	**18**	12
Charge to the income statement	**25**	65	**2**	(5)	**27**	60
Closing balance	**72**	103	**167**	165	**239**	268

6 Other adjustments relate to transfers to Net Present Value Provision Amortisation and Fair Value Accounting Adjustments.

6.9 Analysis by industry

The movement in total impairment provisions, from 1 October 2015 to 30 September 2016, by industry sector is provided below:

Table 17: Analysis of Impairment Provisions by Industry (including Fair Value)

As at 30 September	2016 Impairment Provisions £m	2016 Net Charge £m	2016 Advances Written Off £m	2015 Impairment Provisions £m	2015 Net Charge £m	2015 Advances Written Off £m
Agriculture, forestry, fishing and mining	**23**	**4**	**(3)**	22	1	-
Asset and lease financing	**2**	**1**	**-**	2	-	(1)
Financial, investment and insurance	**2**	**2**	**(3)**	4	3	(2)
Personal Lending	**19**	**7**	**(27)**	23	15	(30)
Manufacturing	**22**	**8**	**(8)**	22	8	(2)
Other commercial and industrial	**129**	**4**	**(27)**	152	14	(70)
Real estate - construction	**3**	**-**	**(1)**	4	1	(2)
Real estate - mortgage	**39**	**1**	**(2)**	39	18	(6)
Total	**239**	**27**	**(71)**	268	60	(113)

6.10 Use of ECAIs

The Group makes limited use of credit assessments by external credit assessment institutions ("ECAIs") in assigning risk weights to credit risk exposures under the standardised approach. This typically applies in the case of certain Central Government, Central Bank and Institution exposures.

Where a credit assessment is used this must be provided by an eligible ECAI from the PRA's approved list. The appropriate risk weight to apply to the credit risk exposure is determined by assigning the exposure to the relevant credit quality step under CRR Part 3, Title II, Chapter 2 (Standardised Credit Risk), based on the EBA's mapping of credit assessments to credit quality steps.

Where appropriate, the Group makes use of credit assessments provided by Moody's. Previously the Group also used Standard and Poor's ("S&P") and Fitch credit assessments for certain exposures. This was reviewed and revised following the demerger from NAB during 2016, taking into account the limited use of credit assessments outside of Central Governments or Central Banks and Institution exposures.

The table below shows exposure by credit quality step pre- and post-application of credit risk mitigation but before credit conversion factors. For Retail exposures secured by mortgages the protection effect of mortgage collateral is intrinsically part of the definition of the original exposure class.

Table 18: Exposure Values associated with Credit Quality Step

	Credit Quality Step ("CQS")	2016		2015	
		Exposure Pre Mitigation £m	Exposure Post Mitigation £m	Exposure Pre Mitigation £m	Exposure Post Mitigation £m
Central Governments or Central Banks	CQS 1	7,003	6,463	6,477	6,477
Regional Government or Local Authority	Unrated	527	433	594	480
Public Sector Entities	CQS 1	46	46	-	-
	Unrated	17	17	16	16
Multilateral Development Banks	CQS 1	195	195	100	100
Institutions	CQS 1	633	633	736	736
	CQS 2	601	115	1	1
	CQS 3	9	9	34	34
	CQS 4	-	-	5	5
	Unrated	102	102	65	65
Corporates	CQS 1	7	7	7	7
	CQS 3	16	16	12	12
	Unrated	6,091	6,010	5,895	5,774
Retail	Unrated	3,053	3,053	3,125	3,125
Secured by Mortgages on Immovable Property	Unrated	28,046	28,003	26,823	26,778
Exposures in Default	Unrated	346	346	367	367
Exposures associated with particularly high risk	Unrated	15	15	-	-
Exposures in the form of covered bonds	CQS 1	191	191	-	-
Collective investments undertakings (CIU)	Unrated	4	4	4	4
Equity Exposures	Unrated	9	9	10	10
Other Items	Unrated	1,650	1,650	1,905	1,905
Total Exposure		48,561	47,317	46,176	45,896

6.11 Credit risk mitigation

The Group uses a range of approaches to mitigate credit risk. The Group has a RAS and comprehensive credit risk management policies that restrict the level of exposure to any one borrower or group of borrowers, industries and countries.

6.11.1 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 varies, 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.

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 valuers or indexed valuation subject to policy rules and confidence levels.

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. Table 19 shows the non-property collateral held at 30 September 2016 in terms of cash and guarantees (these guarantors are predominantly other financial institutions who are considered to be of a high credit quality).

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 Credit Risk 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, 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, by product, by geographical region and by 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 focussing particularly on comparing the portfolio against market benchmarks.
- Single Large Exposure excesses: All excesses are reported to the Transactional Credit Committee ("TCC") and CCO. 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.

The table below shows separately for each exposure class, the total exposure (after, where applicable, on- or off-balance sheet netting) that is covered by (i) eligible collateral; and, (ii) guarantees.

Table 19: Use of credit risk mitigation techniques

As at 30 September	**2016**		2015	
Exposure Type	**Guarantees £m**	**Eligible Collateral £m**	Guarantees £m	Eligible Collateral £m
Central Governments or Central Banks	**-**	**721**	-	-
Institutions	**-**	**504**	-	-
Corporates	**40**	**49**	53	64
Secured by Mortgages on Immovable Property	**-**	**6**	-	6
Total	**40**	**1,280**	53	70

The increase in total eligible collateral held is due to increased repo transactions outstanding at 30 September 2016, reflected within institutions and central governments or central banks. There were no repo transactions outstanding at 30 September 2015.

Corporates is the largest sector utilising other risk mitigation techniques, with all methods used dependent on credit quality. The extent to which these will be used will be dependent on the specific circumstances of the customer. As at 30 September 2016 the Group held £164m of collateral in relation to on balance sheet netting (2015: £209m).

6.11.2 Treasury

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 is only 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 customer's 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 which 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 if contracts are settled via an exchange or clearing house.

7.1 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 the identification, assessment, mitigation, monitoring and reporting of risks and events is applied consistently.

The Group has identified, assessed and is currently monitoring all key operational risks across the Basel II 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 the Basel II event types 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 documents a proposed response to identify how the scenarios would be managed and monitored if they occurred.

Risk Category	
Customer, products and sales practices	The risks associated with the fair treatment of customers and the potential customer impact on all the Group's core activities.
Regulatory environment and market practices	The risks associated with ensuring the Group complies with a large volume of laws and regulations, including managing regulatory change.
Payments and process management	The risks associated with the management of large volumes of transactions, including ensuring core processing activities are conducted safely and efficiently.
Workplace practices and environment	The risks associated with failing to provide a safe environment for customers and colleagues, including ensuring there is adequate capacity of resource, with clearly defined objectives and an effective and efficient management structure in place.
Systems and infrastructure	The risks associated with failing to maintain the Group's systems and infrastructure, including as a result of a potential cyber-attack.
Third party providers	The risks associated with failing to manage third party providers effectively, which may also impact on the level of service available to customers.
Strategic Execution Risk	The risks associated with failing to manage change effectively, including the ability to define and deliver a plan that enables the Group to meet its strategic objectives.

7.2 Measurement

The Group calculates its operational risk capital requirements under the standardised approach ("TSA"). The capital requirement is calculated using the historic three year average risk weighted income method where different income streams are allocated a different risk weighting.

7.3 Operational risk RWAs and capital requirement

The capital requirement calculated under TSA at 30 September 2016 was £130 million (2015: £127 million). The capital charge is included in Table 9.

The table below shows movements in RWAs for operational risk from 1 October 2015 to 30 September 2016.

Table 20: Operational risk RWAs

Operational risk RWAs	£m
As at 1 October 2015	1,589
Movement	34
As at 30 September 2016	**1,623**

The increase in RWAs for operational risk is due to the increase in revenue generated by the Group over the last three years compared to the three years prior to 30 September 2015. The Group recognises the limitations of TSA and applies a more granular firm specific assessment as part of Pillar 2.

8.1 Objectives and roles in relation to securitisation activity

The Group has established two master trust Residential Mortgage Backed Security ("RMBS") securitisation programmes which provide the Group with term funding via public debt capital markets and potential contingent liquidity. The master trust structure facilitates the issuance of multiple series of notes which can have different rated tranches, tenor and repayment features tailored specifically to investor preference. Each series of notes is supported by the same pool of mortgage assets that can be replenished, subject to eligibility criteria, as the trust reduces in size due to prepayments.

The master trust structure comprises three Special Purpose Vehicles ("SPVs") which legally isolate the underlying mortgage assets beyond the reach of the Group and its creditors in a bankruptcy, winding-up or receivership event. The three SPVs are:

- Mortgages Trustee – The purpose of which is to acquire mortgage assets and their related security from the Bank and Yorkshire Bank Home Loans Limited and hold such mortgage assets and their related security on trust.
- Funding – The purpose of which is to purchase a beneficiary share in the trust property, using the proceeds of an inter-company loan from the Master Issuer.
- Master Issuer – The purpose of which is to issue RMBS notes which represent the mortgage backed obligations, and to lend the note proceeds to Funding under the inter-company loan arrangements.

8.2 Roles

The Group's roles in the securitisation programmes are sponsor, originator, servicer, cash manager and transaction account provider. The obligations in these roles are outlined in the transaction documents in accordance with market practice and regulatory requirements.

The master trust structures are supported by fully funded reserve accounts that are sized according to rating agency requirements. The reserve accounts are funded from a subordinated loan from the Bank. The programmes have to date repaid all outstanding subordinated loans. The Bank also provides a start-up loan for each issuance. This loan provides for fees charged in relation to new issuances and is repaid in the form of revenue receipts generated by the asset pool.

The Group is under no obligation to support any losses incurred by the securitisation programmes or noteholders. The principal and interest received from the mortgage assets are used to repay note principal and meet interest payments.

8.3 Associated risks

The Group has not sought to obtain regulatory capital relief from securitisation as significant risk transfer is not achieved. Capital is therefore calculated in accordance with the underlying risk weighting on the balance sheet. The principal risks within the securitised transformation are:

- credit risk: the risk that borrowers fail to meet their obligations as and when they fall due. This risk is assessed by credit rating agencies both at note issuances and on an ongoing basis. All Class A notes have a AAA credit rating from Moody's, Fitch and S&P. The Group monitors the performance of its mortgage book and the securitisation portfolio by assessing key metrics such as arrears, loan-to-value and geographic distributions.
- prepayment risk: the risk that Customers could prepay all or part of their outstanding debt before the maturity of outstanding bonds. This risk is factored into credit rating agencies cash flow models and is mitigated through mortgage substitution or pool replenishment.
- basis risk: there is a fixed-floating interest rate mismatch between the mortgage pool assets and the 3 month Sterling LIBOR linked intercompany loan. To mitigate this risk, Funding has entered into interest rate swap agreements.
- foreign exchange rate risk: there is a mismatch between the GBP denominated intercompany loan between Funding and Master Issuer, and the amounts payable to non-GBP denominated noteholders. This risk is mitigated by a balance guaranteed cross currency swap. Where there are non-GBP tranches, cross currency swaps have been executed with suitably rated counterparties to mitigate foreign exchange currency risk.
- call risk: there is a risk that any notes are not called on their respective call dates.
- liquidity risk: there is a mismatch between the capital and interest payments on the underlying mortgage assets and the capital and interest payments through securitisation structures to investors.

The Group retains credit risks associated with the mortgage assets as these remain on-balance sheet. The risk to the programme is mitigated by the over collateralisation of mortgage assets, seller share and reserve accounts.

8.4 Issuer and retained positions

In August 2007, the Group launched the inaugural issuance from Lanark Master Trust ("Lanark"). The asset pool originally comprised of owner-occupied residential mortgage loans and a small amount of buy to let ("BTL") loans. In June 2011, BTL loans were removed from the Lanark mortgage pool and replaced with owner-occupied residential mortgage loans.

To date, there have been eight issuances from Lanark. An external credit rating assessment is provided and monitored by Moody's, Fitch and S&P. All outstanding Class A notes are rated AAA.

Credit enhancement for the securitisation structures is provided by subordinated Class Z Notes representing specific reserves and excess spread. The Group retains the Class Z Note in the form of an amortising variable funding note ("Z VFN"). The Group securitised a pool of owner-occupied residential mortgages via the Lanark programme in August 2016 with the issuance of £750m GBP-denominated floating rate notes in Lanark 2016-1.

In September 2011, the Group established Lannraig Master Trust ("Lannraig"). The asset pool is made up exclusively of BTL mortgage loans. To date, there have been two issuances from Lannraig. External credit rating assessments are provided by Moody's, Fitch and S&P. All outstanding Class A notes are rated AAA and have been sold or retained by the Group. Credit enhancement for the securitisation structures is provided by subordinated Class Z Notes representing specific reserves and excess spread. The Group retains the Class Z Note in the form of an amortising Z VFN.

Table 21: Outstanding notes

At 30 September 2016, the outstanding notes are:

Issuer	Class A Notes	Class Z Notes	Total retained position
Lanark Master Issuer plc	£2,856m	£396m	£396m
Lannraig Master Issuer plc	£1,187m	£214m	£1,049m

Table 22: On balance sheet securitised exposures

As at 30 September 2016, on balance sheet securitised exposures are:

Issuer	Mortgage Asset pool	Impaired and 90 days Past Due
Lanark Trustee Ltd	£3,898m	£25m
Lannraig Trustee Ltd	£1,537m	£10m

The SPVs are fully consolidated in the Group's Annual Report and Accounts.

The Group does not have any synthetic securitisations outstanding or any re-securitisations.

8.5 Securitisation accounting policies

The Bank has sold mortgages to the securitisation vehicles. However, these mortgages continue to be recognised on the Group's balance sheet. The mortgages do not qualify for de-recognition from the balance sheet because the Group remains exposed to the risks and rewards of ownership on an ongoing basis. It is exposed primarily to the credit risk, liquidity risk and interest rate risk of the mortgages. The Group is also exposed to the residual rewards of the mortgages as a result of its ability to benefit from the future performance of the mortgages through the receipt of deferred consideration.

9.1 Overview

The term encumbrance is used to denote those assets on a bank's balance sheet which have been pledged as security, collateral or legally 'ring-fenced' in some other way which prevents the firm from being able to transfer, pledge, sell or otherwise use/dispose of these assets.

These disclosures are based on the EBA guidelines on disclosure of encumbered and unencumbered assets, the PRA's Supervisory Statement 11/14 and the "Dear CFO" letter from the PRA dated December 2015.

9.2 Debt securities

Sale and repo transactions are used, in the ordinary course of business, to manage short-term cash flow requirements and mismatches. A repo transaction involves the pledge of marketable securities as security in exchange for receiving a deposit. During the period of the repo, the securities pledged become encumbered. The Group has entered into a number of repo agreements with a range of market counterparties.

In addition, during the year the Group entered into a term repo transaction using self-issued RMBS notes as collateral. This transaction provided term funding to the Group.

The Bank is a direct participant in a number of payment and clearing systems, all of which require collateral to be posted to support its obligations. Where the collateral requirements are met with marketable securities, the securities pledged become encumbered.

9.3 Loans and advances - mortgage encumbrance

The Group's wholesale term funding requirements are currently met via issuance from SPVs. These structured issuances result in a portion of the Group's mortgage assets becoming encumbered.

The Group has three structured funding programmes: two securitisation Master Trust structures as outlined in section 8 and one RCB programme ("Clydesdale Covered Bonds No. 2 LLP"), also backed by residential mortgages.

Over-collateralisation levels are embedded in each programme to meet the minimum levels as specified by the programme documents and as agreed with the ratings agencies and regulators to mitigate certain legal risks, such as set-off rights.

The SPVs also hold cash balances in segregated Guaranteed Investment Contract ("GIC") bank accounts. The use of these balances is restricted to the repayment of debt securities issued by the SPVs and other legal obligations associated with these structures. These balances are, therefore, considered by the Group to be encumbered.

From time to time cash held in the GIC accounts is invested for a short term in Certificates of Deposit ("CDs") issued by highly rated counterparties. The purpose of these transactions is to manage concentration risk. The use of these CDs is similarly restricted so they are also considered to be encumbered.

9.4 Other assets

Note cover

Under Part 6 of the Banking Act 2009, banks in Scotland and Northern Ireland which issue bank notes are required to hold backing assets for their notes at all times. Banks may use a combination of Bank of England notes, UK coin and funds held in specific bank accounts at the Bank of England. As a result of this permanent requirement for note-issuing banks to provide 100% 'cover' for the value of their bank notes in circulation at all times, note cover requirements are considered to be encumbered assets. If note issuance increases then additional cash balances are required to be placed with the Bank of England. However, as this process creates equal and offsetting liabilities for the assets encumbered there is no material risk to depositors or the Group.

Cash ratio deposit

Cash Ratio Deposits are non-interest bearing deposits lodged with the Bank of England by eligible institutions (i.e. banks and building societies), who have reported average eligible liabilities of over £600 million over a calculation period. The level of each institution's Cash Ratio Deposit is currently calculated twice-yearly (currently in May and November) at 0.18% of average eligible liabilities, over the previous six end-calendar months, in excess of £600m. Due to the permanent nature of the Cash Ratio Deposit, the requirement is considered to be an encumbered asset.

Cash margin

As noted above, a repo transaction involves the pledge of marketable securities as security in exchange for receiving a deposit. During the period of the repo, the market value of the securities pledged fluctuates whilst the value of the underlying cash deposit remains fixed. To account for the fluctuations in the market value of the securities, additional cash ('margin') is passed between the parties. Where the Group has paid out additional cash margin, this is treated as encumbered by the Group.

Likewise, where the Group has entered into a derivative with another market counterparty, the market value of the derivative fluctuates with changes in market rates. To account for the fluctuations in market value, additional margin is passed between the parties. Where the Group has paid out cash margin, this is treated as encumbered by the Group.

Payment system collateral

The Group (via the Bank) is a direct participant in a number of UK payment and clearing systems, all of which require collateral to be posted to support the Group's obligations. The value of the cash or assets pledged is treated as encumbered.

The Group is a direct member of Trans-European Automated Real-time Gross Settlement Express Transfer ("Target2"). This is facilitated via an account held with the Dutch Central Bank which is funded as and when required to meet payments. The balance of this account is, therefore, treated as encumbered by the Group.

In general intangible assets, deferred tax assets, derivative fair values and other assets are not considered to be available for encumbrance in the normal course of business. Additional information is provided in the Risk Report in the Group's Annual Report and Accounts.

9.5 Encumbered assets

The amounts disclosed in table 23 and table 24 below are median values for the financial year 2016 calculated using quarterly data.

Table 23 shows the carrying and, where included in the regulatory templates, the fair value of encumbered and unencumbered assets by asset category. Table 24 shows the carrying value of encumbered assets and associated liabilities by sources of encumbrance. The disclosures are in accordance with PRA/EBA regulatory reporting requirements and as such differ from the disclosures contained in the Annual Report and Accounts as at 30 September 2016. Volatility in the level of encumbered assets is not significant and the use of monthly data is not expected to result in materially different information compared to the data below.

Table 23: Fair Value of Encumbered Assets (Template A)

	2016			
	Carrying amount of encumbered assets £m	Fair value of encumbered assets £m	Carrying amount of unencumbered assets £m	Fair value of unencumbered assets £m
Assets of the reporting institutions	10,201		29,125	
Equity instruments	-	-	10	10
Debt securities	118	118	1,454	1,454
Other assets	459		1,007	

	2015			
	Carrying amount of encumbered assets £m	Fair value of encumbered assets £m	Carrying amount of unencumbered assets £m	Fair value of unencumbered assets £m
Assets of the reporting institutions	10,230		28,364	
Equity instruments	-	-	6	6
Debt securities	388	388	932	932
Other assets	371		997	

Table 24: Encumbered Assets / Collateral Received & Associated Liabilities (Template C)

	2016		2015	
	Matching liabilities, contingent liabilities or securities lent £m	**Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered £m**	Matching liabilities, contingent liabilities or securities lent £m	Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered £m
Carrying amount of selected financial Liabilities	**5,092**	**7,681**	4,905	7,830

The Group has elected to apply the waiver available under PRA Supervisory Statement 11/14 regarding disclosure of details of collateral received and therefore Template B has not been disclosed.

10.1 Definition

The Group provides products to its customers in order to manage their interest rate, currency and commodity risk, and the Group in turn hedges this risk with other financial counterparties. In addition, the Group enters into sale and repurchase agreements with other financial counterparties for the purpose of liquidity risk management and funding.

Derivative and repo transactions give rise to credit exposures to counterparties. Counterparty credit risk ("CCR") is the risk that a counterparty to a transaction may default before the final settlement of the transaction's cash flows. This section describes the Group's approach to managing CCR concerning financial instruments, including derivatives and repurchase agreements.

10.2 Internal capital and credit limits

Counterparty credit limits for derivatives are approved and assigned by an appropriately authorised Delegated Commitment Authority ("DCA"). Limits are based on the credit quality of the counterparty and the appetite for the projected maximum potential future exposure of anticipated derivative transactions. They also reflect the nature of the relevant documentation, including whether or not the transaction is subject to regular exchange of margin. Credit exposures for each transaction are measured as the current mark-to-market value and the potential credit exposure which is an estimate of possible future changes in mark-to-market value replacement cost. Limit excesses, whether they are active or passive, are subject to formal approval by a DCA.

10.3 Securing collateral and establishing credit reserves

The risk that counterparties could default is mitigated by offsetting the amounts due to the same counterparties (i.e. netting) and by cash collateral deposited by counterparties (i.e. collateralisation).

Collateralisation reduces the credit exposure recorded against market transactions. Counterparty credit exposures may be collateralised by an approved list of eligible collateral via market standard master agreements (such as CSAs to ISDA Master Agreements and GMRAs). CCR policy governs types of acceptable collateral and that collateral which may be subject to haircuts depending on asset type. Systems support daily marking-to-market of net exposures and margin requirements, marking-to-market of collateral value and reconciliation of collateral receipt and holdings against collateral due.

10.4 Wrong way risk

Wrong way risk occurs when exposure to a counterparty increases when the credit quality of that counterparty deteriorates. This could happen, for example, where CCR is mitigated through the use of collateral issued by the counterparty. Our high quality collateral requirements mitigate this risk to a material extent. This is not considered to be material risk to the Group due to the types of credit mitigation that are in place.

10.5 Downgrade impact

The Group calculates, as part of its regular liquidity reporting, the amount of any additional collateral that would have to be posted in the event of a downgrade in its external rating. For transactions that would be affected by a downgrade clause, planning for, and the impact of, the event for the Group is managed by the Group's Treasury division.

10.6 Exposures

Counterparty credit risk exposures are first measured using the mark-to-market method and subsequently risk-weighted under the standardised approach. The Group calculates a CVA on external derivative transactions with financial counterparties. The Group has no exposures to credit derivatives as at 30 September 2016 (30 September 2015: £nil).

10.7 Counterparty credit risk exposures

An analysis by measurement approach, by exposure class, by risk weight approach and by contract type is presented in the table below:

Table 25: Counterparty credit risk exposure

	2016		2015	
	Exposure £m	RWA £m	Exposure £m	RWA £m
Mark to Market Approach:				
Interest Rate Contracts	**312**	**99**	235	87
Foreign Exchange Contracts	**198**	**102**	38	22
Commodities Contracts	**13**	**13**	31	29
	523	**214**	304	138

10.8 Net derivatives credit exposure

Details of the net derivatives credit exposure are set out below:

Table 26: Net derivatives credit exposure

As at 30 September	2016 £m	2015 £m
Gross positive fair value of contracts	**585**	285
Potential Future Credit Exposure	**270**	446
Netting Benefits	**(277)**	(671)
Net Current Credit Exposures	**578**	60
Collateral Pledged	**(55)**	244
Net Derivative Credit Exposure	**523**	304

11.1 Market risks

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.

11.2 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's 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;
- 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);
- VaR and EaR are measured on a statistical basis: 99% confidence level with appropriate holding periods depending on varying risk types;
- EaR utilises a twelve month forecast period;
- eight years of business day historical data is used in modelling;
- VaR methodology is based on proportional rather than absolute changes in historical interest rates;
- 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.

11.3 Management

Market risks are overseen by ALCO with delegation for day to day management given to the Group's Treasury division. The Group's Treasury division 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, using interest rate swaps.

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 transactions which are hedged using FX forward contracts. The fair value of derivatives is disclosed in note 15 of the Annual Report and Accounts.

11.4 Monitoring

Model parameters and assumptions are reviewed and updated on at least an annual basis. Material changes require the approval of ALCO. Oversight is conducted by the Group's Balance Sheet & Liquidity Risk Oversight team that is independent of the Treasury division. The Board and Executive Risk Committee, through ALCO's oversight, monitors risk to ensure it remains within approved policy, limits and Board requirements.

Table 27: Interest Rate Risk in the Banking Book

This table provides the increase or decrease in economic value for upward and downward rate shocks.

As at 30 September	**2016**		2015	
	200bp parallel increase £m	**200bp parallel decrease £m**	200bp parallel increase £m	200bp parallel decrease £m
Change in economic value	**44**	**(48)**	36	(35)

Note: Assuming that rates are floored at zero, the impact of the downward rate shock as at 30 September 2016 is £(17) million.

APPENDIX 1: DISCLOSURES FOR CLYDESDALE BANK PLC

The following tables present the disclosures required for the Bank on an individual consolidated basis. The differences between the Group and the Bank relate primarily to reserves held by entities that sit outside of the scope of the Bank solo consolidation that are included in the Group consolidation, a small impact from the risk weighted assets of these entities and AT1 capital issued by the Group. Some line items have been presented in an expanded format compared to the prior year to show additional detail. The comparative line items have been similarly expanded.

Table 28: Capital composition

As at 30 September		2016 £m	2015 £m
	Common Equity Tier 1 (CET1) capital: Instruments and reserves		
1	Capital instruments and the related share premium accounts	**324**	2,812
1a	Of which: Ordinary Shares	**324**	2,812
2	Retained earnings	**2,983**	435
3	Accumulated other comprehensive income (and other reserves)	**102**	(1)
6	**Common Equity Tier 1 (CET1) capital before regulatory adjustments**	**3,409**	3,246
	Common Equity Tier 1 (CET1) capital: regulatory adjustments		
7	Additional value adjustments	**(7)**	(2)
8	Intangible assets	**(256)**	-
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences	**(71)**	(273)
11	Fair value reserves related to gains or losses on cash flow hedges	**(67)**	-
15	Defined benefit pension fund assets	**-**	(42)
19	Direct, indirect and synthetic holdings of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount above 10% threshold and net of eligible short positions) (negative amount)	**-**	(318)
25a	Losses for the current financial year (negative amount)	**(617)**	(256)
28	**Total regulatory adjustments to Common Equity Tier 1 (CET1)**	**(1,018)**	(891)
29	**Common Equity Tier 1 (CET1) capital**	**2,391**	2,355
	Additional Tier 1 (AT1) capital: instruments		
30	Capital instruments and the related share premium accounts	**425**	450
31	of which: classified as equity under applicable accounting standards	**425**	450
36	**Additional Tier 1 (AT1) capital before regulatory adjustments**	**425**	450
44	**Additional Tier 1 (AT1) capital**	**425**	450
45	**Tier 1 Capital**	**2,816**	2,805
	Tier 2 (T2) capital: Instruments and provisions		
46	Capital instruments and the related share premium accounts	**479**	300
47	Amount of qualifying items referred to in Article 484 (5) and the related share premium accounts subject to phase out from T2	**-**	175
50	Credit risk adjustments	**151**	138
51	**Tier 2 (T2) capital before regulatory adjustment**	**630**	613
58	**Tier 2 (T2) capital**	**630**	613
59	**Total Capital**	**3,446**	3,418
60	Total risk weighted assets	**18,873**	17,795
	Capital Ratios		
61	Common Equity Tier 1	**12.7%**	13.2%
62	Tier 1	**14.9%**	15.8%
63	Total Capital	**18.3%**	19.2%

64	Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements plus a systemic risk buffer, plus systemically important institution buffer expressed as a percentage of total risk exposure amount)	**5.1%**	4.5%
65	of which: capital conservation buffer requirement	**0.6%**	0%
66	of which: countercyclical buffer requirement	**0%**	0%
67	of which: systemic risk buffer requirement	**0%**	0%
67a	of which: Global Systemically Important Institution (G-SII) or Other Systemically Important Institution (O-SII) buffer	**0%**	0%
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	**8.2%**	8.7%
	Applicable caps on the inclusion of provisions in Tier 2		
76	Credit risk adjustments included in T2 in respect of exposures subject to standardised approach (prior to the application of the cap)	**151**	138
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach	**213**	202

The Bank's individually consolidated CET1 ratio at 30 September 2016 is 12.7%, with the movement driven by similar factors as those driving the movement in the Group's ratio. Items specific to changes in the Bank's CET1 capital position were the successful completion of a court-approved reduction in share capital in August 2016, resulting in the nominal value of each ordinary share in the Bank being reduced from £1.00 to £0.10 per share and the payment of a dividend of £51.4m to CYBI.

The table below shows movements in the Bank's capital during 2016.

Table 29: Capital flow statement

	2016 £m	2015 £m
CET1 capital		
CET1 capital at 1 October	**2,355**	2,228
Share capital: ordinary share new issuance	**426**	770
Share premium transfer	**-**	(243)
Retained earnings and other reserves	**2,651**	227
Prudent valuation adjustment	**(5)**	-
Intangible assets	**(256)**	-
DTA relying on future profitability	**202**	(50)
Defined benefit pension fund assets	**42**	(3)
Share redenomination	**(2,914)**	-
Fair Value reserves related to gains or losses on cash flow hedges	**(67)**	-
Losses for the current financial year	**(361)**	(256)
CET1 instruments of financial sector entities where the institution has a significant investment	**318**	(318)
	2,391	2,355
Tier 1 capital		
Tier 1 capital at 1 October	**450**	-
Share capital repurchased: perpetual non-cumulative preference shares	**(450)**	-
Share capital issued: Additional Tier 1 capital perpetual notes	**-**	450
Share capital issued: Perpetual Subordinated Contingent Convertible Notes	**425**	-
	425	450
Total Tier 1 capital	**2,816**	2,805
Tier 2 capital		
Tier 2 capital at 1 October	**613**	1,211
Capital instruments repurchased: Subordinated debt redemption	**(475)**	(601)
Capital instruments issued: Subordinated debt	**479**	-
Credit risk adjustments	**13**	3
	630	613
Total capital at 30 September	**3,446**	3,418

Tier 1 capital

The Bank's Tier 1 capital comprises:

- ordinary shares;
- retained earnings;
- accumulated other comprehensive income (and other reserves);
- AT1 instruments; and
- adjustments as set out by the regulatory requirements governing capital resources.

Regulatory adjustments are made where appropriate. These are made on a consistent basis as the Group, described in section 4.

Tier 2 capital

Tier 2 capital comprises:

- subordinated loan debt;
- eligible collective impairment allowances; and
- adjustments as set out by the regulatory requirements governing capital resources.

Table 30: CRD IV end-point vs transitional comparison

		Current Rules		Full Impact	
	As at 30 September	**2016 £m**	2015 £m	**2016 £m**	2015 £m
	Common Equity Tier 1 (CET1) capital: Instruments and reserves				
1	Capital instruments and the related share premium accounts	**324**	2,812	**324**	2,812
1a	Of which: Ordinary Shares	**324**	2,812	**324**	2,812
2	Retained earnings	**2,983**	435	**2,983**	435
3	Accumulated other comprehensive income (and other reserves)	**102**	(1)	**102**	(1)
6	Common Equity Tier 1 (CET1) capital before regulatory adjustments	**3,409**	3,246	**3,409**	3,246
	Common Equity Tier 1 (CET1) capital: regulatory adjustments				
7	Additional value adjustments	**(7)**	(2)	**(7)**	(2)
8	Intangible assets (net of related tax liability)	**(256)**	-	**(256)**	-
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences	**(71)**	(273)	**(71)**	(273)
11	Fair value reserves related to gains or losses on cash flow hedges	**(67)**	-	**(67)**	-
15	Defined benefit pension fund assets	**-**	(42)	**-**	(42)
19	Direct, indirect and synthetic holdings of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount above 10% threshold and net of eligible short positions) (negative amount)	**-**	(318)	**-**	(318)
25a	Losses for the current financial year (negative amount)	**(617)**	(256)	**(617)**	(256)
28	Total regulatory adjustments to Common Equity Tier 1 (CET1)	**(1,018)**	(891)	**(1,018)**	(891)
29	Common Equity Tier 1 (CET1) capital	**2,391**	2,355	**2,391**	2,355
	Additional Tier 1 (AT1) capital: instruments				
30	Capital instruments and the related share premium accounts	**425**	450	**425**	450
31	of which: classified as equity under applicable accounting standards	**425**	450	**425**	450
36	Additional Tier 1 (AT1) capital before regulatory adjustments	**425**	450	**425**	450
44	Additional Tier 1 (AT1) capital	**425**	450	**425**	450
45	Tier 1 Capital	**2,816**	2,805	**2,816**	2,805
	Tier 2 (T2) capital: Instruments and provisions				
46	Capital instruments and the related share premium accounts	**479**	300	**479**	300
47	Amount of qualifying items referred to in Article 484 (5) and the related share premium accounts subject to phase out from T2	**-**	175	**-**	-
50	Credit risk adjustments	**151**	138	**151**	138
51	Tier 2 (T2) capital before regulatory adjustment	**630**	613	**630**	438

58	Tier 2 (T2) capital	**630**	613	**630**	438
59	Total Capital	**3,446**	3,418	**3,446**	3,243
60	Total risk weighted assets	**18,873**	17,795	**18,873**	17,795
	Capital Ratios				
61	Common Equity Tier 1	**12.7%**	13.2%	**12.7%**	13.2%
62	Tier 1	**14.9%**	15.8%	**14.9%**	15.8%
63	Total Capital	**18.3%**	19.2%	**18.3%**	18.2%
64	Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements plus a systemic risk buffer, plus systemically important institution buffer expressed as a percentage of total risk exposure amount)	**5.1%**	4.5%	**7.0%**	4.5%
65	of which: capital conservation buffer requirement	**0.6%**	0%	**2.5%**	0%
66	of which: countercyclical buffer requirement	**0%**	0%	**0%**	0%
67	of which: systemic risk buffer requirement	**0%**	0%	**0%**	0%
67a	of which: Global Systemically Important Institution (G-SII) or Other Systemically Important Institution (O-SII) buffer	**0%**	0%	**0%**	0%
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	**8.2%**	8.7%	**8.2%**	8.7%
	Applicable caps on inclusion of provisions in Tier 2				
76	Credit risk adjustments included in T2 in respect of exposures subject to standardised approach (prior to the application of the cap)	**151**	138	**151**	138
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach	**213**	202	**213**	202

Table 31: Reconciliation of statutory equity to regulatory capital

	2016 £m	2015 £m
Statutory total equity	**3,217**	3,443
Less pension regulatory adjustments	**-**	(42)
Less Additional Value Adjustment	**(7)**	(2)
Less intangible assets	**(256)**	-
Less share option reserve	**-**	(3)
Less deferred tax asset relying on future profitability	**(71)**	(273)
Less cash flow hedge	**(67)**	-
Less CET1 instruments of financial sector entities where the institution has a significant investment	**-**	(318)
Regulatory Tier 1 capital	**2,816**	2,805
Statutory Tier 2 subordinated debt	**479**	475
Regulatory Tier 2 subordinated debt	**479**	475

Table 32: Leverage Ratio

The Bank's individual consolidated leverage ratio is calculated on a basis consistent with that of the Group, as set out in section 4.4. The table below shows the calculation of the leverage ratio for the Bank as at 30 September.

As at 30 September	2016 £m	2015 £m
Total Tier 1 capital for the leverage ratio		
Total Common Equity Tier 1 (CET1) capital	**2,391**	2,355
Additional Tier 1 (AT1) capital	**425**	450
Total Tier 1	**2,816**	2,805
Exposures for the leverage ratio		
Total statutory assets as per the published financial statements	**41,696**	40,548
Adjustment for off balance sheet items	**1,982**	2,034
Adjustment for derivative financial instruments	**(359)**	23
Adjustment for securities financing transactions (SFTs)	**601**	-
Other adjustments	**(402)**	(635)
Leverage ratio exposure	**43,518**	41,970
Leverage ratio common disclosure		
On-balance sheet exposures (excluding derivatives and SFTs)		
On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	**41,308**	40,320
Asset amounts deducted in determining Tier 1 capital	**(402)**	(635)
Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets)	**40,906**	39,685
Derivative exposures		
Replacement cost associated with *all* derivative transactions	**291**	81
Add-on amounts for PFE associated with *all* derivatives transactions (mark-to-market method)	**75**	170
(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	**(337)**	-
Total derivatives exposures	**29**	251
SFT exposures		
Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions	**1,827**	-
(Netted amounts of cash payables and cash receivables of gross SFT assets)	**(1,226)**	-
Total securities financing transaction exposures	**601**	-
Other off-balance sheet exposures		
Off-balance sheet exposures at gross notional amount	**7,813**	8,096
Adjustment for conversion to credit equivalent amounts	**(5,831)**	(6,062)
Other off-balance sheet exposures	**1,982**	2,034

Capital and total exposure measure		
Tier 1 capital	**2,817**	2,804
Leverage ratio total exposure measure	**43,518**	41,970
Leverage ratio		
Leverage ratio	**6.5%**	6.7%
Choice on transitional arrangements and amount of derecognised fiduciary items		
Choice on transitional arrangements for the definition of the capital measure	**Full impact**	Full impact
Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures)		
Total on-balance sheet exposures (excluding derivatives, SFTs and exempted exposures), of which:	**41,308**	40,320
Banking book exposures, of which:		
- Covered bonds	**191**	-
- Exposures treated as sovereigns	**6,154**	6,576
- Exposures to regional governments, MDB, international organisations and PSE not treated as sovereigns	**12**	12
- Institutions	**324**	392
- Secured by mortgages of immovable properties	**25,807**	24,560
- Retail exposures	**1,124**	1,169
- Corporate	**2,847**	2,539
- Exposures in default	**337**	352
- Other exposures (e.g. equity, securitisations, and other non-credit obligation assets)	**4,512**	4,720

Table 33: Minimum capital requirement - Pillar 1

The following table shows the Bank's individual consolidated capital resources requirement under Pillar 1 as at 30 September 2016.

	2016		2015	
Pillar 1 Capital Requirements	**RWA £m**	**Capital £m**	RWA £m	Capital £m
Regional Government or Local Authority	**20**	**2**	22	2
Public Sector Entities	**5**	**-**	3	-
Institutions	**147**	**12**	131	11
Corporates	**3,547**	**284**	3,287	264
Retail	**897**	**72**	930	74
Secured by Mortgages on Immovable Property	**11,241**	**899**	10,862	869
Exposures in Default	**408**	**33**	427	34
Exposures associated with particularly high risk	**15**	**1**	-	-
Covered bonds	**19**	**2**	-	-
Claims in the Form of CIU	**3**	**-**	3	-
Equity Exposures	**26**	**2**	6	-
Other Items	**518**	**41**	337	27
Total Credit Risk	**16,846**	**1,348**	16,008	1,281
Credit Counterparty Risk	**174**	**14**	128	10
Credit Valuation Adjustment	**248**	**20**	135	11
Operational Risk	**1,605**	**128**	1,524	122
	18,873	**1,510**	17,795	1,424

The differences between the credit RWAs for the Group and those of the Bank relate primarily to exposures arising within the Group's securitisation vehicles in relation to the GIC account, partially offset by intercompany exposures which exist at Bank level but not at Group level. The difference in RWAs for counterparty credit risk relates to derivatives within the Group's securitisation vehicles.

APPENDIX 2: MAIN FEATURES OF REGULATORY CAPITAL INSTRUMENTS

1	Issuer	CYBG PLC	CYBG PLC	CYBG PLC	Clydesdale Bank PLC	Clydesdale Bank PLC	Clydesdale Bank PLC
2	ISIN	GB00BD6GN030	XS1346644799	XS1346646901	n/a	n/a	n/a
3	Governing law	English	English	English	English	English	English
	Regulatory treatment						
4	Transitional CRR rules	Common Equity Tier 1	Additional Tier 1	Tier 2	Common Equity Tier 1	Additional Tier 1	Tier 2
5	Post-transitional CRR rules	Common Equity Tier 1	Additional Tier 1	Tier 2	Common Equity Tier 1	Additional Tier 1	Tier 2
6	Eligible at Group or Bank	CYBG Group	CYBG Group	CYBG Group	CB Solo Consolidated	CB Solo Consolidated	CB Solo Consolidated
7	Instrument type (type to be specified by each jurisdiction)	Ordinary Shares	Additional Tier 1 – Fixed Rate Reset Perpetual Subordinated Contingent Convertible Notes	Fixed Rate Reset Callable Subordinated Tier 2 Notes due 2026	Ordinary Shares	Additional Tier 1 – Fixed Rate Reset Perpetual Subordinated Permanent Write Down Notes	Fixed Rate Reset Callable Subordinated Tier 2 Notes due 2026
8	Regulatory capital value	88,153,185	449,658,000	473,542,700	323,709,449	425,431,130	479,331,796
9	Nominal value (£)	88,153,185	450,000,000	475,000,000	323,709,449	450,000,000	475,000,000
9a	Issue price (£)	88,153,185	449,658,000	473,318,500	323,709,449	425,431,130	479,998,226
9b	Redemption price (£)	88,153,185	450,000,000	475,000,000	323,709,449	450,000,000	475,000,000
10	Accounting classification	Equity	Equity	Liability - amortised cost	Equity	Equity	Liability - amortised cost
11	Original date of issue	Various	8th February 2016	8th February 2016	Various	8th February 2016	8th February 2016
12	Perpetual or dated	Perpetual	Perpetual	10-year non-call 5-years	Perpetual	Perpetual	10-year non-call 5-years
13	Original maturity date	n/a	n/a	9th February 2026	n/a	n/a	9th February 2026
14	Issuer call subject to prior supervisory approval	n/a	Yes	Yes	n/a	Yes	Yes
15	First call date	n/a	8th December 2022	8th February 2021	n/a	8th December 2022	8th February 2021

16	Subsequent call dates	n/a	Any Distribution payment date thereafter	Any interest payment date thereafter	n/a	Any Distribution payment date thereafter	Any interest payment date thereafter
	Coupons / dividends						
17	Fixed or floating dividend/coupon	n/a	Fixed	Fixed	n/a	Fixed	Fixed
18	Coupon rate and any related index	n/a	8%	5%	n/a	8%	5%
19	Existence of a dividend stopper	n/a	No	No	n/a	No	No
20a	Fully discretionary, partially discretionary or mandatory (in terms of timing)	Fully discretionary	Fully discretionary	Mandatory	Fully discretionary	Fully discretionary	Mandatory
20b	Fully discretionary, partially discretionary or mandatory (in terms of timing)	Fully discretionary	Fully discretionary	Mandatory	Fully discretionary	Fully discretionary	Mandatory
21	Existence of step up or other incentive to redeem	n/a	No	No	n/a	No	No
22	Non-cumulative or cumulative	Non-cumulative	Non-cumulative	n/a	Non-cumulative	Non-cumulative	n/a
23	Convertible or non-convertible	n/a	Equity Conversion	Non-convertible	n/a	Non-convertible	Non-convertible
24	If convertible, conversion triggers	n/a	CYBG Group CET1 < 7%	n/a	n/a	n/a	n/a
25	If convertible, fully or partially	n/a	Fully	n/a	n/a	n/a	n/a
26	If convertible, conversion rate	n/a	119p (66% of IPO share price)	n/a	n/a	n/a	n/a
27	If convertible, mandatory or optional conversion	n/a	Mandatory	n/a	n/a	n/a	n/a
28	If convertible, specify instrument type convertible into	n/a	Ordinary Shares	n/a	n/a	n/a	n/a
29	If convertible, specify issuer of instrument it converts into	n/a	CYBG PLC	n/a	n/a	n/a	n/a
30	Write-down feature	n/a	No	None contractual, statutory via bail-in	n/a	Yes - full permanent	None contractual, statutory via bail-in
31	If write-down, trigger(s)	n/a	n/a	n/a	n/a	CB Group CET1 < 7% or CB Solo CET1 < 7%	n/a

32	If write-down, full or partial	n/a	n/a	n/a	n/a	Full	n/a
33	If write-down, permanent or temporary	n/a	n/a	n/a	n/a	Permanent	n/a
34	If temporary write-down, description of write-up mechanism	n/a	n/a	n/a	n/a	n/a	n/a
35	Instrument type immediately senior	n/a	Tier 2	Senior Unsecured	n/a	Tier 2	Senior Unsecured
36	Non-compliant transitioned features	n/a	No	No	n/a	No	No
37	If yes, specify non-compliant features	n/a	n/a	n/a	n/a	n/a	n/a

TABLES

Basel II	The capital adequacy framework issued by the Basel Committee on Banking Supervision ("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.
Brexit	The UK vote (on 23 June 2016) to leave the European Union.
Capital buffers	Capital conservation buffer – A buffer set for all banks that can be used to absorb losses while avoiding breaching minimum requirements. It is designed to ensure that banks build up capital outside periods of stress which can be drawn down as losses are incurred. Systemic risk buffer ("SRB") – A buffer set for ring-fenced banks and large building societies to reduce their probability of failure or distress. It is commensurate with the greater cost that their failure or distress would have for the UK economy. Firms with total assets less than £175 billion are subject to a 0% SRB. Countercyclical capital buffer ("CCyB") - A capital buffer to ensure eligible firms have a sufficient capital base to absorb losses in stressed periods. The CCyB aims to ensure that banking sector capital requirements take account of the macroeconomic financial environment in which banks operate. It enables the Bank of England's Financial Policy Committee ("FPC") to adjust the resilience of the banking system to the changing scale of risk the system faces over time. PRA buffer – A buffer set using supervisory judgement informed by the impact of stress scenarios on a firm's capital requirements and resources, and taking account where appropriate of other factors including leverage, systemic importance and weaknesses in firms' risk management and governance. This is set on a firm-specific basis.
Capital conservation buffer	Refer to "Capital buffers".
Capital Requirements Directive IV ("CRD IV")	European legislation to implement Basel III. It replaces earlier European capital requirements directives with a revised package consisting of Capital Requirements Directive 2013/36/EU and Capital Requirements Regulation (EU) No. 575/2013 ("CRR"). CRD IV raises capital and liquidity requirements for European banks and harmonises the European framework for bank supervision. See also "Basel III".
Cash Ratio Deposit	Non-interest bearing deposits lodged with the Bank of England ("BoE") by eligible institutions.
CIU	Collective Investment Undertaking
Collateral	The assets of a borrower that are used as security against a loan facility.
Common Equity Tier 1 ("CET1") capital	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.
Common Equity Tier 1 ratio	CET1 capital divided by risk-weighted assets at a given date.
Countercyclical capital buffer	Refer to "Capital buffers".
Counterparty credit risk	Counterparty credit risk ("CCR") is the risk that a counterparty to a transaction may default before the final settlement of the transaction's cash flows. This risk concerns financial instruments, including derivatives and repurchase agreements.
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 in the event of the issuer's default. The assets used as collateral for covered bonds remain on the issuer's balance sheet and are a source of term funding.
Credit conversion factor ("CCF")	Credit conversion factors ("CCF") are used in determining the exposure at default in relation to a credit risk exposure. The CCF is an estimate of the proportion of undrawn and off-balance sheet commitments expected to be drawn down at the point of default.
Credit quality steps	A credit quality assessment scale as set out in CRD IV.

Credit risk	Risk of financial loss if a customer or counterparty fails to meet a payment obligation under a contract. It arises mainly from direct lending, trade finance and leasing business, but also from products such as guarantees, derivatives and debt securities.
Credit risk mitigation	Techniques to reduce the potential loss in the event that a customer (borrower or counterparty) becomes unable to meet its obligations. This may include the taking of financial or physical security, the assignment of receivables or the use of credit derivatives, guarantees, credit insurance, set-off or netting.
Earnings at risk ("EaR")	A measure of the quantity by which net interest income might change in the event of a change in interest rates.
EBA Implementing Technical Standard on Disclosure for Own Funds	Commission Implementing Regulation (EU) No 1423/2013 of 20 December 2013 laying down implementing technical standards with regard to disclosure of own funds requirements for institutions according to Regulation (EU) No 575/2013 of the European Parliament and of the Council.
Encumbrance	Denotes those assets on a bank's balance sheet which have been pledged as security, collateral or legally 'ring-fenced' in some other way which prevents the firm from being able to transfer, pledge, sell or otherwise use/dispose of these assets.
External Credit Assessment Institutions ("ECAIs")	ECAIs include external credit rating agencies such as Moody's, Fitch, and S&P.
FCA	Financial Conduct Authority.
The Group	CYBG PLC and its controlled entities.
Interest rate risk in the banking book ("IRRBB")	IRRBB arises from changes in interest rates that may impact the Group's financial condition in terms of earnings (net interest income) or economic value of the balance sheet.
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.
Internal Liquidity Adequacy Assessment Process ("ILAAP")	The Group's assessment of the liquidity and funding risks across different time horizons and stress scenarios, consistent with the risk appetite established by the Board. This leads to firms determining the amount of liquidity that should be held.
Internal ratings based ("IRB") approach	An approach for measuring exposure to credit risk. The IRB approaches are more sophisticated and risk sensitive than the standardised approach. They may be Foundation or Advanced. IRB approaches may only be used with PRA permission.
Leverage ratio	This is a regulatory standard ratio proposed by 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.
Market risk	The risk that movements in market risk factors (including foreign exchange rates and commodity prices, interest rates, credit spreads and equity prices) will reduce income or portfolio values.
Minimum requirement for own funds and eligible liabilities ("MREL")	The amount of capital and liabilities firms are to hold in order that 'bail-in' of creditors is a credible means of absorbing losses and recapitalising failing banks that have entered resolution.
Operational risk	The risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk.
Pillar 1	The quantitative elements of the Basel III framework including the minimum regulatory capital requirements for credit, operational and market risks.
Pillar 2	The qualitative expectations of the Basel III framework to be met through the supervisory review process. This includes the ICAAP, governance process and the supervisory review and evaluation process ("SREP").
Pillar 3	The final pillar of the Basel III framework which aims to encourage market discipline by improving the information made available to the market. This pillar sets out disclosure requirements for banks on their capital, risk exposures and risk assessment processes.
PPI	Payment Protection Insurance
PRA	Prudential Regulation Authority
PRA Buffer	Refer to "Capital buffers."
Regulatory capital	The capital which banks hold, determined in accordance with rules established by the relevant regulatory bodies.

Repurchase ("repo") agreement	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 counter-party (buying the security and agreeing to sell in the future) it is a reverse repurchase agreement or a reverse repo.
Residential mortgage-backed securities ("RMBSs")	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).
Risk appetite	An assessment of the types and quantum of risks to which the Group is prepared to be exposed.
Risk weighted assets ("RWAs")	On and off balance sheet assets are allocated a risk weighting based on the amount of capital required to support the asset.
Risk Management Framework ("RMF")	The Group identifies and manages risk using the RMF 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.
Securities Financing Transaction ("SFT")	Repurchase transactions, securities or commodities lending or borrowing transactions or other capital market driven transactions.
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 that can achieve a reduction in funding costs by offering typically AAA rated securities secured by the underlying financial asset.
Standardised Approach	In relation to credit risk, a method for calculating credit risk capital requirements using 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.
Systemic risk buffer	Refer to "Capital buffers."
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 1 capital ratio	Tier 1 capital resources divided by risk-weighted assets at a given date.
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.