Clydesdale Bank

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Yorkshire Bank

Annual report & consolidated financial statements

Clydesdale Bank PLC

For the year ended 30 September 2014

Company Number: SC001111

Clydesdale Bank PLC

Annual report and consolidated financial statements

For the year ended 30 September 2014

Contents

Overview

Clydesdale Bank PLC ("the Bank"), together with its subsidiary undertakings (which together comprise "the Group"), is the United Kingdom retail and commercial banking business of National Australia Bank Limited ("NAB"). Its immediate parent is National Australia Group Europe Limited ("NAGE"). The Group operates under both the Clydesdale Bank and Yorkshire Bank brands. It offers a range of banking services for both personal and business customers through retail branches, Business & Private Banking centres, direct and online banking and brokers.

Forward looking statements

This document contains certain forward looking statements with respect to the expectations, plans and aims of the Group relating to future performance, financial position and results. The Group considers the expectations these forward looking statements reflect to be reasonable. However, we can give no assurance that these expectations will not differ materially from actual outcomes. All forward looking statements involve risk and uncertainty because they relate to future events and circumstances that are beyond the Group's control. Factors beyond the Group's control include, amongst others, domestic UK and global economic, business and political conditions, the policies and actions of Governments and other regulatory bodies, changes in the tax regimes or other legislation in the jurisdictions the Group and its parent operate, market related risks such as interest or exchange rate movements, inflation, changes in customer preferences and the actions of competitors, the effect, timing and other uncertainties around future acquisitions or other combinations within relevant industries, delays in implementing proposals and risks affecting borrower credit quality. As a result, the Group recommends that readers of this document do not place undue reliance on such forward looking statements.

The Group undertakes no obligation to update any forward looking statements in light of any future events, new information or otherwise.

Front cover image: "The Kelpies" in Falkirk, the largest equine sculptures in the world.

Officers and professional advisers

Directors	**Chairman**	James Pettigrew
	Non-executive	David Allvey * # David Browne * # Richard Gregory OBE, Senior Independent Director * # ~ Barbara Ridpath # ~ Teresa Robson-Capps (appointed 8 October 2014) Alexander Shapland # ~
	Executive	David Thorburn, Chief Executive Officer Debbie Crosbie Richard Sawers (National Australia Bank)
UK Executive Committee		David Thorburn, Chief Executive Officer Debbie Crosbie, Executive Director Ian Smith, Chief Financial Officer (appointed 1 November 2014) David Gillespie, Distribution Director ^ Eric Gunn, Chief Risk Officer James Peirson, General Counsel ^ Lynn McManus, People & Communications Director Helen Page, Customer Experience & Marketing Director Kevin Page, Strategy & Transformation Director Paul Shephard, Business & Private Bank Director John Shovelin, Operations & IT Director
Company Secretary		Lorna McMillan
Registered Office		30 St Vincent Place Glasgow, G1 2HL
Auditor		Ernst & Young LLP 1 More London Place London, SE1 2AF

* Member of the Boards' Audit Committee
\# Member of the Boards' Risk Committee
~ Member of the Boards' Governance and Nomination Committee
^ Appointment subject to Regulatory approval

Chairman's statement

James Pettigrew

This year we have continued to re-shape our business and pursue sustainable growth by enhancing customer experience and investing in new products. As well as delivering a better underlying financial performance, we are also dealing decisively with the historic conduct issues that continue to mask the full extent of our progress.

Over the last three years, we have taken firm action to control costs, restructure our balance sheet, and move our focus to those geographies and sectors where we can compete most effectively. During this year, we have had a particular drive to improve customer experience, increase brand awareness, and invest in products and projects that support our customers, including more on-line services and new current accounts.

Our commitment to improving customer experience is matched with a determination to address past conduct issues. We have significantly increased our provision for PPI related matters. We deeply regret the impact that these historic issues had on our customers at the time and we are determined to resolve them fairly now so we can concentrate on our future growth and innovation.

The extent of the financial provisions we have made have resulted in the Bank reporting a loss for the period, despite the increases in operating income and substantial reductions in bad and doubtful debts. Improving financial performance, reducing exposure to historic conduct charges and securing sustainable growth, by putting the customer at the heart of what we do, remains the critical focus for the business.

The Board has also undergone considerable change in recent years with a substantial renewal in Board membership bringing a fresh approach to its scrutiny and oversight. This year saw Cameron Clyne step down as both Chairman of the Clydesdale Bank Board and as Group CEO. The business benefitted considerably from Cameron's insight and drive, and I am grateful for the opportunity to continue the strategic direction that he helped to set. Other changes included the appointment of Debbie Crosbie as a new Executive Director, Teresa Robson-Capps as a Non-executive Director, and the recent retirement from both the Board and the business of John Hooper. The Board is grateful for John's considerable contribution and is pleased to welcome its new Directors as well as the new members of executive management highlighted in the Chief Executive Officer's statement.

Just as we have recognised the need for decisive action to improve trust and confidence in our business, the industry as a whole continues to face into the further reforms driven by regulators and policy makers within the UK and Europe. I do not underestimate the impact that these reforms, coupled with the changes that we are driving, have on the Bank's employees. I'm grateful for their support and for their relentless efforts on behalf of our customers and our business as we build a better bank.

James Pettigrew
Chairman
17 November 2014

Chief Executive Officer's statement

David Thorburn

In the year just ended we intensified our clear focus on our customers and the communities we serve. Our drive to put customers at the heart of everything we do is helping to improve our underlying performance. This, combined with the strengthened UK economy, leaves us well positioned for sustainable growth over the medium term.

Clearly demonstrating benefits from the restructuring of the business and the improved UK economy, underlying pre-tax profits of £218m were achieved compared to £87m in the prior corresponding period.

The charge to provide for bad and doubtful debts fell by 48.7% or £70m to £74m, reflecting a more stable UK economy as well as the steps taken by management to improve underlying asset quality.

While no new material conduct issues have emerged since the Half Year, regrettably legacy conduct related matters continued to have a materially negative impact. Additional provisions of £433m were raised in the year leading to a loss position at the year-end for the Group. Payment Protection Insurance ("PPI") provision balances stood at £515m at 30 September 2014.

We have made good progress in the past year in sharpening the competitiveness of our products, introducing customer service enhancements and improving the efficiency of our operations. In addition, we have undertaken extensive programmes to address legacy conduct issues and ensure fairness for our customers is at the heart of everything we do. We are determined to ensure there is no recurrence of the legacy conduct issues that have emerged in recent years.

Clydesdale and Yorkshire Banks are strong brands with good market shares in the communities in which we operate. Our focus continues to be building on our core strengths in personal and business banking. The pace of change is accelerating as we drive further improvements to products, delivery channels, the experience, efficiency and quality of service we offer our customers. In order to support me in this journey a number of key executive appointments have been made including Ian Smith, David Gillespie and James Peirson.

The Bank has benefitted from a significant period of change with the support of its employees and further improvements and challenges lie ahead. We are well placed to further improve our underlying financial performance as we continue to invest significantly in building a better bank.

David Thorburn.

David Thorburn
Chief Executive Officer
17 November 2014

Strategic report

The Directors of the Bank with its subsidiary undertakings (which together comprise “the Group”) present their Strategic Report for the year ended 30 September 2014.

The Strategic Report is a statutory requirement under the Companies Act 2006 (Strategic Report and Directors’ Report) Regulations 2013, replacing the previous Business Review, and is intended to be fair and balanced, and to provide information that enables the Directors to be satisfied that they have complied with s172 of the Companies Act 2006 (which sets out the Directors’ duty to promote the success of the company).

Our business model

The Group operates a full service UK-focused retail and commercial banking business under the brand names “Clydesdale Bank” and “Yorkshire Bank”, in Scotland, the North of England and selected other sites. The Bank delivers these services through a network of 298 retail branches, 42 Business & Private Banking centres (including 23 sites co-located with retail branches), direct and online banking. The Bank employs 4,758* staff. The Bank is an "authorised person" under the Financial Services and Markets Act 2000 and is regulated by the Prudential Regulation Authority (“PRA”) and the Financial Conduct Authority (“FCA”).

Operating environment

The UK economy continues to show signs of improvement, having experienced seven consecutive quarters of output growth. The economy expanded by 0.7% in the September quarter and by 0.9% in the three months to June. The Q3 2014 GDP figures were enhanced by expansion in the service, production and construction industries. While the slowdown in the pace of growth has raised concerns that the economic recovery will stall as a result of the issues facing the Eurozone, the UK is still forecast to be the fastest growing advanced economy in 2014. The UK unemployment rate as at September 2014 was 6%, its lowest level since late 2008, with 1.96m people unemployed at that point, a reduction of 115,000 from the previous quarter.

The inflation rate (as measured by annualised growth in the Consumer Prices Index) reduced to 1.2% in September 2014, its lowest level for five years, and is below the Bank of England target of 2.0%. The Bank of England Bank Rate has remained at 0.5% since March 2009, and the spread between Bank Rate and 3 month LIBOR has remained relatively narrow throughout the year.

The regulatory and political environment in which the Group operates continues to evolve. Key changes, all of which the Group is responding to, include:

- The PRA, in partnership with the FCA, issued two consultation papers in July 2014, covering a range of factors associated with the regulatory framework and remuneration. This included a new “Senior Managers Regime” to replace the current Approved Persons regime, a set of “Conduct Rules” to replace the existing Codes of Practice, and new remuneration rules to strengthen the alignment between risk and reward. Implementation of these rules is anticipated during 2015 and the Group is assessing the impacts.
- The Payment Accounts Directive (“Directive”). This Directive was published in the Official Journal on 28 August 2014. The Bank has two years to implement the requirements which encompass measures on transparency of fees and charges, access to basic bank accounts across the EU and arrangements to facilitate the provision of information to customers and transfer of balances if they wish to switch accounts between EU member states.
- The Mortgage Credit Directive (“Directive”). The Directive was published in the Official Journal on 28 February 2014. The FCA issued a consultation paper on 25 September 2014 which outlined the key changes that will be required to be made regarding the mortgage sales process as well as documentation to be made available to customers. The UK is required to implement these rules by March 2016 and the Group is assessing their impact.

* This is the Clydesdale Bank PLC full time equivalent (“FTE”). UK Banking (as defined in note 4) has 7,278 FTEs which includes employees working within other National Australia Group Europe Limited subsidiaries who provide support services to the Group.

Strategic report (continued)

Operating environment (continued)

- Under the Financial Services (Banking Reform) Act 2013 ("FSBRA 2013"), the FCA has been tasked with setting up a new UK payment systems regulator. This change is as the result of Government concerns around UK payment systems. The regulator's work is expected to cover issues such as access to the payments systems, the terms offered for access and the industry's pace of innovation. The Treasury published a consultation on 14 October 2014 which set out which payment systems it intends to be regulated by the new rules, with a final decision to be confirmed in time for designation to be effective from April 2015.
- In October 2014, the PRA issued a consultation paper on the implementation of ring-fencing of retail banks in the UK. The Government has stated that its intention is for ring-fencing to be implemented from 1 January 2019. The PRA is expected to undertake further consultation during 2015, and publish its rules and supervisory statements during 2016. The Bank is expected to qualify as a ring-fenced bank under the criteria of the FSBRA 2013 and is considering potential impacts.
- The European Union implemented Basel III through the Capital Requirements Directive IV ("CRD IV") package published in June 2013. The PRA published its final rules on the UK implementation of CRD IV during December 2013 in Policy Statement 7/13. These introduced a wide range of measures commencing on 1 January 2014. The Group currently complies with the inforce measures and is working with the regulator to ensure it continues to meet capital requirements throughout the progressive implementation of these rules.
- The PRA issued a consultation paper in August 2014 to implement the Financial Policy Committee's ("FPC") recommendation on loan-to-income ("LTI") and affordability stress requirements. The proposals ensure that mortgage lenders limit the number of mortgage loans made at or greater than four and a half times LTI, to no more than 15% of their total number of new mortgage loans. The Group already conformed to this requirement. The PRA's final rules came into force on 1 October 2014.
- The Basel Committee have issued proposals for consultation on the Net Stable Funding Ratio ("NSFR") with a final standard due by the end of 2014. The NSFR aims to reduce reliance on short term funding by ensuring that banks hold a sufficient amount of stable funding to match the maturity characteristics of their different business activities. It is anticipated that the NSFR will become a minimum standard with all banks required to maintain an indicative NSFR of greater than 100% by 1 January 2018. The Group will continue to monitor its NSFR in light of this development.

Our goal and strategic priorities

The Group's goal is to be a strong, customer-focused bank for the communities it serves.

To achieve this, we are pursuing four strategic priorities:

1. Putting the customer at the heart of our business

The customer is rightly at the heart of everything we do as an organisation.

During the course of the year, we have made improvements in the experience that we offer to our customers. This has involved a range of initiatives including a mortgage transformation programme which has delivered a 20% reduction in the end-to-end mortgage processing timeframe, and a personal current account opening review which has reduced the time spent opening an account by 40%. Our new Service proposition announced in June 2014 provides customers with a named contact with the aim of driving an improved service experience. Progress has also been made towards resolving a number of legacy conduct issues during the year.

Strategic report (continued)

Our goal and strategic priorities (continued)

A major part of responding to changing customer needs has centred on the reshaping of our Retail Branch network. In March 2014, we announced a programme which resulted in the closure of 28 unsustainable branches and the relocation of three branches to improved locations. Six flagship branches will be launched in heartland locations with access to new in-house facilities, services and technology. This investment, combined with the expansion of mobile banking and improvements to internet banking and text alerts, will allow us to offer the choice and flexibility which both existing customers and prospective customers demand.

We have continued to build on our "We Care About Here" branding, through regular advertising and an improved digital presence, reflecting our belief that we can and do make a positive difference in the communities we operate in.

2. Embedding strong management of risk and controls

We have strengthened our overall risk and control framework in recent years, and will continue to do so, to ensure that material risks which we face are appropriately managed.

Central to this work has been the embedding of an effective conduct risk management framework across all activities. The Customer Trust and Confidence function was established during the year to ensure clear accountability and dedicated focus on fair outcomes for customers.

Further information about the Group's approach to management of risk can be found in note 39.

3. Building sustainable returns

While the economic, regulatory and legacy conduct environment remains challenging, we aim to deliver appropriate returns for our shareholders through controlled and efficient growth of our Retail and Business & Private Banking franchises within agreed risk appetite settings.

In executing this strategy, we have continued to focus on providing support to Retail and SME customers. Strong asset growth in mortgage lending nationally, the continued management of the lower yielding assets and the benefits of actions taken in the year to reduce funding costs have delivered net interest margin improvements and had a positive impact on returns. The risk profile of our portfolio has also been reduced during the year with improvements seen across all key asset quality metrics.

4. Employee engagement and enablement

The three strategic priorities outlined above can only be delivered if our people are motivated and equipped to do their best. Key to this is determining and understanding what they think about the Group as an employer and as a place to work. To do this, we undertake an annual "Speak Up Step Up" ("SUSU") survey, that asks a range of questions to gauge how engaged our employees are with the Group and what the Group can do to enable them going forward.

The recent SUSU results were pleasing and provide a good indicator of where improvements can be made to strengthen our employee proposition. 87% of employees responded to the voluntary survey. Whilst the measure of engagement changed in 2014, a like for like comparison using the previous measure showed an overall improvement. In particular, employee advocacy, pride and motivation to go beyond what is expected had all improved. Furthermore, our staff are now more aware of how their role contributes to the Group's strategy, which is something we have worked hard on since the previous survey. The results also indicated a very strong customer focus and a similar risk and compliance culture across our staff. We will continue to work proactively on the insights that are derived from SUSU to ensure we understand and act on areas where improvements can be made.

Our goal and strategic priorities (continued)

The following table highlights our progress to date (as at 30 September 2014) in relation to the key performance indicators ("KPI") that we have identified to measure progress against our strategic goals:

Priority	*Strategic goal*	*KPI*	*Comments*
The Customer	"We Care About Here" is how we put customers at the heart of our business. We listen to customers to learn how to become a better bank, act in a way that shows we are all accountable to them, and design every product and service to meet their expectations.	Net promoter score	The Group launched its new Service proposition offering customers a single named contact, supported by ongoing investment in our brand and advertising. We also announced the reshaping of our Retail branch network, including new concept branches, refurbishments and relocations to improved sites. These investments, combined with improvements to our mobile and internet banking services, are designed to enhance the overall customer experience.
Risk & Control Framework	Embed a strong risk culture in our staff that consistently delivers the right customer outcomes and take informed risk and reward decisions that maintain the financial strength of the Group while protecting our customers, staff, assets and earnings.	Adherence to risk appetite settings	The Group continues to operate within its credit risk tolerance while the number of operational risk loss events has reduced in the year. Other than in respect to legacy conduct issues, we are within operational risk tolerance in all other measures.
Sustainable Returns	Maintain capital, liquidity and funding ratios within risk appetite while returning the UK business to sustainable profit and return on equity measures. Through the execution of detailed strategic initiatives, targets for capital, funding, liquidity and cash earnings will be achieved and deliver sustainable and satisfactory returns to shareholders.	Capital, liquidity, and funding ratios, together with a sustainable profit and return on equity	Financial performance measures continue to be affected by legacy conduct issues but underlying measures continue to show improvements (see pages 8, 14 and 17).
People	Provide a compelling employee proposition that motivates, equips and rewards staff and encourages appropriate behaviours; demonstrated through increased employee satisfaction and our ability to develop and attract talent.	Employee engagement survey scores	Recruiting, retaining and developing people is one of the Bank's key strategic priorities. There was a significant increase in employee engagement and enablement scores in the 2014 SUSU survey. We have also designed a dedicated People Programme that will deliver positive change over the next two years, ranging from changes to our reward and remuneration schemes to a brand new Intranet site.

Strategic report (continued)

Financial analysis

The Group made a loss after tax of £178m compared to a loss after tax of £44m for the year to September 2013.

The impact of dealing with legacy conduct matters continues to have an impact on statutory results, with £433m of additional provisions raised in the year (2013: £180m). Underlying performance has improved significantly, with a £131m increase in profit before tax. The key driver has been a material reduction in impairment losses on credit exposures reflecting improving economic conditions. This was supported by an improvement in net interest margin.

The Group's Common Equity Tier 1 ("CET1") capital ratio increased to 12.1% (from 10.5% at 30 September 2013), driven by a reduction in business lending and an increase in ordinary share capital.

The Group has actively managed its customer deposits during the year to achieve an efficient customer balance sheet position. The Customer Funding Index (CFI) reduced from 90.2% in September 2013 to 86.2% at September 2014 and the Stable Funding Index ("SFI") reduced from 108.5% to 102.5% in the same period.

The Group delivered on its strategy to grow the retail mortgage portfolio with the business achieving mortgage growth of 9.6% over the prior year compared to system growth of 1.1%* while maintaining the quality of our underwriting standards.

Summarised Income Statement	2014 £m	2013 £m As restated [2]	2014 vs 2013 %
Net interest income	**771**	756	2.0%
Non-interest income	**192**	184	4.1%
Total operating income	**963**	940	2.4%
Total operating and administrative expenses	**(1,105)**	(850)	(29.9%)
Operating (loss)/profit before impairment losses	**(142)**	90	Large
Impairment losses on credit exposures [1]	**(74)**	(144)	48.7%
Loss on ordinary activities before tax	**(216)**	(54)	Large
Analysed as:			
Profit before tax, Payment Protection Insurance redress expense, FSCS levy and bank levy	**218**	87	
Payment Protection Insurance redress expense	**(420)**	(130)	
FSCS levy and bank levy	**(14)**	(11)	
Loss on ordinary activities before tax	**(216)**	(54)	
Tax credit	**38**	10	
Loss attributable to equity holders	**(178)**	(44)	

(1) Impairment losses on credit exposures relate solely to loans and advances to customers (see notes 15 and 16 to the financial statements) and exclude the credit risk adjustments on loans at fair value through profit or loss which are incorporated in the movement in fair value assets within non-interest income (refer to note 6 to the financial statements).

(2) The comparative period 30 September 2013 has been restated to incorporate the IAS 19 pension changes disclosed in note 1 to the financial statements and to reclassify the charge for PPI from non-interest income to operating expenses.

* Source: Bank of England – September 2014.

Financial analysis (continued)

Key measures	2014	2013 As restated [2]	2014 vs 2013
Net interest margin	**2.26%**	2.14%	12bp
Cost to income ratio [2]	**114.8%**	90.4%	(244)bp
CET1 ratio	**12.1%**	10.5%	160bp
Gross loans and acceptances [3] [4] (£bn)	**26.9**	27.1	(0.8)%
Interest earning assets [3] (£bn)	**34.1**	35.3	(3.4)%
Total assets [3] (£bn)	**36.5**	37.7	(3.2)%
Customer deposits [3] [5] (£bn)	**23.4**	24.7	(5.0)%

New key measures for 2014	2014
Return on assets	**(0.5)%**
Leverage ratio	**5.7**
Liquidity coverage ratio ("LCR") [6] [8]	**109.6%**
Net stable funding ratio ("NSFR") [7] [8]	**107.8%**

(3) Average volumes.

(4) Gross loans and acceptances include gross loans and advances to customers, loans designated at fair value through profit or loss and amounts due from customers on acceptances.

(5) Customer deposits include current accounts, savings accounts, term deposits and business deposits.

(6) In January 2013, the Basel Committee on Banking Supervision ("BCBS") published its final guidance for calculating the LCR. Following adoption by the EU, this is currently expected to come into effect from October 2015 on a phased basis until 1 January 2018. The Group monitors the LCR based on its own interpretations of current guidance available for CRD IV LCR reporting. Therefore, the reported LCR may change over time with regulatory developments. Due to possible differences in interpretation of the rules, the Group's ratio may not be directly comparable with those of other financial institutions.

(7) In October 2014, the BCBS published its final guidance for calculating the NSFR. Following adoption by the EU, this will be subject to an observation period before coming into effect from 1 January 2018. The Group monitors the NSFR based on its own interpretations of current guidance available for CRD IV NSFR reporting. Therefore, the reported NSFR may change over time with regulatory developments. Due to possible differences in interpretation of the rules, the Group's ratio may not be directly comparable with those of other financial institutions.

(8) Reported at the Defined Liquidity Group level.

September 2014 v September 2013

Net interest income increased by £15m (2.0%). The key driver in this increase was higher mortgage lending income and lower term deposit costs. This was partially offset by lower business lending income as a result of portfolio attrition.

Average gross loans and acceptances, which incorporate loans accounted for at fair value, decreased by £0.2bn (0.8%) to £26.9bn. Business lending balances reduced by £1.7bn or 16.7%, driven by the subdued demand for credit, risk appetite settings and the impact of business restructuring. Mortgage growth of £1.5bn or 9.6%, was higher than system growth of 1.1%* in the period and largely offset the decline in business lending balances.

Average customer deposits decreased by £1.3bn or 5.0%. This reflected the managed rebalancing of the retail deposit book, with a reduction in higher cost term deposits partially offset by growth in current and savings accounts.

* Source: Bank of England – September 2014.

Financial analysis (continued)

The net interest margin increased by 12bps to 2.26% (2013: 2.14%). This was driven by an improved retail deposit mix and a reduction in low yielding liquid assets, partially offset by lower lending margins and a decline in the earnings rate on non-interest bearing deposits and capital.

Non-interest income increased by £8m (4.1%). The key drivers in this increase were favourable movements in fair value and in hedging ineffectiveness. This was partially offset by lower fees and commissions as a result of our strategy to reduce account fees to improve customer outcomes, competitive positioning and the impacts of subdued business credit growth.

Operating and administrative expenses increased by £255m (29.9%) over the prior year. Costs related to legacy conduct related matters continue to have an impact on expenses, with £433m (2013: £180m) of additional provisions charged in the year. Excluding these, underlying operating and administrative expenses were broadly flat in the year. Personnel costs were lower due to a reduction in average FTEs following business restructuring, with occupancy costs lower following property rationalisation. This was partially offset by an increase in marketing costs to support customer acquisition and an increase in project related investment activity.

Impairment losses on credit exposures decreased by £70m (48.7%) over the prior year. This was primarily driven by a reduction in business lending losses as a result of asset quality improvements aligned to a more stable UK economy. Mortgage losses remained stable despite continued growth in the portfolio.

Investment spend

The Group continues to maintain its investment in the business with expenditure focused on regulatory and compliance, efficiency and simplification, and revenue generation activities.

Significant progress has been made during the year including adding payments functionality to our mobile application. The Group has also delivered mandatory reporting capabilities for Foreign Account Tax Compliance Act (FATCA) and European Banking Authority Harmonisation Rules. The second half of the year saw the implementation of our new mortgage processing platform and a refresh of the desktop and laptop estate as part of the Employee Enablement programme. This period also saw the launch of projects to implement the Bank's digital strategy and further enhance our customer proposition.

Asset quality

Provisions on credit exposures (£m)	2014	2013
Specific provision for doubtful debts	110	134
Collective provision for doubtful debts	135	155

Credit risk adjustments on loans at fair value (£m)	2014	2013
Individually assessed credit risk adjustments on loans at fair value	30	23
Collectively assessed credit risk adjustments on loans at fair value	44	54

Past due and impaired assets (£m)	2014	2013
90+ Days Past Due ("DPD") assets [1]	182	157
Gross impaired assets [2]	375	426

Asset quality measures (%)	2014	2013
90+ DPD plus gross impaired assets to gross loans and acceptances [2]	2.01%	2.20%
Specific provision to gross impaired assets [2]	37.5%	36.7%
Net write-offs to gross loans and acceptances	0.43%	0.57%
Total provision as a percentage of net write-offs [3]	279%	239%
Total provision to gross loans and acceptances [3]	1.15%	1.38%
Impairment losses on credit exposures to credit risk-weighted assets	0.45%	0.80%

Impairment provisions on credit exposures (£m)	2014	2013
Business lending (including lease finance)	186	221
Retail lending	59	68
	245	289

Impairment losses on credit exposures	2014 £m	2013 £m
Business lending (including lease finance)	45	102
Retail lending	29	42
	74	144
Of which:		
Specific	95	163
Collective	(21)	(19)
	74	144

(1) September 2014 balance includes UK mortgage defaulted customers not previously disclosed as past due, where the contractual repayment date has passed but customers continue to pay interest due, where an agreed arrangement is in place or where the customer is deceased, totalling £39m. The September 2014 disclosure reflects changes in Group and Regulatory practices. Prior year comparatives have not been restated. For information, the comparative year 90+ DPD balance at September 2013 would have been £222m.

(2) Gross impaired assets for September 2014 and September 2013 include £56m and £63m gross impaired fair value assets respectively.

(3) Total provision to gross loans and acceptances/net write-offs includes the credit risk adjustments on loans at fair value through profit or loss.

Strategic report (continued)

Asset quality (continued)

The UK economy is showing steady signs of improvement, having experienced seven consecutive quarters of output growth.

Retail asset quality continues to improve with lower default rates observed across all unsecured lending. Housing lending impaired loan levels have remained subdued against a growing portfolio due to the prolonged period of low interest rates and recovery in residential property prices. The 90+ DPD levels for housing lending shows a steady reduction with continued improvements in the unsecured portfolios through the 12 months to 30 September 2014.

While the non-retail portfolio remains sensitive to economic conditions, the recent improvement in the environment, combined with management actions, has had a positive impact on asset quality metrics. However, despite the growth in market confidence and the decline in gross impaired assets to £375m as at September 2014, the level of non-retail impaired assets at £311m (2013: £350m) remains elevated when compared with historical norms.

The overall collective provision for doubtful debts continues to decrease, reflecting the reduction in the business lending portfolio and stabilisation in non-retail asset quality. The personal lending collective provision also continues to reduce, driven by the improved delinquency profile of these portfolios.

The ratio of total provisions to gross loans and acceptances decreased by 23 basis points to 1.15% at 30 September 2014. The movement in the ratio reflects the lower risk profile of the book, with a reduced business lending portfolio and growth in the mortgage portfolio which has a lower provisioning requirement.

Capital position

The Group's CET1 ratio increased from 10.5% in September 2013 to 12.1% in September 2014. The Group replaced £300m of preference shares, which were not compliant with Basel III requirements for loss absorbency, with a £300m ordinary share issuance in December 2013. Furthermore, the Group issued an additional £300m of ordinary shares in March 2014. This led to a significant strengthening of the CET1 ratio. Further capital benefits from balance sheet optimisation resulted in a reduction in credit risk weighted assets, however this was partially offset by the impact of conduct charges incurred in the year and the capital deductions arising from the introduction of CRD IV. The Group continues to be fully compliant with the PRA's regulatory capital requirements.

The Group's capital position at 30 September 2014 is summarised on page 13. This table shows the capital position on a CRD IV "transitional" basis and includes grandfathered legacy Tier 2 instruments under the transitional rules implemented by the PRA.

Strategic report (continued)

Capital position (continued)

Regulatory capital

CET1 capital	CRD IV 2014 £m	Basel II 2013 £m
Capital instruments	**2,042**	1,442
Share premium account	**243**	243
Retained earnings and other reserves [1]	**210**	393
Structured entities reserves [1]	**(4)**	-
Prudent valuation adjustment [2]	**(2)**	(3)
Deferred tax asset ("DTA") relying on future profitability [3]	**(223)**	-
Defined benefit pension fund assets (net of deferred tax liabilities) [4]	**(39)**	-
Pension fund deficit adjustment [5]	**-**	2
	2,227	2,077
Tier 1 capital		
Additional Tier 1 capital instruments	**-**	-
Perpetual non-cumulative preference shares [6]	**-**	300
	-	300
Total Tier 1 capital	**2,227**	2,377
Tier 2 capital		
Subordinated loans [7]	**1,076**	1,076
Credit risk adjustments [8]	**135**	155
Revaluation reserve [9]	**-**	2
Qualifying and material holding Tier 2 deductions [10]	**-**	(3)
	1,211	1,230
Total capital	**3,438**	3,607

(1) Under Capital Requirements Regulation ("CRR") the cash flow hedge and asset revaluation reserves now form part of regulatory capital resources. Structured entities reserves are also excluded for regulatory capital purposes.

(2) A prudent valuation adjustment is applied in respect of fair valued instruments as required under regulatory capital rules.

(3) Under CRD IV, deferred tax assets that rely on future profitability shall be deducted from CET1 capital.

(4) Under CRD IV, defined benefit pension fund assets shall be deducted from CET1 capital (net of deferred tax liability).

(5) For regulatory capital purposes under Basel II, the pension fund deficit is added back to regulatory capital and substituted with an estimate of additional pension fund contributions to be made over the next five years, adjusted for deferred tax. CRD IV does not allow the pension fund deficit to be added back to regulatory capital.

(6) During the year perpetual non-cumulative preference shares were redeemed and replaced with CET1 ordinary shares.

(7) Subordinated loans reflect the principal outstanding and does not include accrued interest.

(8) The collective provision add back is limited for regulatory capital purposes.

(9) Under CRD IV, the revaluation reserve is classified as CET1 capital.

(10) Material and qualifying holdings deducted under Basel II, are now risk weighted under CRD IV rules.

Strategic report (continued)

Capital position (continued)

Risk-weighted assets [1]	2014 £m	2013 £m
Retail mortgages	**6,917**	6,319
Business lending	**7,984**	9,674
Other retail lending	**1,030**	1,071
Other lending	**674**	842
Credit risk	**16,605**	17,906
Credit valuation adjustment	**137**	1
Operational risk	**1,549**	1,650
Counterparty risk	**181**	170
	18,472	19,727

Capital ratios		
CET1 ratio [2]	**12.1%**	10.5%
Tier 1 ratio	**12.1%**	12.0%
Total capital ratio	**18.6%**	18.3%

(1) Risk weighted assets ("RWAs") are calculated under the standardised approach.

(2) CET1 capital is Tier 1 capital excluding perpetual non-cumulative preference shares and perpetual notes.

Regulatory capital to statutory total equity reconciliation	2014 £m	2013 £m
Regulatory Tier 1 capital	**2,227**	2,377
Reverse pension regulatory adjustments	**39**	(2)
Reverse deductions from capital	**2**	3
Share option reserve	**2**	2
Asset revaluation reserve	**-**	2
Available for sale reserve	**8**	5
Cash flow hedge reserve	**-**	23
Deferred tax asset relying on future profitability	**223**	-
Structured Entities reserves	**4**	-
Statutory total equity	**2,505**	2,410

Minimum Pillar 1 capital requirements	2014 £m	2013 £m
Credit risk	**1,328**	1,432
Operational risk	**124**	132
Counterparty risk	**14**	14
Credit valuation adjustment	**11**	-
Tier 1 regulatory capital requirements	**1,477**	1,578

Capital position (continued)

Regulatory capital flow of funds	CRD IV 2014 £m	Basel II 2013 £m
CET1 capital		
CET1 capital at 1 October	**2,077**	2,231
Share capital: ordinary share new issuance	**600**	-
Retained earnings and other reserves	**(187)**	(82)
Prudent valuation adjustment	**1**	(1)
DTA relying on future profitability	**(223)**	-
Defined benefit pension fund assets	**(39)**	-
Pension fund deficit adjustment	**(2)**	(71)
	2,227	2,077
Tier 1 capital		
Tier 1 capital at 1 October	**300**	300
Share capital redeemed: perpetual non-cumulative preference shares	**(300)**	-
	-	300
Total Tier 1 capital	**2,227**	2,377
Tier 2 capital		
Tier 2 capital at 1 October	**1,230**	1,405
Credit risk adjustments	**(20)**	(175)
Asset revaluation reserve	**(2)**	1
Qualifying and material holding Tier 2 deductions	**3**	(1)
	1,211	1,230
Total capital	**3,438**	3,607

Risk-weighted assets flow statement

	£m
Risk-weighted assets at 1 October 2013	**19,727**
Book size	**(364)**
Book quality	**(399)**
Methodology and policy	**(492)**
Other	**-**
Risk-weighted assets at 30 September 2014	**18,472**

Methodology and policy includes the implementation of the new CRR rules which came into effect on 1 January 2014. Additionally, in the period a new reporting platform was implemented for the calculation of Credit Risk-Weighted Assets.

Strategic report (continued)

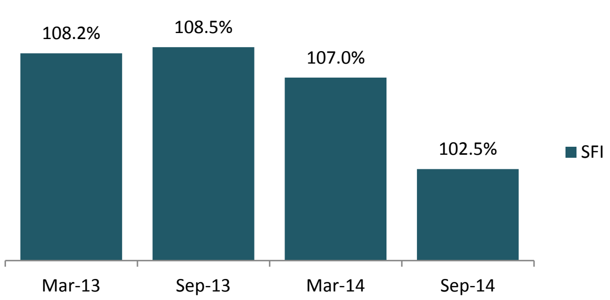
Capital position (continued)

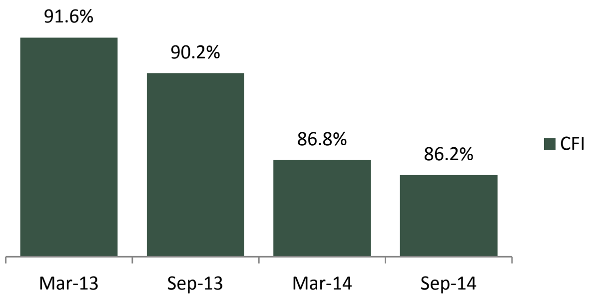
Capital requirements for calculating RWAs	At 30 September 2014 Capital required £m	RWA £m	Exposure £m
Central Governments or Central Banks	-	-	5,105
Regional Governments or Local Authorities	2	22	112
Public Sector Entities	-	3	3
Multilateral development banks	-	-	50
Institutions	18	224	1,006
Corporates			
Term lending - Business	134	1,676	1,715
Other lending	110	1,381	1,426
Overdrafts	27	334	381
Lease	26	328	355
	297	**3,719**	**3,877**
Retail			
Term lending - Retail	46	577	769
Credit cards	21	263	355
Other unsecured including overdrafts	12	154	213
	79	**994**	**1,337**
Secured by mortgages on residential property			
Mortgages	541	6,761	18,872
Term lending - Business	64	795	1,345
	605	**7,556**	**20,217**
Secured by mortgages on commercial real estate			
Term lending - Business	189	2,356	2,585
Overdrafts	51	640	723
	240	**2,996**	**3,308**
Exposures in default	49	611	493
Claims in the form of CIU	-	3	3
Equity exposures	1	12	8
Other items	37	465	1,902
	1,328	**16,605**	**37,421**
Operational risk	124	1,549	
Counterparty risk	14	181	
Credit valuation adjustment	11	137	
	1,477	**18,472**	

The 'Exposure' amounts disclosed above are post Credit Risk Mitigation and Credit Conversion Factors having been applied where applicable. The tables above reflect the Group's interpretation of the revised capital calculation required by CRD IV.

Funding and liquidity

Stable funding and customer funding indices





The Group's customer deposits have been managed lower during the year to achieve an efficient customer balance sheet position. The Customer Funding Index (CFI) reduced from 90.2% in September 2013 to 86.2% at September 2014 and the Stable Funding Index (SFI) reduced from 108.5% to 102.5% in the same period.

The Group has continued to raise term funding through its Covered Bond and Securitisation programmes, with c. £600m raised in March 2014. It remains diversified in terms of the type of instrument and product, currency, counterparty, term structure and markets, available through such programmes.

In May 2014, Standard and Poors changed the outlook of Clydesdale Bank PLC from negative to stable, and on 9 August 2014 it affirmed its BBB+/A-2 credit rating. On 21 October 2014, Moody's affirmed the Clydesdale Bank PLC rating at Baa2/P-2, while maintaining a stable outlook.

The Group's long-term credit ratings are summarised below:

	Outlook as at 17 November 2014	2014	2013
Fitch	**Stable**	**A**	A
Moody's	**Stable**	**Baa2**	Baa2
Standard & Poor's	**Stable**	**BBB+**	BBB+

Liquid reserve	**2014 £m**	**2013 £m**
Cash and balances with central banks	**5,971**	6,715
Encumbered cash balances	**(2,133)**	(2,161)
	3,838	4,554
Investments – available for sale	**1,168**	975
Encumbered AFS investments	**(878)**	(268)
	290	707
Total unencumbered liquid assets	**4,128**	5,261

In addition to the above, as at 30 September 2014, the Bank had £3.6bn (2013: £3.2bn) of gross eligible collateral pre-positioned with the Bank of England for potential use in its liquidity facilities.

Funding and liquidity (continued)

	At 30 September 2014 Encumbered £m	Unencumbered £m	Total £m
Encumbered asset summary			
Cash and balances with central banks	2,133	3,838	5,971
Investments – available for sale	878	290	1,168
Loans and advances to customers	6,770	19,131	25,901
	9,781	**23,259**	**33,040**

Encumbered cash and balances with central banks	
Note cover	2,088
Cash ratio deposit	42
Dutch central bank – EU payment system collateral	3
	2,133
Encumbered investments – available for sale	
Payment system collateral [1]	232
Repurchase ("repo") transaction collateral [1]	646
	878
Encumbered loans and advances to customers	
Structured Programme collateral – Lanark Master Trust	3,211
Structured Programme collateral – Regulated Covered Bond	2,007
Structured Programme collateral – Lannraig Master Trust	1,552
	6,770

(1) Market value of securities posted as collateral.

Liquid assets	**2014 £bn**	2013 £bn
UK Government Treasury Bills and Gilts	**1.1**	0.9
Cash and cash at central bank	**3.9**	4.6
Note cover [2]	**2.0**	2.1
Interbank lending	**0.1**	0.3
Liquid assets	**7.1**	7.9

(2) Note cover is excluded from PRA regulatory liquidity.

The Group has reduced its holding of highly liquid assets during the year due to reduced reliance on short-term wholesale funding.

The Group continues to hold £100m of floating rate notes issued by the European Investment Bank and has no direct exposure to any Eurozone Sovereigns as part of its liquidity portfolio.

Strategic report (continued)

Customers, employees and community

The Group continues to support its customers and the communities it serves.

The Yorkshire and Clydesdale Bank Foundation provides financial support to a large number of charities across the UK. In the last 12 months the Foundation has distributed over £812,000 to over 320 worthy causes. The second year of the annual Spirit in the Community Awards saw £150,000 being donated to 24 charities in June 2014. The charity relationship with Help the Hospices is now in its seventh year and over £3.7m has been raised in this time, including matching donations from the Group. In addition, 20% of employees currently donate to their chosen charities through Payroll Giving and the Group's Employee Volunteering Policy offers all employees the opportunity to take two days paid leave to work in the local community.

During the year, the Group won a "Moneynet Personal Finance" award for "Best New Current Account" following the launch of its Current Account Direct product. The Group also won a "National Payroll Giving Excellence" award for having the most successful sustained scheme by a large employer.

Business model challenges and top and emerging risks

The primary areas of risk to the Group's business model are outlined below. Tolerances for appropriate levels of risk for each category, as well as the other risks to which the Group is exposed, are set regularly through the Group's risk appetite statement ("RAS") process. The position against the various RAS settings is monitored and reported to the Group's various management and Board governance committees as set out in note 39 to the financial statements.

- *Credit risk*: this is the risk of financial loss if a customer or counterparty fails to meet their contractual payments. This risk applies to both customer facing segments of the business (Retail and Business & Private Bank) as well as our treasury operations and is continually assessed as the Group's business and key initiatives evolve. Bank lending activities account for most of the Group's credit risk, with a strategic focus on managing the acceptance of a range of potential credit risk exposures. Further detail on the Group's approach to the management of credit risk is included in note 38 to the financial statements.
- *Conduct risk*: this is the risk that the Group's behaviours (culture, governance, systems and controls) lead to inappropriate outcomes for customers, exposing the Group to customer redress costs and the potential for regulatory action. The Group, in common with the rest of the financial services industry, has faced a number of conduct risk challenges in relation to a range of industry wide issues including PPI and Interest Rate Hedging Products. The Group continues to review these challenges in light of on-going customer and regulatory feedback and action. The Group continues to address legacy conduct related matters and is also reviewing new product designs, sales practices and remuneration policies to ensure the potential for future conduct related issues is mitigated. Further detail on the Group's approach and exposures to conduct risk related matters can be found in notes 3, 26, 32 and 39 to the financial statements.
- *Operational risk (excluding conduct risk)*: this is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk. The Group regards operational risks as a core component of doing business as they arise from day-to-day operational activities as well as from organisational changes such as projects and business change initiatives. The Group has focused on improving these areas over recent years with an emphasis on control effectiveness and improvements in the control environment (processes), enhancing skills and appropriate resource allocation (people) and improvements in system resilience and availability. Service interruption and financial crime are two important constituent parts of operational risk, The Group recognises the impact that any service interruption issues may cause to our customers, as well as potential losses or reputational damage resulting from financial crime events. As such, the Group continues to assess and manage its current technical systems landscape and to develop contingency plans to manage and mitigate these risks.

Strategic report (continued)

Business model challenges and top and emerging risks (continued)

- *Pension risk*: the Group is the sponsoring employer in one defined benefit pension scheme ("the Scheme") and is exposed to the risk that, at any point in time, the Scheme is in deficit (i.e. the Scheme's liabilities outweigh its assets). The Scheme's asset values and liabilities are affected by a number of factors including, but not limited to, the discount rate used to calculate the liability net present value, the long-term inflation assumption and other actuarial assumptions (including mortality rates). The Group has implemented a number of reforms in order to de-risk, as far as possible, the ultimate defined benefit pension obligation and liaises with the Scheme's independent Trustees and actuaries on a regular basis to assess the current liability estimate. Nevertheless, the Scheme exposes the Group to substantial future liabilities and is a significant absorber of capital. Further detail on the Scheme (including the actuarial assumptions) is included in note 28 to the financial statements.
- *Financial management risk*: this falls into 3 broad categories:
  - *Capital risk:* this is the risk that the Group does not hold sufficient capital and reserves to meet regulatory requirements, achieve its strategic plans and objectives, or to cover the risks to which it is already exposed and to protect against unexpected losses. Changes in regulation have the potential to change the required level of capital that the Group is required to hold which may adversely impact the Group's financial performance and position.
  - *Funding and liquidity risk:* these are the risks that the Group is unable to raise short and long-term funding to support its strategic plans and objectives and is unable to meet its financial obligations as they fall due. The Group continues to monitor its stable and customer funding indices, holds significant levels of highly liquid assets and maintains the ability to access term funding through its Securitisation and Covered Bond programmes.
  - *Interest rate risk:* this is the risk to the Group's financial performance and position caused by changes in interest rates. As interest rates and yield curves change over time, the Group may be exposed to a loss in earnings and economic value due to the interest rate profile of its balance sheet. The Group actively monitors and manages interest rate risk principally through the use of interest rate swaps.

Further detail on the risks the Group faces and how these are managed is included in note 39 to the financial statements.

The Group monitors the environment in which it operates to identify those emerging risks that can have an impact on how it operates from a strategic, operational and financial perspective. The Group currently considers its top emerging risks to be:

- *The UK and European economy:* while the UK economic recovery is currently gaining momentum it remains fragile and vulnerable to events and trends in Europe. The Group's future plans are linked to the UK economy achieving a current and prolonged period of economic growth and ultimately, in the medium term, to a resumption of more normalised interest rate conditions.
- *The potential for reconstitution of political arrangements for the UK*: the Group faces risks associated with the possible referendum on the UK withdrawing from the EU and implications of the 2015 General Election. The outcome of these events could have a material impact on the regulatory, fiscal and monetary regimes in the UK and in Europe. The potential effect of any change is uncertain but could have a significant impact on the Group's costs, capital requirements and future business.
- *The changing financial industry landscape:* the Group is subject to extensive regulation and changes to this may adversely impact the Group's financial performance and position. Regulations are designed to protect the interests of depositors and the banking and financial services system as a whole. Future changes in laws, regulations and other industry wide initiatives are unpredictable and beyond the Group's control and could adversely affect its business and operations. These changes are influenced by a number of different and competing drivers including evolving stakeholder expectations regarding transparency, competition, financial system stability and international harmonisation.
- *Competition:* there is substantial competition in the UK banking market. Increased competition for customers can have the effect of compressing profit margins, changing terms and conditions, increasing advertising and related expenses to attract and retain customers, increasing customer turnover, decreasing customer loyalty or driving loss of market share. As technology and customer attitudes are rapidly evolving, particularly in the digital arena, this increases the risk of competition, including from new business entrants, and the cost of doing business.

Strategic report (continued)

The risks and challenges identified in the Strategic Report do not represent an exhaustive list of the risks and issues associated with the Group. Other risks and issues not specifically referenced may adversely impact the future financial position and performance of the Group. Accordingly, no assurances or guarantees of future performance, profitability or returns on capital are given by the Group.

The Strategic Report was approved by the Board of Directors on 17 November 2014 and was signed on its behalf by:

David Thorburn

David Thorburn
Chief Executive Officer

Enhanced risk disclosure

In October 2012, the Enhanced Disclosures Task Force ("EDTF"), an industry-led initiative, reported to the Financial Stability Board on how the risk disclosures of banks could be improved to provide a greater level of transparency as well as improving comparability between banks. Their report included seven fundamental principles and 32 recommendations. The recommendations cover the following broad headings:

- general (recommendations 1 to 4);
- risk governance and risk management strategies/business model (recommendations 5 to 8);
- capital adequacy and risk-weighted assets (recommendations 9 to 17);
- liquidity and funding (recommendations 18 to 21);
- market risk (recommendations 22 to 25);
- credit risk (recommendations 26 to 30); and
- other risks (recommendations 31 to 32).

The EDTF noted that the fundamental principles are applicable to all banks but noted: "We have developed the recommendations for enhanced risk disclosures with large international banks in mind although they should be equally applicable to banks that actively access the major public equity or debt markets. We believe that many of the recommendations may be adopted in 2012 or 2013. However, some recommendations… will take longer to develop and implement… We would expect smaller banks and the subsidiaries of listed banks will adopt only those aspects of the recommendations that are relevant to them." In June 2013 year the Financial Policy Committee ("FPC") made a recommendation that all major UK banks and building societies should comply with the recommendations on a 'comply or explain' basis, under Section 9Q(3) of the Bank of England Act 1998 (as amended by the Financial Services Act 2012).

The Group agrees with and supports the primary objectives of the EDTF and is committed to ensuring compliance with the EDTF's principles and recommendations where possible against the backdrop of the Group's ownership, its position within the UK market and the globally systemic reach of the EDTF's objectives and aims, noting the more recent pronouncement of the FPC.

The Group already provides risk disclosures in accordance with International Financial Reporting Standards which can be found in notes 38, 39 and 40 to the financial statements, with the appropriate cross references made between these notes and the relevant EDTF recommendation as necessary to avoid duplicating information.

In its full year Pillar 3 Report for the year ended 30 September 2013, our ultimate Parent, National Australia Bank Limited, described Clydesdale Bank PLC, as its subsidiary in the United Kingdom, who is regulated by the Prudential Regulation Authority (PRA) and had been accredited to apply the standardised approach to operational and credit risk management in accordance with the regulatory requirements. As described in note 41 to the financial statements, the Group relies on references to comparable National Australia Bank Limited consolidated disclosure to satisfy its Pillar 3 disclosure obligations.

Accordingly, in assessing the EDTF's recommendations, the Bank has taken all of these factors into consideration and applied a measured and proportionate approach with the recommended disclosures. We have applied those recommendations we believe are of more direct relevance to our position as a wholly owned subsidiary applying a standardised approach to operational and credit risk management. The additional disclosures included are designed to increase the reader's understanding of our financial position and risk governance and management.

The table and disclosures from pages 149 to 153 provide a brief description of the EDTF recommendations with the accompanying narrative cross referring to other disclosures provided in the financial statements (where relevant) and/or the additional detail (both quantitative and qualitative where necessary) we believe satisfy the EDTF requirements.

Report of the Directors

The Directors of the Bank with its subsidiary undertakings (which together comprise the "Group") submit their report and consolidated financial statements for the year ended 30 September 2014.

Profits and appropriations

The Group loss before tax for the year ended 30 September 2014 was £216m (2013: loss of £54m). The loss attributable to the shareholders for the year ended 30 September 2014 amounted to £178m (2013: loss of £44m). Preference share dividends of £14m (2013: £24m) were paid during the year. The Directors do not recommend the payment of a final dividend on the ordinary shares in respect of this financial year (2013: £Nil).

The Group's strategic highlights and business developments are set out in the Strategic Report on pages 4 to 21.

Financial instruments

The Group's risk management objectives and policies are discussed in note 39.

Directors and Directors' interests

The current Directors are shown on page 1. Directors who are not full-time employees of the Group or a related body corporate are appointed in accordance with the Articles of Association and may be eligible for reappointment thereafter. No Directors retired by rotation during the year.

Directors' interests

No Director had any interest in the shares of the Group or its subsidiaries at any time during the year. As the Group is a wholly owned subsidiary of NAB, any interest which the Directors may have in NAB does not need to be notified to the Group, and therefore is not disclosed in this report.

Appointments

Debbie Crosbie was appointed as a Director of the Company on 12 May 2014.
Teresa Robson-Capps was appointed as a Director of the Company on 8 October 2014.

Resignations

Mark Joiner resigned as a Director of the Company on 31 December 2013.
Cameron Clyne resigned as a Director of the Company on 1 August 2014.
John Hooper resigned as a Director of the Company on 31 October 2014.
Jennifer Darbyshire resigned as Company Secretary on 1 October 2014.

Directors' liabilities

During the year, the NAB Group paid a premium for a contract insuring the Directors and Officers of NAB, its subsidiaries and controlled entities against personal liabilities which may arise in the course of the performance of their duties, as well as protecting the Group itself to the extent that it is obligated to indemnify Directors and Officers for such liability.

Employee involvement

The Group regularly communicates with staff to keep them informed of business objectives and results using methods including the intranet site and all employee telephone calls with the Executive Committee.

Under the UK National Share Incentive Plan, employees are entitled to purchase up to £1,800 worth of NAB shares each year. Participants contribute each month and the trustee uses the contributions to purchase shares on the open market or issue shares which are then held in trust for the participants. Participants are entitled to receive dividends and exercise voting rights in respect of these shares whilst they are members of the plan and there is no risk of forfeiture. In addition, up to £3,000 of free shares per employee may be gifted per annum through the plan.

During the year, under the UK National Share Incentive Plan, NAB gifted ordinary shares of A$900 in total to each eligible employee based on Group performance in respect of the 2013 financial year. A similar offer A$1,000 for the 2014 financial year has been announced and is based on Group performance.

Equality of employment opportunities

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

The staff network group and membership of the Business Disability Forum provides an ongoing opportunity for progress by identifying and implementing improvements.

The Group is authorised as a “two tick” symbol user by Jobcentre Plus. The disability symbol is a recognition given by Jobcentre Plus to employers who have agreed to take action to meet five commitments regarding the employment, retention, training and career development of disabled employees, and to continually review progress and improve on what they do. Employers who wish to become a symbol user have to evidence they can achieve those commitments in their application.

Political donations

No political donations were made during the year (2013: £Nil).

Corporate governance

The Group confirms that it complies with the Prudential Regulation Authority’s Senior Management Arrangements, Systems and Controls sourcebook (“SYSC”) 4.3A.11R requiring a firm that maintains a website to explain on the website how it complies with certain requirements of SYSC relating to governance. Statements of compliance are included in the Corporate Governance section of the Group's website at www.cbonline.co.uk/corporategovernance and www.ybonline.co.uk/corporategovernance.

To demonstrate compliance with certain of the SYSC requirements the Group has published a Corporate Governance Statement. It is the Group's policy not to include all of the disclosures in respect of voluntary corporate governance Codes of Practice as it is a wholly owned subsidiary of NAB. The NAB Group's Annual Financial Report details the full Corporate Governance framework applicable to the Group and its subsidiaries. These disclosures are made after consideration of authoritative pronouncements on Audit Committees and associated disclosures in Australia and the UK. Remuneration policy is not the responsibility of the Board. The remuneration policy that applies to employees and Directors of the Group is decided at the NAB Group level.

Management of risk

The Group has a well-established Boards' Risk Committee for the consideration of risks. The membership is shown on the list of Directors on page 1 and the Committee meets at quarterly intervals. The NAB Group publishes an annual and half-yearly "Risk and Capital Report" which provides extensive and rigorous coverage of all aspects of risk considered relevant including the position in the UK. Further disclosure on the Group's risk management structure in the UK is included in note 39.

Going concern

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

The Group's use of the going concern basis for preparation of the accounts is discussed in note 1.

Events after the balance sheet date

There have been no subsequent events which have occurred since 30 September 2014 that would require disclosure in the annual report and financial statements of Clydesdale Bank PLC.

Auditors

In accordance with section 485 of the Companies Act 2006, a resolution to reappoint Ernst & Young LLP, and to authorise the Directors to fix their remuneration, will be proposed at the next Annual General Meeting.

The Directors who were members of the Board at the time of approving the Report of the Directors are listed on page 1. Having made enquiries of fellow Directors and of the Group's auditor, each of these Directors confirms that:

- to the best of each Director's knowledge and belief, there is no information relevant to the preparation of their report of which the Group's auditor is unaware; and
- each Director has taken all the steps a Director might reasonably be expected to have taken to be aware of relevant audit information and to establish that the Group's auditor is aware of that information.

By order of the Board

LFM

Lorna McMillan
Company Secretary
17 November 2014

Statement of Directors' responsibilities

The Directors are responsible for preparing the Strategic Report, Directors' Report and the financial statements in accordance with applicable law and regulations.

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

- select suitable accounting policies in accordance with International Accounting Standard 8: Accounting Policies, Changes in Accounting Estimates and Errors and then apply them consistently;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the financial performance; and
- state that the Group and Bank have complied with IFRSs, subject to any material departures disclosed and explained in the financial statements.

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

Lorna McMillan
Company Secretary
17 November 2014

Building a better working world

Independent auditor's report to the members of Clydesdale Bank PLC

We have audited the financial statements of Clydesdale Bank PLC for the year ended 30 September 2014 which comprise the Consolidated Income Statement, the Group and Bank Statements of Comprehensive Income, the Group and Bank Balance Sheets, the Group and Bank Statements of Changes in Equity, the Group and Bank Statements of Cash Flow and the related notes 1 to 42. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the Bank's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Bank's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 26, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group and Bank's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the Group and Bank's affairs as at 30 September 2014 and of the Group's loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the Bank's financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Report of Directors for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the Group financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Javier Faiz (Senior Statutory Auditor)
For and on behalf of Ernst & Young LLP
Statutory Auditor, London
17 November 2014

Notes:

1. The maintenance and integrity of the Clydesdale Bank PLC web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.

2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Consolidated financial statements

Contents

Consolidated income statement
for the year ended 30 September 2014

	Note	2014 £m	2013 £m As restated
Interest income and similar income		**1,135**	1,209
Interest expense and similar charges		**(364)**	(453)
Net interest income	5	**771**	756
Gains less losses on financial instruments at fair value		**11**	(14)
Other operating income		**181**	198
Non-interest income	6	**192**	184
Total operating income		**963**	940
Personnel expenses		**(216)**	(224)
Depreciation expense		**(19)**	(19)
Other operating and administrative expenses		**(870)**	(607)
Total operating and administrative expenses before impairment losses	7	**(1,105)**	(850)
Operating (loss)/profit before impairment losses		**(142)**	90
Impairment losses on credit exposures	16	**(74)**	(144)
Loss on ordinary activities before tax		**(216)**	(54)
Analysed as:			
Profit before tax, Payment Protection Insurance redress expense, FSCS levy and bank levy		**218**	87
Payment Protection Insurance redress expense	26	**(420)**	(130)
FSCS levy and bank levy		**(14)**	(11)
Loss on ordinary activities before tax		**(216)**	(54)
Tax credit	8	**38**	10
Loss for the year attributable to the equity holders of the parent		**(178)**	(44)

All material items dealt with in arriving at the loss before tax for the above periods relate to continuing activities.

The notes on pages 36 to 148 form an integral part of these financial statements.

Statements of comprehensive income
for the year ended 30 September 2014

	Note	Group 2014 £m	Group 2013 £m As restated	Bank 2014 £m	Bank 2013 £m As restated
(Loss)/profit for the year		**(178)**	(44)	**(183)**	46
Items that may be reclassified to the income statement					
Change in cash flow hedge reserve					
Gains/(losses) during the year		**1**	(81)	**1**	(81)
Transfers to the income statement		**(50)**	(51)	**(50)**	(51)
Taxation thereon		**10**	31	**10**	31
		(39)	(101)	**(39)**	(101)
Change in available for sale investments reserve					
Gains/(losses) during the year		**4**	(13)	**4**	(13)
Taxation thereon		**(1)**	6	**(1)**	5
		3	(7)	**3**	(8)
Total items that may be reclassified to the income statement		**(36)**	(108)	**(36)**	(109)
Items that will not be reclassified to the income statement					
Actuarial gains on defined benefit pension plans	28	**24**	21	**24**	21
Restatement in respect of rate change/taxation thereon		**(2)**	(37)	**(2)**	(37)
		22	(16)	**22**	(16)
Change in asset revaluation reserve					
Restatement in respect of rate change/taxation thereon		**1**	1	**1**	1
		1	1	**1**	1
Total items that will not be reclassified to the income statement		**23**	(15)	**23**	(15)
Other comprehensive losses net of taxation		**(13)**	(123)	**(13)**	(124)
Total comprehensive losses for the year		**(191)**	(167)	**(196)**	(78)
Attributable to equity holders of the parent		**(191)**	(167)	**(196)**	(78)

The notes on pages 36 to 148 form an integral part of these financial statements.

Balance sheets
as at 30 September 2014

	Note	Group 2014 £m	Group 2013 £m As restated	Bank 2014 £m	Bank 2013 £m As restated
Assets					
Cash and balances with central banks	10	5,971	6,715	5,971	6,715
Due from related entities	11	1,495	1,417	3,010	5,979
Due from other banks		13	184	13	184
Investments – available for sale	12	1,168	975	1,168	975
Investments – held to maturity	12	-	-	1,483	1,415
Other financial assets at fair value	13	1,583	2,171	1,583	2,171
Derivative financial instruments	14	220	244	220	244
Loans and advances to customers	15	25,901	23,960	24,450	19,438
Due from customers on acceptances		5	4	5	4
Current tax assets		-	23	-	18
Property, plant and equipment	18	106	120	106	120
Investment properties	19	44	63	44	63
Property inventory	20	2	6	2	6
Investments in controlled entities and associates	21	2	3	12	609
Deferred tax assets	22	287	227	281	221
Defined benefit pension assets	28	49	-	49	-
Other assets	23	237	381	204	339
Total assets		37,083	36,493	38,601	38,501
Liabilities					
Due to other banks	24	914	521	914	521
Other financial liabilities at fair value	13	91	123	91	123
Derivative financial instruments	14	548	651	451	566
Due to customers	25	24,073	24,355	24,073	24,355
Liabilities on acceptances		5	4	5	4
Current taxes		19	-	36	-
Provisions	26	952	315	952	315
Due to related entities	11	2,452	2,860	6,465	6,931
Bonds and notes	27	3,453	3,085	1,108	1,110
Retirement benefit obligations	28	4	202	4	202
Deferred tax liabilities	22	10	7	10	7
Other liabilities	29	2,057	1,960	2,017	1,982
Total liabilities		34,578	34,083	36,126	36,116
Equity (parent entity interest)					
Share capital	30	2,042	1,742	2,042	1,742
Share premium	31	243	243	243	243
Other reserves	31	334	370	334	370
Retained earnings	31	(114)	55	(144)	30
Total equity		2,505	2,410	2,475	2,385
Total liabilities and equity		37,083	36,493	38,601	38,501

The notes on pages 36 to 148 form an integral part of these financial statements.

These financial statements were approved by the Board of Directors on 17 November 2014 and were signed on its behalf by:

David Thorburn.

David Thorburn
Chief Executive Officer

Company name: Clydesdale Bank PLC

Company number: SC001111

Statements of changes in equity
for the year ended 30 September 2014

Group

	Note	Share capital £m	Share premium account £m	Merger reserve £m	Share option reserve £m	Asset revaluation reserve £m	Available for sale investments reserve £m	Cash flow hedge reserve £m	Retained earnings £m As restated	Total equity £m As restated
As at 1 October 2012		1,742	243	338	5	1	12	124	139	2,604
Loss for the year		-	-	-	-	-	-	-	(44)	(44)
Other comprehensive income/(losses)		-	-	-	-	1	(7)	(101)	(16)	(123)
Total comprehensive income/(losses) for the year		-	-	-	-	1	(7)	(101)	(60)	(167)
Dividends paid – preference shares	9	-	-	-	-	-	-	-	(24)	(24)
Share options expensed		-	-	-	3	-	-	-	-	3
Share options settled		-	-	-	(6)	-	-	-	-	(6)
As at 30 September 2013	30, 31	**1,742**	**243**	**338**	**2**	**2**	**5**	**23**	**55**	**2,410**
Loss for the year		-	-	-	-	-	-	-	(178)	(178)
Other comprehensive income/(losses)		-	-	-	-	-	3	(39)	23	(13)
Total comprehensive income/(losses) for the year		-	-	-	-	-	3	(39)	(155)	(191)
Dividends paid – preference shares	9	-	-	-	-	-	-	-	(14)	(14)
Shares issued – ordinary shares		600	-	-	-	-	-	-	-	600
Share redemption – preference shares		(300)	-	-	-	-	-	-	-	(300)
Share options expensed		-	-	-	6	-	-	-	-	6
Share options settled		-	-	-	(6)	-	-	-	-	(6)
As at 30 September 2014	30, 31	**2,042**	**243**	**338**	**2**	**2**	**8**	**(16)**	**(114)**	**2,505**

The notes on pages 36 to 148 form an integral part of these financial statements.

Statements of changes in equity (continued)
for the year ended 30 September 2014

Bank

	Note	Share capital £m	Share premium account £m	Merger reserve £m	Share option reserve £m	Asset revaluation reserve £m	Available for sale investments reserve £m	Cash flow hedge reserve £m	Retained earnings £m As restated	Total equity £m As restated
As at 1 October 2012		1,742	243	338	5	1	13	124	24	2,490
Profit for the year		-	-	-	-	-	-	-	46	46
Other comprehensive income/ (losses)		-	-	-	-	1	(8)	(101)	(16)	(124)
Total comprehensive income/ (losses) for the year		-	-	-	-	1	(8)	(101)	30	(78)
Dividends paid – preference shares	9	-	-	-	-	-	-	-	(24)	(24)
Share options expensed		-	-	-	3	-	-	-	-	3
Share options settled		-	-	-	(6)	-	-	-	-	(6)
As at 30 September 2013	30, 31	**1,742**	**243**	**338**	**2**	**2**	**5**	**23**	**30**	**2,385**
Loss for the year		-	-	-	-	-	-	-	(183)	(183)
Other comprehensive income/ (losses)		-	-	-	-	-	3	(39)	23	(13)
Total comprehensive income/ (losses) for the year		-	-	-	-	-	3	(39)	(160)	(196)
Dividends paid – preference shares	9	-	-	-	-	-	-	-	(14)	(14)
Shares issued – ordinary shares		600	-	-	-	-	-	-	-	600
Share redemption – preference shares		(300)	-	-	-	-	-	-	-	(300)
Share options expensed		-	-	-	6	-	-	-	-	6
Share options settled		-	-	-	(6)	-	-	-	-	(6)
As at 30 September 2014	30, 31	**2,042**	**243**	**338**	**2**	**2**	**8**	**(16)**	**(144)**	**2,475**

The notes on pages 36 to 148 form an integral part of these financial statements.

Statements of cash flows
for the year ended 30 September 2014

	Note	Group 2014 £m	Group 2013 £m As restated	Bank 2014 £m	Bank 2013 £m As restated
Operating activities					
(Loss)/profit on ordinary activities before tax		**(216)**	(54)	**(230)**	24
Adjustments for:					
Non-cash or non-operating items included in loss before tax	33	**(696)**	(583)	**(622)**	(658)
Changes in operating assets	33	**(1,191)**	6,129	**(4,259)**	6,012
Changes in operating liabilities	33	**563**	(2,636)	**528**	(2,674)
Interest received		**1,134**	1,213	**1,085**	1,114
Interest paid		**(257)**	(317)	**(278)**	(316)
Tax received- group relief		**34**	50	**55**	80
Net cash (used in)/provided by operating activities		**(629)**	3,802	**(3,721)**	3,582
Cash flows from investing activities					
Dividends received		**-**	-	**26**	116
Interest received		**8**	8	**8**	8
Proceeds from sale or maturity of investments		**50**	50	**59**	121
Return of subsidiary company capital		**-**	-	**-**	4
Proceeds from sale of tangible fixed assets [(1)]		**41**	39	**41**	37
Purchase of tangible fixed assets [(1)]		**(16)**	(32)	**(16)**	(32)
Purchase of available for sale investments		**(251)**	(50)	**(251)**	(50)
Purchase of held to maturity investments		**-**	-	**(76)**	(777)
Net cash (used in)/provided by investing activities		**(168)**	15	**(209)**	(573)
Cash flows from financing activities					
Interest received		**4**	5	**58**	56
Interest paid		**(132)**	(132)	**(213)**	(133)
Proceeds from ordinary shares issued	30	**600**	-	**600**	-
Redemption of preference shares	30	**(300)**	-	**(300)**	-
Redemption, principal repayment and other movements on residential mortgage backed securities and covered bonds	17	**(216)**	(613)	**-**	-
Issuance of residential mortgage backed securities and covered bonds	17	**601**	541	**-**	-
Net (increase)/decrease in amounts due from related entities		**(73)**	(152)	**2,960**	(159)
Net (decrease)/increase in amounts due to related entities		**(338)**	(4,846)	**174**	(4,246)
Dividends paid	9	**(14)**	(24)	**(14)**	(24)
Net cash provided by/(used in) financing activities		**132**	(5,221)	**3,265**	(4,506)
Net decrease in cash and cash equivalents		**(665)**	(1,404)	**(665)**	(1,497)
Cash and cash equivalents at the beginning of the year		**6,545**	7,949	**6,545**	8,042
Cash and cash equivalents at the end of the year	33	**5,880**	6,545	**5,880**	6,545

(1) Tangible fixed assets include property, plant and equipment, investment properties and property inventory.

The notes on pages 36 to 148 form an integral part of these financial statements.

Notes to the consolidated financial statements

1. Basis of preparation

Reporting entity

The Bank is incorporated in the UK and registered in Scotland. The consolidated financial statements comprise the Bank and its controlled entities (together the "Group"). The Group's principal controlled entities are listed in note 21.

The ultimate parent undertaking, and ultimate controlling party is NAB, a company incorporated in the State of Victoria, Australia. NAB also heads the largest group in which the results of the Group are consolidated. The smallest group in which the results of the Group are consolidated is that headed by the Group's immediate parent, NAGE, which is incorporated and registered in England and Wales.

Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with IFRS as adopted by the European Union (EU) as applied in accordance with the provisions of the Companies Act 2006. As permitted by section 408 of the Companies Act 2006, no income statement is presented for the Bank.

The consolidated financial statements of the Group for the year ended 30 September 2014 were authorised for issue by the Board of Directors on 17 November 2014.

Basis of measurement

The financial information has been prepared under the historical cost convention, as modified by the revaluation of land and buildings, investment properties, available-for-sale financial assets and certain other financial assets and liabilities at fair value through profit or loss and all derivative contracts.

Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report. In addition, note 39 to the financial statements includes the Group's risk management objectives and note 40 to the financial statements includes the Group's objectives, policies and processes for managing its capital.

The Directors have a reasonable expectation that the Bank and the Group have adequate resources to continue in operational existence for the foreseeable future and therefore believe that the Group is well placed to manage its business risks successfully despite the current uncertain economic outlook. Accordingly, they continue to adopt the going concern basis in preparing the consolidated financial statements.

Notes to the consolidated financial statements (continued)

1. Basis of Preparation (continued)

Prior year restatement

Payment Protection Insurance ("PPI") redress

Consistent with its ultimate parent, the Group has reclassified costs related to PPI redress from Other operating income to Other operating and administrative expense within the consolidated income statement. This change has been applied retrospectively in these financial statements and the prior year comparative disclosures restated accordingly.

The impact on the Group's result for the year ended 30 September 2013 was an increase in Other operating income of £130m, with a corresponding increase in Other operating and administrative expense of £130m. In addition, note 4 'Segment information', note 6 'Non-interest income' and note 7 'Operating and administrative expenses' have been impacted by the restatement. There has been no impact on the Group's or Bank's total assets, net assets or reserves as a result of the change.

Amendments to IAS 19 'Employee benefits

As detailed in note 2 ' Accounting Policies', the Group has adopted amendments to IAS 19 'Employee Benefits' in the current financial year. This change has been applied retrospectively and comparatives restated accordingly.

In the comparative period to 30 September 2013, the personnel expenses line in the consolidated income statement has been increased by £21m (with a tax effect of £4m) with an offsetting adjustment to the actuarial gains/(losses) on defined benefit plans in the statement of comprehensive income. In addition, note 4 'Segment information', note 8 'Taxation', note 22 'Deferred tax', note 33 'Notes to the statement of cash flows' and note 28 'Retirement benefit obligations' have been impacted by the restatement. There has been no impact on the Group or Bank's total assets, net assets or reserves at 30 September 2013 as a result of the change.

Accrued interest

Consistent with other UK banks and financial institutions, from 11 November 2014 the Group will submit financial reporting information ("FINREP") to the Prudential Regulatory Authority ("PRA") in a European Banking Authority ("EBA") prescribed format. The first reporting date is 30 September 2014. Where this does not require a change in accounting policy, the Group has chosen to conform the classification convention of items in the consolidated financial statements with the FINREP reporting format. This decision has been taken in order to assist comparability and minimise reconciliation differences between the financial statements and FINREP reporting.

The principal changes are the reclassification of certain interest receivable and payable amounts on the balance sheet from other assets and other liabilities into the relevant line items of the underlying financial instruments; and the treatment of forbearance (note 38). Derivative interest receivable and payable have also been grouped at a trade level in order to reflect the net amount due to or from the derivative counterparty.

Prior year comparative disclosures have been amended to conform the classification of interest receivable and payable amounts with current year presentation. This has resulted in a reduction of total assets and total liabilities in the Group's balance sheet at 30 September 2013 of £139m; and a reduction of total assets and total liabilities in the Bank's balance sheet of £96m. Accrued interest reclassified within prior period comparative disclosures is shown within the notes to the financial statements for loans and advances due to customers (note 15); due to customers (note 25) and bond and notes (note 27). The impact on the Group's and Bank's prior period comparative disclosures for other balance sheet lines impacted is detailed below.

Amounts due from related entities increased by £9m and £38m for Group and Bank respectively; investments - available for sale increased by £2m for both Group and Bank; other financial assets at fair value increased by £16m for both Group and Bank; derivative financial assets increased by £4m for both Group and Bank; other assets decreased by £235m and £206m for Group and Bank respectively; other financial liabilities at fair value increased by £3m in both Group and Bank; derivative financial liabilities decreased by £12m and £1m in Group and Bank respectively; amounts due to related entities increased by £10m and £nil in Group and Bank respectively; and other liabilities decreased by £362m and £322m in Group and Bank respectively. These changes have no impact on the Group's and the Bank's statements of income and comprehensive income for current and prior years.

2. Accounting policies

Basis of consolidation

Controlled entities are all entities (including structured entities) to which the Bank is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. An assessment of control is performed on an ongoing basis. For details of material controlled entities refer to note 21.

Controlled entities are consolidated from the date on which control is established by the Bank until the date that control ceases. The acquisition method of accounting is used to account for the acquisition of controlled entities. Balances and transactions between entities within the Group and any unrealised gains and losses arising from those transactions are eliminated in full upon consolidation. The consolidated financial statements have been prepared using uniform accounting policies and are based on the same accounting period as NAB.

New accounting standards and interpretations adopted during the year

The Group has adopted the following IASB pronouncements in the current financial year:

- Amendments to IAS 19 *'Employee Benefits'*, issued June 2011 and effective for financial years beginning on or after 1 January 2013. The amended accounting standard requires the amounts recorded in profit or loss to be limited to current and past service costs, gains or losses, settlements and net interest income/(expense). All other changes in the net defined benefit asset/(liability) including actuarial gains and losses, will be recognised in other comprehensive income with no subsequent recycling into profit or loss. The expected return on plan assets is no longer recognised in profit or loss. Instead, interest income is now measured using the same discount rate used to measure the defined benefit obligation. This change has been applied retrospectively and comparatives restated accordingly. A summary of the restatement impact is included in note 1 'Basis of Preparation'.
- Amendments to IFRS 7 *'Financial Instruments: Disclosures – Offsetting Financial Assets and Liabilities'*, issued December 2011 and effective for financial years beginning on or after 1 January 2013. The amendments require disclosures regarding the Group's financial instruments that are either offset in the consolidated statement of financial position or subject to an enforceable master netting agreement or similar arrangement, see note 38.
- IFRS 13 *'Fair Value Measurement'*, issued May 2011 and effective for financial years beginning on or after 1 January 2013. IFRS 13 establishes a single source of guidance for fair value measurements and disclosures about fair value measurements. IFRS 13 applies to both financial instrument items and non-financial instrument items for which other IFRSs require or permit fair value measurements and disclosures about fair value measurements, except for share-based payment transactions that are within the scope of IFRS 2 *'Share-based Payment'*, leasing transactions that are within the scope of IAS 17 *'Leases'*, and measurements that have some similarities to fair value but are not fair value (e.g. value in use for impairment assessment purposes).

  IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions. Fair value under IFRS 13 is an exit price regardless of whether that price is directly observable or estimated using another valuation technique. IFRS 13 also includes extensive disclosure requirements.

  The application of IFRS 13 has not had any material impact on the amounts recognised in the consolidated financial statements, however additional disclosures have been incorporated in this financial report. In accordance with transitional provisions, comparatives have not been presented.

2. Accounting policies (continued)

New accounting standards and interpretations adopted during the year (continued)

- *'Annual Improvements to IFRSs 2009 – 2011 cycle'*, issued May 2012 and effective for financial years beginning on or after 1 January 2013. The IASB made amendments to the following standards that are relevant to the Group: IAS 1 *'Presentation of financial statements'*, IAS 32 *'Financial Instruments Presentation'* and IAS 34 *'Interim financial reporting'*. The impact of these amendments is not considered to be material to the Group.

The Group has elected to early adopt the following IASB pronouncements in the current year:

- IFRS 10 *'Consolidated Financial Statements'*, IFRS 11 *'Joint Arrangements'*, IFRS 12 *'Disclosure of Interests in Other Entities'*, issued May 2011 and effective for financial years beginning on or after 1 January 2013 (with the application date for EU entities being financial years beginning on or after 1 January 2014). The Group chose to early adopt these standards from 1 October 2013 to align with the ultimate parent company.

  IFRS 10 introduces a single control model to determine which investees should be consolidated. It defines control as consisting of three elements: power, exposure to variable returns and an investor's ability to use power to affect its amount of variable returns. This requires an analysis of all facts and circumstances and the application of judgement in making the control assessment. IFRS 11 introduces a revised model for accounting for joint arrangements. There has been no material impact to the Group as a result of adopting IFRS 10 and IFRS 11.

  IFRS 12 requires new disclosure requirements on interests held in subsidiaries and structured entities, which are included in notes 17 and 21.
- IAS 27 *'Consolidated and Separate Financial Statements'* and IAS 28 *'Investment in Associates and Joint Ventures'*, issued May 2011 and effective for financial years beginning on or after 1 January 2013 (with the application date for EU entities being financial years beginning on or after 1 January 2014). The Group chose to early adopt this standard from 1 October 2013 to align with the ultimate parent company. There has been no material impact to the Group as a result of adopting IAS 27 and IAS 28.
- IFRIC Interpretation 21 *'Levies'* issued May 2013 and effective for financial years beginning on or after 1 January 2014. The Group has early adopted IFRIC 21 with effect from 1 October 2013. The IFRIC addresses the accounting for a liability to pay a levy recognised in accordance with IAS 37 *'Provisions, Contingent liabilities and Contingent assets'*, and the liability to pay a levy whose timing and amount is certain. The revised interpretation has not had any material impact on the amounts recognised in the consolidated financial statements.

New accounting standards and interpretations not yet adopted

The following IASB pronouncements are relevant to the Group and were available for adoption in the European Union, but are not mandatory and have not been applied by the Group in the 30 September 2014 reporting year. The impact of these pronouncements is still being assessed by the Group. Except where otherwise stated, the Group does not expect that the adoption of the following standards, amendments to standards and interpretations will have a material impact on the financial statements:

- IAS 39 *'Novation of Derivatives and Continuation of Hedge accounting – Narrow Scope Amendment'*, issued June 2013 and effective for financial years beginning on or after 1 January 2014. This narrow scope amendment addresses the question around whether hedge accounting can be continued if an entity novates its hedging derivative from one counterparty to a central clearing counterparty as a result of regulatory changes if specific conditions are met.
- Amendments to IAS 32 *'Financial instruments – Presentation'*, issued December 2011 and effective for financial years beginning on or after 1 January 2014. This amendment provides clarification to the criteria that already exist for offsetting.
- Amendments to IAS 36 *'Recoverable Amount Disclosures for Non-Financial Assets'* issued May 2013 and effective for financial years beginning on or after 1 January 2014. This amends the disclosure requirements of IAS 36 to include additional information about the fair value measurement where the recoverable amount of the impaired asset is based on fair value less costs of disposal.

2. Accounting policies (continued)

New accounting standards and interpretations not yet adopted (continued)

The following IASB pronouncements are relevant to the Group but are not available for adoption in the European Union and have not been applied by the Group in the 30 September 2014 reporting year. The impact of these pronouncements is still being assessed by the Group. Except where otherwise stated, the Group does not expect that the adoption of the following standards, amendments to standards and interpretations will have a material impact on the financial statements:

- IFRS 9 *'Financial Instruments'*, issued July 2014 and effective for financial years beginning on or after 1 January 2018. This standard replaces IAS 39 *'Financial instruments: Recognition and measurement'* and contains new requirements for the recognition and measurement of financial assets and liabilities, the recognition of impairment, and hedge accounting.

  The revised recognition and measurement approach will lead to the Group's financial assets being classified as either amortised cost, fair value through other comprehensive income, or fair value through the income statement, dependant on the business model and cash flow characteristics of the financial asset. Financial liabilities will in most cases be accounted for as at present. One exception is where the Group opts to fair value a financial liability. Movement in fair value due to own credit risk would be directly recognised in other comprehensive income.

  The impairment of financial assets under IFRS 9 will be based on expected credit losses rather than incurred credit losses as at present.

  Hedge accounting proposals will amend existing IAS 39 approaches for micro hedge accounting. Accounting for dynamic risk management (macro hedge accounting) has been decoupled from IFRS 9 and is now subject to separate consultation.

  IFRS 9 will introduce significant changes in the way the Group accounts for financial instruments with the full impact on the Group's results still being assessed. There is currently no definitive date for the European Union endorsement of this standard.
- IFRS 15 *'Revenue from Contracts with Customers'*, issued May 2014 and effective for financial years beginning on or after 1 January 2017. This standard establishes principles for reporting information about the nature, timing, and uncertainty of revenue and cash flows arising from an entity's contracts with customers. The standard provides a single, principles based five step model to be applied to all contracts with customers.
- *'Annual improvements to IFRS 2010-2012 cycle'* issued December 2013 and effective for financial years beginning on or after 1 July 2014. The IASB have made amendments to the following standards that are relevant to the Group: IFRS 2 *'Share based payments'*, IFRS 3 *'Business Combinations'*, IFRS 8 *'Operating Segments'*, IFRS 13 *'Fair Value Measurement*, IAS 16 *'Property, Plant and Equipment'* and IAS 24 *'Related party disclosures'*.
- *'Annual improvements to IFRS 2011-2013 cycle'*, issued December 2013 and effective for financial years beginning on or after 1 July 2014. The IASB have made amendments to the following standards that are relevant to the Group: IFRS 3 *'Business Combinations'*, IFRS 13 *'Fair value measurement'* and IAS 40 *'Investment Property'*.
- *'Defined benefit plans: Employee Contributions (Amendments to IAS 19')*, issued November 2013 and effective for financial years beginning on or after 1 July 2014. This amendment to IAS 19 permits certain contributions from employees or third parties (only those contributions that are independent of the number of years of service) to be recognised as a reduction in the service cost in the period in which the employee's services are rendered, rather being attributed to periods of service as a 'negative benefit'.
- Amendments to IAS 16: *'Clarification of acceptable methods of depreciation and amortisation'*, issued May 2014 and effective for financial years beginning on or after 1 January 2016. IAS 16 establishes the principle for the basis of depreciation being the expected pattern of consumption of the future economic benefits of an asset. This amendment provides clarification that the use of certain revenue based methods to calculate depreciation are not appropriate.
- Amendments to IAS 27: *'Equity Method in Separate Financial Statements'*, issued August 2014 and effective for financial years beginning on or after 1 January 2016. The amendments to IAS 27 will allow entities to use the equity method to account for investments in subsidiaries, joint ventures and associates in their separate financial statements.

2. Accounting policies (continued)

Foreign currency

Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in pounds sterling (GBP), which is the Group's functional and presentation currency, rounded to the nearest million pounds sterling (£m) unless otherwise stated.

Transactions and balances

Initially, at the date of a foreign currency transaction, the Group records an asset, liability, expense or revenue arising from a transaction using the end of day spot exchange rate between the functional and foreign currency on the transaction date.

Subsequently, at each reporting date, the Group translates foreign currency monetary items at the closing rate. Foreign exchange differences arising on translation or settlement of monetary items are recognised in the income statement during the year in which the gains or losses arise. Foreign currency non-monetary items measured at historical cost are translated at the date of the transaction. Foreign currency non-monetary items measured at fair value will be translated at the date when the fair value is determined. Foreign exchange differences are recognised directly in equity for non-monetary items where any component of associated gains or losses is recognised directly in equity. Foreign exchange differences arising from non-monetary items, whereby the associated gains or losses are recognised in the income statement, are also recognised in the income statement.

Revenue recognition

Net interest income

Interest income is reflected in the income statement using the effective interest method.

The effective interest method is a method of calculating amortisation using the effective interest rate of a financial asset or financial liability. The effective interest rate is the rate that exactly discounts the estimated stream of future cash payments or receipts over the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or liability.

When calculating the effective interest rate, the cash flows are estimated considering all contractual terms of the financial instrument (e.g. prepayment, call and similar options) excluding future credit losses.

The calculation of the effective interest rate includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts. Where it is not possible to estimate reliably the cash flows or the expected life of a financial instrument (or group of financial instruments), the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments) are used.

Loan origination and commitment fees are recognised as revenue within the effective interest rate calculation. When the non-utilisation of a commitment fee occurs, this is taken as revenue upon expiry of the agreed commitment period. Loan related administration and service fees are recognised as revenue over the period of service.

Direct loan origination costs are netted against loan origination fees and the net amount recognised as revenue over the life of the loan as an adjustment of yield. All other loan related costs are expensed as incurred.

Fees and commissions

Fees and commissions not integral to the effective interest rate arising from services provided to customers and third parties are recognised once the service has been provided.

2. Accounting policies (continued)

Gains less losses on financial instruments at fair value through profit or loss

Gains less losses on financial instruments at fair value through profit or loss comprise fair value gains and losses from three distinct activities:

- trading derivatives;
- hedged assets, liabilities and derivatives designated in hedge relationships; and
- financial assets and liabilities designated at fair value through profit or loss.

For trading derivatives, the full change in fair value is recognised inclusive of interest income and expense arising on those derivatives. However, in cases where a trading derivative is economically offsetting movements in the fair value of a financial asset or liability designated at fair value through profit or loss, the interest income and expense attributable to the derivative is recognised within net interest income and not as part of the fair value movement of the trading derivative.

Hedged assets, liabilities and derivatives designated in hedge relationships result in the recognition of fair value movements on both the hedged item and hedging derivative in a fair value hedge relationship, and hedge ineffectiveness for both fair value and cash flow hedge relationships.

Financial assets and liabilities designated at fair value through profit or loss recognise fair value movements (excluding interest) on those items designated as fair value through profit or loss.

Interest income and interest expense on hedged assets and liabilities and financial assets and liabilities designated as fair value through profit or loss are recognised in net interest income.

Income tax

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it is related to items recognised in equity, in which case the tax is also recognised in equity.

Income tax expense or revenue is the tax payable or receivable on the current year's taxable income based on the applicable tax rate adjusted by changes in deferred tax assets and liabilities.

Current tax

Current tax is the expected tax payable or recoverable on the taxable profit or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax

Deferred tax assets and liabilities are recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred tax is determined using tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets are only recognised for temporary differences, unused tax losses and unused tax credits if it is probable that future taxable amounts will arise to utilise those temporary differences and losses.

Deferred tax liabilities are not recognised for temporary differences arising from investments in subsidiaries and associates where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the difference will not reverse in the foreseeable future. Deferred tax assets are not recognised for temporary differences arising from investments in subsidiaries and associates where it is probable that the difference will not reverse in the foreseeable future, and it is not probable that taxable profit will be available against which the temporary difference can be utilised.

The effects of income taxes arising from asset revaluation adjustments are recognised directly in the asset revaluation reserve where relevant.

2. Accounting policies (continued)

Income tax (continued)

Deferred tax (continued)

Deferred tax assets and liabilities related to fair value re-measurement of cash flow hedges, which are charged or credited directly to equity, are also credited or charged directly to equity. The tax associated with these transactions will be recognised in the income statement at the same time as the underlying transaction.

Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition. This includes: cash and liquid assets, amounts due to other banks (to the extent less than 90 days).

Repurchase and reverse repurchase agreements

Securities sold subject to repurchase agreements ("repos") are retained in their respective balance sheet categories. The counterparty liability is included in amounts due to other banks, deposits from banks, other deposits or deposits due to customers, as appropriate based upon the counterparty to the transaction.

Securities purchased under agreements to resell ("reverse repos") are accounted for as collateralised loans. The difference between the sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method. Such amounts are normally classified as deposits with other banks or cash and cash equivalents. Securities lent to counterparties are also retained in the financial statements. Securities borrowed are not recognised in the financial statements unless they are sold to third parties, in which case the purchase and sale are recorded with the gain or loss included in trading income. The obligation to return securities borrowed is recorded at fair value as a trading liability.

Financial instruments

Recognition and derecognition of financial instruments

A financial asset or a financial liability is recognised on the balance sheet when the Bank becomes party to the contractual provisions of the instrument. Loans and receivables are recognised when cash is advanced (or settled) to the borrowers.

The Bank classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, held to maturity investments and available for sale securities. Management determines the classification of its financial assets at initial recognition.

The Bank classifies its financial liabilities in the following categories: financial liabilities at fair value through profit or loss and amortised cost.

The Bank derecognises a financial asset when the contractual cash flows from the asset expires or it transfers the right to receive contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership are transferred.

A financial liability is derecognised from the balance sheet when the Bank has discharged its obligation to the contract, or the contract is cancelled or expires.

Notes to the consolidated financial statements (continued)

2. Accounting policies (continued)

Financial Instruments (continued)

Offsetting financial instruments

A financial asset and a financial liability shall be offset and the net amount presented in the balance sheet if, and only if, the Bank has a legally enforceable right to set off the recognised amounts and it intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Financial instruments designated at fair value through profit or loss

Purchases and sales of financial assets classified within fair value through profit or loss are recognised on trade date, being the date that the Group is committed to purchase or sell a financial asset.

Upon initial recognition, financial assets and liabilities may be designated as held at fair value through profit or loss and are initially recognised at fair value, with transaction costs being recognised in the income statement immediately. Subsequently, they are measured at fair value with gains and losses recognised in the income statement as they arise. Items held at fair value through profit or loss comprise both items held for trading and items specifically designated as fair value through profit or loss at initial recognition.

Restrictions are placed on the use of the designated fair value option and the classification can only be used in the following circumstances:

- if a host contract contains one or more embedded derivatives, the Group may designate the entire contract as being held at fair value;
- designating the instruments will eliminate or significantly reduce measurement or recognition inconsistencies (i.e. eliminate an accounting mismatch) that would otherwise arise from measuring related assets or liabilities on a different basis; or
- assets and liabilities are both managed and their performance is evaluated on a fair value basis in accordance with documented risk management and investment strategies.

Financial assets held for trading

A financial asset is classified as held for trading if it is acquired principally for the purpose of selling in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative not in a qualifying hedge relationship.

Held to maturity financial assets

Held to maturity investments are non-derivative financial assets with fixed or determinable payments that the Group has the intention and ability to hold to maturity. Held to maturity assets are initially recognised at fair value and subsequently recorded at amortised cost using the effective interest method.

2. Accounting policies (continued)

Financial instruments (continued)

Available for sale investments

Available for sale investments are non-derivative financial assets that are designated as available for sale and are not categorised into any of the categories of (i) fair value through profit or loss (ii) loans and receivables or (iii) held to maturity.

Consistent with financial assets classified as fair value through profit or loss the Group applies trade date accounting to purchases and sales of available for sale investments.

Available for sale investments are initially recognised at fair value including direct and incremental transaction costs. They are subsequently held at fair value. Gains and losses arising from changes in fair value are included as a separate component of equity until sale or impairment when the cumulative gain or loss is transferred to the income statement.

Interest income is determined using the effective interest method. Impairment losses and translation differences on monetary items are recognised in the income statement within the year in which they arise. Available for sale investments are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership. Available for sale investments consist primarily of debt securities and an immaterial investment in equity securities.

Financial liabilities

A financial liability is classified as held-for-trading if it is incurred principally for the purpose of selling in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative not in a qualifying hedge relationship.

All other financial liabilities are measured at amortised cost using the effective interest method.

Fair value measurement

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

Where no such active market exists for the particular asset or liability, the Group uses a valuation technique to arrive at the fair value, including the use of transaction prices obtained in recent arm's length transactions where possible, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. In doing so, fair value is estimated using a valuation technique that makes maximum possible use of market inputs and that places minimal possible reliance upon entity-specific inputs.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Group recognises profits or losses on the transaction date.

Notes to the consolidated financial statements (continued)

2. Accounting policies (continued)

Financial instruments (continued)

Fair value measurement (continued)

The carrying value of financial assets at fair value through profit or loss reflects the credit risk attributable to the counterparty. Changes in the credit profile of the counterparty are reflected in the fair value of the asset and recognised in the income statement.

Derivative financial instruments and hedge accounting

All derivatives are recognised on the balance sheet at fair value on trade date and are classified as trading except where they are designated as part of an effective hedge relationship. The carrying value of a derivative is measured at fair value throughout the life of the contract. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

The method of recognising the resulting fair value gain or loss on a derivative depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged. The Group designates certain derivatives as either hedges of the fair value of recognised assets or liabilities or firm commitments (a fair value hedge); or hedges of highly probable future cash flows attributable to a recognised asset or liability, or a highly probable forecast transaction (a cash flow hedge). Hedge accounting is used for derivatives designated in this way providing certain criteria are met.

The Group makes use of derivative instruments to manage exposures to interest rates and foreign currency, including exposures arising from forecast transactions and firm commitments. In order to manage particular risks, the Group applies hedge accounting for transactions which meet the specified criteria.

The Group documents, at the inception of a transaction, the relationship between hedging instruments and the hedged items, and the Group's risk management objective and strategy for undertaking these hedge transactions. The Group documents how effectiveness will be measured throughout the life of the hedge relationship and its assessment, both at hedge inception and on an on-going basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. A hedge is expected to be highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated are expected to offset in a range of 80% to 125%.

Fair value hedge

The carrying value of the hedged item on initial designation is adjusted for the fair value attributable to the hedged risk. Subsequent to initial designation, changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The movement in the fair value of the hedged item attributable to the hedged risk is made as an adjustment to the carrying value of the hedged asset or liability. Where the hedged item is derecognised from the balance sheet, the adjustment to the carrying amount of the asset or liability is immediately transferred to the income statement.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item is amortised to the income statement on an effective yield basis over the remaining period of the original hedge relationship.

Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity, while the gain or loss relating to the ineffective portion is recognised immediately in the income statement. The carrying value of the hedged item is not adjusted.

Amounts accumulated in equity are transferred to the income statement in the year in which the hedged item will affect profit or loss.

2. Accounting policies (continued)

Financial instruments (continued)

Cash flow hedge (continued)

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. This could occur for two reasons:

- the derivative is held for purposes of short-term profit taking; or
- the derivative is held to economically hedge an exposure but does not meet the accounting criteria for hedge accounting.

In both these cases, the derivative is classified as a trading derivative and changes in the value of the derivative are immediately taken to the income statement.

Certain derivatives embedded in financial instruments are treated as separate derivatives when their economic characteristics and risks are not clearly and closely related to those of the host contract and the host contract is not carried at fair value. These embedded derivatives are separately measured at fair value with changes in fair value recognised in the income statement.

Loans and advances

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and which are not classified as available for sale or designated at fair value through profit or loss. They arise when the Group provides money or services directly to a customer with no intention of trading the loan. Loans and advances include overdrafts, credit card lending, market rate advances, bill financing, mortgages, lease finance and term lending.

Loans and advances are initially recognised at fair value including direct and incremental transaction costs. They are subsequently recorded at amortised cost, using the effective interest method, adjusted for impairment losses and unearned income. They are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership.

As noted above, in certain limited circumstances the Group applies the fair value measurement option to financial assets. This option is applied to loans and advances where there is an embedded derivative within the loan contract and the Group has entered into a derivative to offset the risk introduced by the embedded derivative. The loan is designated as being carried at fair value through profit or loss to offset the movements in the fair value of the derivative within the income statement. When this option is applied the asset is included within other financial assets at fair value, and not within loans and advances. When a loan is held at fair value, a statistical-based calculation is used to estimate expected losses attributable to adverse movements in credit risk on the assets held. This adjustment to the credit quality of the asset is then applied to the carrying amount of the loan to arrive at fair value.

2. Accounting policies (continued)

Impairment of financial assets other than fair value loans

The Group assesses at each balance sheet date whether there is evidence that a financial asset or a portfolio of financial assets that is not carried at fair value through profit or loss is impaired. A financial asset or portfolio of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of the asset and prior to the balance sheet date ("a loss event"), and that loss event or events has had an impact on the estimated future cash flows of the financial asset or the portfolio that can be reliably estimated.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

For loans and advances and held to maturity investments, 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.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure and any costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar 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.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist. In addition, the Group uses 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.

The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Following impairment, interest income is recognised using the original effective rate of interest which was used to discount the future cash flows for the purpose of measuring the impairment loss.

When a loan is uncollectible, it is written off against the related provision. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off reduce the amount of the expense in the income statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

2. Accounting policies (continued)

Impairment of financial assets other than fair value loans (continued)

If the originally contracted terms of loans and advances are amended, the amounts are classified as restructured and may also be disclosed as forbearance if the customer is experiencing, or is about to experience, difficulties in meeting their financial commitments to the Group. Such accounts accrue interest as long as the loan performs in accordance with the restructured terms.

Equity and debt instruments – classed as available for sale

In the case of equity instruments classified as available for sale, the Group seeks evidence of a significant or prolonged decline in the fair value of the security below its cost to determine whether impairment exists. Where such evidence exists, the cumulative net loss that has been previously recognised directly in equity is removed from equity and recognised in the income statement.

Reversals of impairment of equity shares classified as available for sale are not recognised in the income statement. Increases in the fair value of equity shares classified as available for sale after impairment are recognised directly in equity.

In the case of debt instruments classified as available for sale, impairment is assessed based on the same criteria as all other financial assets. Where evidence of impairment exists, the net loss that has been previously recognised directly in equity is recognised in the income statement. Reversals of impairment of debt securities classified as available for sale are recognised in the income statement.

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether:

- fulfilment of the arrangement is dependent on the use of a specific asset or assets; and
- the arrangement conveys a right to use the asset.

As lessee

The leases entered into by the Group as lessee are primarily operating leases. Operating lease rentals are charged to the income statement on a straight-line basis over the period of the lease.

When an operating lease is terminated before the end of the lease period, any payment made to the lessor by way of penalty is recognised as an expense in the period of termination.

Sale and leaseback transactions entered into by the Group as lessee are primarily operating leases. Where an operating lease is established at fair value, any excess of sales proceeds over the carrying amount is recognised immediately in the income statement.

As lessor

Leases entered into by the Group as lessor, where the Group transfers substantially all the risks and rewards of ownership to the lessee, are classified as finance leases. The net investment in the lease, which is comprised of the present value of the lease payments including any guaranteed residual value and initial direct costs, is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is unearned income. Income is recognised over the term of the lease using the net investment method (before tax) reflecting a constant periodic rate of return.

Assets under operating leases are included within property, plant and equipment at cost and depreciated over the useful life of the lease after taking into account anticipated residual values. Operating lease rental income is recognised within other operating income in the income statement on a straight line basis over the life of the lease. Depreciation is recognised within depreciation expense in the income statement consistent with the nature of the asset (refer to note 18, Property plant and equipment).

2. Accounting policies (continued)

Property, plant and equipment

All freehold and long-term leasehold land and buildings are revalued annually on an open market basis by the Directors to reflect current market values, based on advice received from independent valuers. In addition, full independent valuations are carried out on a three year cycle on an open market basis, including directly attributable acquisition costs but without deducting expected selling costs. For properties that are vacant, valuations are carried out on an open market basis. Revaluation increments are credited to the asset revaluation reserve, unless these reverse deficits on revaluations charged to the income statement in prior years. To the extent that they reverse previous revaluation gains, revaluation losses are charged against the asset revaluation reserve. This policy is applied to assets individually. Revaluation increases and decreases are not offset, even within a class of assets, unless they relate to the same asset.

All other items of property, plant and equipment are carried at cost, less accumulated depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to acquisition.

Property, plant and equipment carrying amounts are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of (i) the asset's fair value less costs to sell and (ii) the asset's value in use.

Where a group of assets working together supports the generation of cash inflows largely independent of cash inflows from other assets or groups of assets, the recoverable amount is assessed in relation to that group of assets (a cash-generating unit).

With the exception of freehold land, all items of property, plant and equipment are depreciated or amortised using the straight-line method, at rates appropriate to their estimated useful life to the Group. For major classes of property, plant and equipment, the annual rates of depreciation or amortisation are:

- buildings - 2%;
- leases (leasehold improvements) - the lower of the expected lease term and the assets useful life; and
- motor vehicles, fixtures and equipment - 10% to 33.33%.

Assets residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

Gains or losses on the disposal of property, plant and equipment, which are determined as the difference between the net sale proceeds and the carrying amount at the time of sale, are included in the income statement.

Any realised amounts in the asset revaluation reserve are transferred directly to retained earnings.

Investments in controlled entities and associates

The Group's investments in controlled entities and associates are valued at cost or valuation less any provision for impairment. Such investments are reviewed annually for impairment, or more frequently when there are indications that impairment may have occurred. Losses relating to impairment in the value of shares in controlled entities and associates are recognised in the income statement.

2. Accounting policies (continued)

Investment properties

Investment property is property (land or building, or part of a building, or both) held by the owner or by the lessee under a finance lease to earn rentals or for capital appreciation or both, rather than for:

- use in the production or supply of goods or services or for administrative purposes; or
- sale in the ordinary course of business.

Investment property assets are carried at fair value, with fair value increments and decrements taken to the income statement in the period in which they arise. Investment property assets are revalued annually by Directors to reflect fair values. Directors' valuations are based on advice received from independent valuers. Such valuations are performed on an open market basis being the amounts for which the assets could be exchanged between a knowledgeable willing buyer and a knowledgeable willing seller in an arm's length transaction at the valuation date. Newly acquired investment property assets are held at cost (i.e. equivalent to fair value due to their recent acquisition) until the time of the next annual review, a period not exceeding twelve months.

Property inventory

Property acquired or being constructed for sale in the ordinary course of business, rather than to be held for rental or capital appreciation, is held as inventory and is measured at the lower of cost and net realisable value.

Provisions

Provisions are recognised when a legal or constructive obligation exists as a result of past events, it is probable that an outflow of economic benefits will be necessary to settle the obligation, and the obligation can be reliably estimated. Provisions are not discounted to the present value of their expected net future cash flows except where the time value of money is considered material.

Pension and post retirement costs

Employees of the Group are entitled to benefits on retirement, disability or death from the Group's pension plans. The Group operates both defined benefit and defined contribution pension schemes.

Defined contribution pension scheme

The defined contribution scheme receives fixed contributions from Group companies and the Group's obligation for contributions to these plans is recognised as an expense in the income statement as incurred. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payment is available.

Defined benefit pension scheme

The defined benefit scheme provides defined benefits based on years of service and career averaged revalued earnings. A liability or asset in respect of the defined benefit scheme is recognised in the balance sheet and is measured as the present value of the defined benefit obligation less the fair value of the defined benefit scheme assets at the reporting date. The present value of the defined benefit obligation for the scheme is discounted by high quality corporate bond rates that have maturity dates approximating to the terms of the Group's defined benefit obligation.

Pension expense attributable to the Group's defined benefit scheme comprises current service cost, net interest on the net defined benefit obligation/(asset), past service cost resulting from a scheme amendment or curtailment, gains or losses on settlement and administrative costs incurred. The Group's policy where actuarial remeasurements arise is to fully recognise such amounts directly in retained earnings through the statement of comprehensive income, in the period in which they occur. Actuarial remeasurements arise from experience adjustments (the effects of differences between previous actuarial assumptions and what has actually occurred) and changes in actuarial assumptions.

The Group also provides post-retirement health care for certain retired employees. The calculation of the post-retirement health care liability is calculated in the same manner as the defined benefit pension obligation.

2. Accounting policies (continued)

Subordinated liability and related entity balances

Subordinated liabilities and related entity balances, other than derivatives, are recorded at amortised cost. Subordinated liabilities comprise undated and dated loan capital which is provided to the Bank by NAGE and NAB. Subordinated liabilities are included within amounts due to related entities on the balance sheet.

Debt issues

Debt issues are short and long term debt issued by the Group including commercial paper, notes, term loans, medium term notes and residential mortgage backed securities. Debt issues are typically recorded at amortised cost using the effective interest method. Premiums, discounts and associated issue expenses are recognised using the effective interest method through the income statement from the date of issue to accrete the carrying value of securities to redemption values by maturity date. Interest is charged to the income statement using the effective interest method.

Financial guarantees

The Group provides guarantees in the normal course of business on behalf of its customers. Guarantees written are conditional commitments issued by the Group to guarantee the performance of a customer to a third party. Guarantees are primarily issued to support direct financial obligations such as commercial bills or other debt instruments issued by a counterparty. It is the rating of the Group as a guarantee provider that enhances the marketability of the paper issued by the counterparty in these circumstances.

The financial guarantee contract is initially recorded at fair value which is equal to the premium received, unless there is evidence to the contrary. Subsequently, the Group records and measures the financial guarantee contract at the higher of:

- where it is likely the Group will incur a loss as a result of issuing the contract, a liability is recognised for the estimated amount of the loss payable; and
- the amount initially recognised less, when appropriate, amortisation of the fee which is recognised over the life of the guarantee.

Contingent liabilities

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefits is uncertain or cannot be reliably measured. Contingent liabilities are not recognised in the balance sheet but are disclosed unless they are remote.

Equity

Share option reserve

The share option reserve records the outstanding balance payable to NAB for equity benefits provided to employees and Directors as part of their remuneration including deferred tax.

Cash flow hedge reserve

The cash flow hedge reserve records the effective portion of the fair value revaluation of derivatives designated as cash flow hedging instruments.

2. Accounting policies (continued)

Preference shares

Preference shares are classified as an equity instrument if and only if the instrument includes no contractual obligation to:

- deliver cash or another financial asset to another entity; or
- exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the issuer.

Where preference shares do not satisfy the above conditions, they are classified as a financial liability. The Company's preference shares which were redeemed on 13 December 2013 met the criteria for classification as equity.

Dividends on ordinary and preference shares

Dividends on ordinary and preference shares classified as equity instruments are recognised as a liability and deducted from equity when they are approved by the Bank's Directors. Interim dividends are deducted from equity when they are declared and no longer at the discretion of the Bank.

Dividends for the year that are approved after the balance sheet date are disclosed as an event after the balance sheet date.

Equity based compensation

The Group engages in share-based payment transactions in respect of services received from certain of its employees and to provide long term incentives. The fair value of the services received is measured by reference to the fair value of the NAB shares or share options granted on the date of the grant. This is recognised as an expense in the income statement over the relevant vesting period and results in an increase in the share option reserve which is reduced on repayment to the ultimate parent company.

The grant date fair value of shares is generally determined by reference to the weighted average price of the NAB shares in the week up to, and including, the date on which the shares are granted. Employee share plans are linked to internal performance, market performance and/or service conditions. The fair value of shares with a market performance condition is determined using a Monte Carlo simulation. The grant date fair value of the performance options and performance rights is determined using a simulated version of the Black-Scholes model. The key assumptions and inputs used in the valuation model are the exercise price of the performance options or performance rights, the expected volatility of the share price, the risk-free interest rate and the expected dividend yield on the shares for the life of the performance options and performance rights. The simulation takes into account both the probability of achieving market performance conditions and the potential for early exercise of vested performance options or performance rights.

While market performance conditions are incorporated into the grant date fair values, non-market conditions are not taken into account when determining the fair value and expected time to vesting of shares, performance options and performance rights. Instead, non-market conditions are taken into account by adjusting the number of shares, performance options and performance rights included in the measurement of the expense so that the amount recognised in the income statement reflects the number of shares, performance options or performance rights that actually vest.

2. Accounting policies (continued)

Securitisation

Through its loan securitisation programme, the Group packages and sells loans (principally housing mortgage loans) as securities to investors through a securitisation vehicle. All such financial instruments continue to be held on the Group balance sheet, and a liability recognised for the proceeds of the funding transaction as the Group retains substantially all the risks and rewards.

3. Critical accounting estimates and judgements

The preparation of financial statements requires the use of certain critical accounting estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosed amount of contingent liabilities. Assumptions made at each balance sheet date are based on best estimates at that date. Although the Group has internal control systems in place to ensure that estimates can be reliably measured, actual amounts may differ from those estimates. The most significant use of judgements and estimates are as follows:

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the balance sheet cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data is not available, judgement is required to establish fair values. The judgements include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions for asset backed securities.

The most significant judgement is in relation to the Group's fair value loan portfolio. The significant inputs impacting the carrying value of the loans other than interest rates are future expectations of credit losses and the expected repayment profile of the loans. Sensitivity analysis indicating the impact of reasonable possible changes in these inputs on the fair value is included within note 37.

The valuation of these financial instruments is described in more detail in note 13.

Impairment losses on loans and advances

The Group reviews its individually significant loans and advances at each balance sheet date to assess whether an impairment loss should be recorded in the income statement. In particular, judgement by management is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. In estimating these cash flows, the Group makes judgements about the borrower's financial situation and the net realisable value of collateral. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the impairment allowance.

3. Critical accounting estimates and judgements (continued)

Loans and advances that have been assessed individually and found not to be impaired and all not individually significant loans and advances are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence but whose effects are not yet evident. The collective assessment takes account of data from the loan portfolio (such as credit quality, levels of arrears, credit utilisation, loan to collateral ratios etc.), concentrations of risk and economic data (including levels of unemployment, real estate price indices, country risk and the performance of different individual groups). To the extent that the probabilities of default improves from those presently used within the Group's provisioning models by 5% the impairment provision on loans and advances would decrease by £4m. Alternatively, if probabilities of default deteriorate by 5%, the impairment provision on loans and advances would increase by £4m. To the extent that recovery rates improve from those presently used within each of the Group's provisioning models by 5%, the impairment provision on loans and advances would decrease by £12m. Alternatively, if recovery rates deteriorate by 5%, the impairment provision on loans and advances would increase by £20m. There are interactions between the various assumptions within the provisioning models, which mean that no single factor is likely to move independent of others; however, the sensitivities disclosed above assume all other assumptions remain unchanged.

The impairment loss on loans and advances is disclosed in more detail in note 16.

Payment Protection Insurance redress provision and other conduct related matters

Disclosures in relation to the Group's payment protection insurance redress provision can be found in note 26 with the Group holding a provision of £515m at 30 September 2014 (2013: £152m). Significant judgement by management is required in determining the key assumptions used to estimate the quantum of the provision, including the level of complaint volumes, uphold rates (how many claims are, or may be, upheld in the customer's favour) and redress costs (the average payment made to customers). The provision is therefore subject to inherent uncertainties as a result of the subjective nature of the assumptions used in quantifying the overall estimated position at 30 September 2014. Consequently, the provision calculated may be subject to change in future years as a result of the emergence of new trends in relation to the judgements and assumptions which differ to those currently used. Sensitivity analysis indicating the impact of reasonable possible changes in key assumptions on the PPI provision is included within note 26.

There are similar uncertainties and judgements for other conduct risk related matters disclosed in note 26 however the level of liability for each matter is lower.

Retirement benefit obligations

The cost of the defined benefit pension plan is determined using an actuarial valuation. The actuarial valuation involves making assumptions about discount rates, future salary increases, mortality rates and future pension increases. Due to the long-term nature of these plans, such estimates are subject to significant uncertainty. Further details on the assumptions used are provided in note 28.

4. Segment information

The Group's operating segments are operating units engaged in providing different products or services and whose operating results are regularly reviewed by the entity's Chief Operating Decision Maker, the Chief Executive Officer.

The Group's business is organised into two principal operating segments: Business & Private Banking (including Business Banking centres, small business and private banking customers) and Retail Banking. Business & Private Banking provides a range of banking products and services to segments of business and private customers, including loans and finance, day to day banking, wealth management, international services and treasury solutions. Retail Banking provides a range of banking products and services to personal customers, including current accounts, mortgages, overdrafts, personal loans, savings accounts, insurances and financial planning.

The Group's Central Functions are Customer Trust & Confidence, Finance, Risk, Operations & IT, Legal & Governance, CEO Office Support, Customer Experience & Marketing, Strategy & Transformation, Treasury and People & Communications, together with other functions which are not considered to be separate reportable operating segments.

Notes to the consolidated financial statements (continued)

4. Segment information (continued)

UK Banking is the NAB Group's UK management reporting entity. It comprises Business & Private Banking, Retail Banking and Central Functions, along with the UK-based wealth management business of the NAB Group. Historically it also included certain elements of the mid-corporate lending on the NAB Group Wholesale Banking balance sheet.

The reconciliation from UK Banking to statutory results table on page 57 shows other segments and adjustments, which are deductions for the wealth management business which are not part of Clydesdale Bank PLC. Also included are adjustments to incorporate Wholesale Banking business written on the Clydesdale Bank PLC balance sheet not included within UK Banking.

Further details of the NAB Group's operating segments including UK Banking and how they are evaluated are contained within note 2 of NAB Group's annual report and consolidated financial statements for the year ended 30 September 2014. The segment information in the tables on page 57 has been prepared on the same basis. The accounting policies of the operating segments are consistent with those described in note 2 to the NAB Group financial statements for the year ended 30 September 2014.

Major customers

Revenues from no one single customer amount to greater than 10% of the Group's revenues.

Geographical areas

The Group has no material operations outside the UK and therefore no secondary geographical area information is presented. Further information on the Group's geographical locations can be found in the other information section at the end of these annual report and consolidated financial statements.

4. Segment information (continued)

Operating segments 2014	**Business & Private £m**	**Retail £m**	**Central and other functions £m**	**UK Banking £m**
Net interest income	308	453	(2)	759
Other operating income	75	105	30	210
Operating income	383	558	28	969
Operating and administrative expenses	(80)	(138)	(468)	(686)
Impairment losses on credit exposures	(58)	(26)	4	(80)
Segment operating profit/(loss)	245	394	(436)	203
Tax (expense)/credit	(54)	(87)	96	(45)
Segment cash earnings after tax	**191**	**307**	**(340)**	**158**
Average assets	**10,486**	**15,621**	**10,945**	**37,052**

Operating segments 2013	Business & Private £m	Retail £m	Central and other functions £m As restated	UK Banking £m As restated
Net interest income	335	410	6	751
Other operating income	85	123	27	235
Operating income	420	533	33	986
Operating and administrative expenses	(90)	(134)	(498)	(722)
Impairment losses on credit exposures	(123)	(38)	3	(158)
Segment operating profit/(loss)	207	361	(462)	106
Tax (expense)/credit	(49)	(84)	106	(27)
Segment cash earnings after tax	158	277	(356)	79
Average assets	12,796	14,020	11,320	38,136

Comparative disclosures have been amended to conform with current year presentation.

Reconciliation between segment and statutory results 2014	**UK Banking £m**	**Non-cash earnings items £m**	**Other segments and adjustments £m**	**Clydesdale Bank PLC £m**
Net interest income	759	-	12	771
Other operating income	210	-	(18)	192
Operating income	969	-	(6)	963
Operating and administrative expenses	(686)	-	(419)	(1,105)
Impairment losses on credit exposures	(80)	-	6	(74)
Operating profit/(loss)	203	-	(419)	(216)
Tax (expense)/credit	(45)	-	83	38
	158	-	(336)	(178)
Items outside of UK Banking cash earnings after tax:				
Payment Protection Insurance redress	(336)	-	336	-
Loss after tax	**(178)**	**-**	**-**	**(178)**
Average assets	**37,052**	**-**	**(504)**	**36,548**

4. Segment information (continued)

Reconciliation between segment and statutory results 2013	UK Banking £m As restated	Non-cash earnings items £m As restated	Other segments and adjustments £m As restated	Clydesdale Bank PLC £m As restated
Net interest income	751	-	5	756
Other operating income	235	(23)	(28)	184
Operating income	986	(23)	(23)	940
Operating and administrative expenses	(722)	-	(128)	(850)
Impairment losses on credit exposures	(158)	-	14	(144)
Operating profit/(loss)	106	(23)	(137)	(54)
Tax (expense)/credit	(27)	4	33	10
	79	(19)	(104)	(44)
Items outside of UK Banking cash earnings after tax:				
Fair value and hedge ineffectiveness	(19)	19	-	-
Payment Protection Insurance redress	(104)	-	104	-
Loss after tax	(44)	-	-	(44)
Average assets	38,136	-	(398)	37,738

5. Net interest income

	2014 £m	2013 £m
Interest income and similar income		
Loans and advances to other banks	25	31
Available for sale investments	8	8
Loans and advances to customers	1,052	1,100
Due from related entities (note 11)	4	5
Other interest income	1	1
	1,090	1,145
Financial assets at fair value through profit or loss	45	64
Total interest income and similar income	1,135	1,209
Less: Interest expense and similar charges		
Due to other banks	5	2
Financial liabilities at fair value through profit or loss	1	2
Due to customers	212	305
Bonds and notes	81	75
Due to related entities (note 11)	51	57
Other interest expense [1]	14	12
Total interest expense and similar charges	364	453
Net interest income	771	756

[1] Other interest expense includes the FSCS levy.

6. Non-interest income

	2014 £m	2013 £m As restated
Gains less losses on financial instruments at fair value		
Interest rate derivatives	**47**	147
Margin on foreign exchange derivative brokerage	**19**	21
Other assets and liabilities at fair value	**(64)**	(171)
Ineffectiveness arising from fair value hedges (note 14)	**7**	(8)
Ineffectiveness arising from cash flow hedges (note 14)	**2**	(3)
	11	(14)
Other operating income		
Fees and commission	**172**	193
Gain on disposal of tangible fixed assets [1]	**7**	1
Other income	**2**	4
	181	198
Total non-interest income	**192**	184

[1] Tangible fixed assets include property, plant and equipment, investment properties and property inventory.

The movement in fair value of assets incorporates valuation movements for certain financial assets which are designated at inception as fair value through profit or loss. These assets are predominantly fixed interest rate loans which are measured at fair value. The movements in fair value are taken through the income statement as part of non-interest income. The fair value of these loans is derived from the future loan cash flows using appropriate discount rates and includes adjustments for credit risk and credit losses. In general, as interest rates fall, the carrying value of the loan portfolio increases. Similarly, as interest rates increase, the carrying value of the loan portfolio decreases. The valuation technique used is reflective of current market practice.

Notes to the consolidated financial statements (continued)

7. Operating and administrative expenses

	2014 £m	2013 £m As restated
Personnel expenses		
Salaries, wages and non-cash benefits	149	153
Related personnel expenses	13	13
Defined contribution pension expense	8	8
Defined benefit pension expense	28	39
Equity-based compensation	7	4
Other personnel expenses	11	7
	216	224
Depreciation expense		
Depreciation of property, plant and equipment (note 18)	19	19
Other operating and administrative expenses		
Operating lease rental	31	32
Other occupancy charges	39	42
Related entity recharges (note 11)	262	249
Payment Protection Insurance redress (note 26)	420	130
Other operating and administrative expenses	118	154
	870	607
Total operating and administrative expenses	1,105	850

Auditors' remuneration

Included within other operating and administrative expenses:	2014 £'000	2013 £'000
Audit of the financial statements	1,231	1,303
Other fees to auditors:		
Audit of the Group pension scheme	58	58
Local statutory audits for subsidiaries	91	220
Other assurance including regulatory compliance based work	141	141
	1,521	1,722

8. Taxation

	2014 £m	2013 £m As restated
Current tax		
UK corporation tax		
Current year	7	(4)
Adjustment in respect of prior years	4	(5)
	11	(9)
Deferred tax (note 22)		
Current year	(44)	(3)
Adjustment in respect of prior years	(5)	2
	(49)	(1)
Tax credit	(38)	(10)

The tax assessed for the year differs from the standard rate of corporation tax in the UK (22%). A reconciliation from the expense implied by the standard rate to the actual tax expense is as follows:

	2014 £m	2013 £m As restated
Loss on ordinary activities before tax	(216)	(54)
Tax credit based on the standard rate of Corporation Tax in the UK of 22% (2013: 23.5%)	(47)	(13)
Effects of:		
Expenses not deductible for tax purposes	3	4
Chargeable gains	3	-
Rate differences	4	2
Adjustments in respect of prior years	(1)	(3)
Tax credit	(38)	(10)

9. Dividends paid

	2014 £m	2013 £m
Preference dividends paid – 12% per annum payable semi-annually (2014: 6p per share; 2013: 10p per share)	6	10
Preference dividends paid – 6 month LIBOR plus a margin of 779bps per annum payable semi-annually (2014: 4p per share; 2013: 7p per share)	8	14
	14	24

10. Cash and balances with central banks

	Group		Bank	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Cash assets	**1,302**	1,207	**1,302**	1,207
Balances with central banks (including EU payment systems)	**4,669**	5,508	**4,669**	5,508
	5,971	6,715	**5,971**	6,715
Less mandatory deposits with central banks [1]	**(42)**	(43)	**(42)**	(43)
Included in cash and cash equivalents (note 33)	**5,929**	6,672	**5,929**	6,672

[1] Mandatory deposits are not available for use in the Group or Bank's day to day business and are non-interest bearing.

11. Related party transactions

During the year there have been transactions between the Group, its ultimate parent, controlled entities of the ultimate parent, controlled entities of the Group, and other related parties.

The Group provides a range of services to related parties, including the provision of banking facilities and standby financing arrangements. Other dealings include granting loans and accepting deposits, and the provision of finance, forward foreign exchange and interest cover.

The Group receives a range of services from the parent and related parties, including loans and deposits, forward exchange and interest rate cover and various administrative services.

Amounts due from related entities	Group		Bank	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Loans				
Ultimate parent	**1,104**	1,278	**347**	437
Controlled entities of the ultimate parent	**8**	21	**8**	21
Controlled entities of the Bank	**-**	-	**1,441**	4,533
	1,112	1,299	**1,796**	4,991
Other receivables				
Ultimate parent	**367**	96	**383**	125
Controlled entities of the ultimate parent	**16**	22	**831**	863
	383	118	**1,214**	988
Total amounts due from related entities	**1,495**	1,417	**3,010**	5,979
Interest income on the above amounts was as follows:				
Ultimate parent (note 5)	**4**	5	**4**	5
Controlled entities of the Bank	**-**	-	**56**	148
	4	5	**60**	153

11. Related party transactions (continued)

Amounts due to related entities	Group 2014 £m	Group 2013 £m	Bank 2014 £m	Bank 2013 £m
Deposits				
Ultimate parent	**897**	1,275	**897**	875
Controlled entities of the Bank	**9**	-	**29**	25
	906	1,275	**926**	900
Bonds and notes				
Ultimate parent	**410**	441	**-**	-
Subordinated liabilities				
Ultimate parent	**555**	550	**555**	550
Controlled entities of the ultimate parent	**526**	526	**526**	526
	1,081	1,076	**1,081**	1,076
Other payables				
Ultimate parent	**38**	21	**54**	11
Controlled entities of the ultimate parent	**17**	47	**16**	47
Controlled entities of the Bank	**-**	-	**4,388**	4,897
	55	68	**4,458**	4,955
Total amounts due to related entities	**2,452**	2,860	**6,465**	6,931
Interest expense on the above amounts was as follows (note 5):				
Ultimate parent	**41**	47	**41**	47
Controlled entities of the ultimate parent	**10**	10	**10**	10
Controlled entities of the Bank	**-**	-	**127**	77
	51	57	**178**	134

Repurchase agreements

Included in amounts due to related entities is £Nil (2013: £51m) for securities sold subject to repurchase agreements. The fair value of the securities sold under these terms as at 30 September 2014 amounts to £Nil (2013: £51m).

Derivatives

The following derivative positions are held with the ultimate parent:

	Group 2014 £m	Group 2013 £m	Bank 2014 £m	Bank 2013 £m
Derivative financial assets				
Designated as hedging instruments (note 14)	**13**	7	**13**	7
Designated as held for trading (note 14)	**75**	95	**75**	95
	88	102	**88**	102
Derivative financial liabilities				
Designated as hedging instrument (note 14)	**245**	204	**148**	119
Designated as held for trading (note 14)	**278**	412	**278**	412
	523	616	**426**	531

Subordinated liabilities

Subordinated liabilities comprise undated and dated loan capital which is provided to the Bank by NAGE and NAB. Interest on the loans is payable at rates related to the London Interbank Offered Rate ("LIBOR"). The undated loans are subject to five years and one day's notice of redemption by the lenders and are repayable at par. Early repayment is at the option of the borrower, subject to the prior consent of the PRA. The loans are subordinated to the claims of other creditors and are unsecured. The loans are employed in the general business of the Bank.

Notes to the consolidated financial statements (continued)

11. Related party transactions (continued)

Subordinated liabilities (continued)

Details of subordinated liabilities in excess of 10% of the total balance of the subordinated loans are disclosed below.

Group and Bank

The rates of interest stated below apply at 30 September 2014:	**2014 £m**	2013 £m
10 year, non-call with a final maturity of 20 December 2023 - LIBOR +3.41%	**300**	300
10 year, non-call with a final maturity of 25 January 2021 - LIBOR + 4.42%	**250**	250
	550	550
Other subordinated notes	**531**	526
Total subordinated liabilities	**1,081**	1,076

Securitisation

The Group has securitised part of its residential mortgage portfolio and the cash raised from the issue of residential mortgage backed securities ("RMBS") through structured entities forms part of the Group's medium term funding. A portfolio of buy to let mortgages has been securitised through the Lannraig Master Trust Issuer programme and a total of £410m (2013: £441m) of the securities issued are held by the Group's ultimate parent.

Other transactions with related entities

	Group		Bank	
	2014 £m	2013 £m	**2014 £m**	2013 £m
Non-interest income received				
Controlled entities of the ultimate parent	**6**	7	**6**	7
Administrative expenses (note 7)				
Ultimate parent	**5**	(8)	**5**	(8)
Controlled entities of the ultimate parent	**257**	257	**257**	248
	262	249	**262**	240

Offset within Administrative expenses paid to the ultimate parent are amounts received by the Group in relation to expenses incurred in the provision of services to the NAB UK Commercial Real Estate ("CRE") portfolio.

Compensation of key management personnel ("KMP")

For the purposes of IAS 24 Related Party Disclosures, KMP's comprise Directors of the Bank, members of the UK Executive Committee and PRA approved persons with a control function of 1 to 29.

Group	**2014 £m**	2013 £m
Salaries and other short-term benefits	**10**	10
Share based payments	**2**	-
	12	10

Directors' emoluments are analysed in note 36.

Notes to the consolidated financial statements (continued)

11. Related party transactions (continued)

Transactions with key management personnel

KMPs, their close family members and any entities controlled or significantly influenced by the KMPs have undertaken the following transactions with the Group in the normal course of business. The transactions were made on the same terms and conditions as applicable to other Group employees, or on normal commercial terms.

Group	2014 £m	2013 £m
Loans and advances	1	2
Deposits	-	1

No provisions have been recognised in respect of loans provided to KMPs (2013: £Nil). There were no debts written off or forgiven during the year to 30 September 2014 (2013: £Nil). Included in the above are twelve (2013: six) loans totalling £0.1m (2013: £0.9m) made to Directors.

Other related party transactions

The Group incurred costs in relation to pension scheme administration. These costs, which amounted to £0.5m in the year ended 30 September 2014 (2013: £0.3m) were charged to the Group sponsored Scheme. The Group has deposits of £3.4m (2013: £4.5m) at the year end placed by the Scheme at market rates.

Pension contributions of £252m (2013: £134m) were made during the year to the Yorkshire and Clydesdale Bank Pension Scheme sponsored by the Bank (note 28).

12. Investments

	Group		Bank	
	2014 £m	2013 £m	2014 £m	2013 £m
Available for sale – listed	1,161	968	1,161	968
Available for sale – unlisted	7	7	7	7
	1,168	975	1,168	975
Held to maturity – listed	-	-	993	924
Held to maturity – unlisted	-	-	490	491
	-	-	1,483	1,415
	1,168	975	2,651	2,390

Included in the available for sale ("AFS") listed securities are £1.1bn (2013: £0.9bn) in UK Government Gilts and £0.1bn (2013: £0.1bn) of other banks' debt securities.

12. Investments (continued)

The listed AFS investments are classified as Level 1 in the fair value hierarchy, with the unlisted AFS investments classified as Level 3 (see note 37).

Credit quality of investments	Group		Bank	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Available for sale				
Senior investment grade	**1,161**	968	**1,161**	968
Other	**7**	7	**7**	7
	1,168	975	**1,168**	975
Held to maturity				
Investment grade	**-**	-	**854**	862
Sub investment grade	**-**	-	**629**	553
	-	-	**1,483**	1,415

13. Other financial assets and liabilities at fair value

	Group		Bank	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Other financial assets at fair value through profit or loss				
Loans and advances	**1,583**	2,171	**1,583**	2,171
Other financial liabilities at fair value through profit or loss				
Due to customers – term deposits	**91**	123	**91**	123

Derivatives which did not meet the requirements for hedge accounting and that are related to loans held at fair value through profit or loss are accounted for as held for trading derivative financial instruments (note 14).

Loans and advances

Included in other financial assets at fair value is a portfolio of loans. Interest rate risk associated with these loans is managed using interest rate derivative contracts and the loans are recorded at fair value to avoid an accounting mismatch. The maximum credit exposure of the loans is £1,583m (2013: £2,171m). The cumulative loss in the fair value of the loans attributable to changes in credit risk amounts to £74m (2013: £77m) and the change for the current year is a gain of £3m (2013: gain of £5m).

The Group ceased further sales of this suite of loan products with effect from 30 April 2012.

Due to customers - term deposits

Included in other financial liabilities at fair value are fixed rate deposits which have been hedged with interest rate derivative contracts with matching cash flows.

The change in fair value attributable to changes in the Bank credit risk is £Nil (2013: £Nil). The Bank is contractually obligated to pay £8m (2013: £10m) less than the carrying amount at maturity to the deposit holder.

14. Derivative financial instruments

The Group uses derivatives for risk mitigation purposes and does not have a trading book. However, certain derivatives do not meet the hedging criteria within IAS 39 and are therefore accounted for as held for trading, although they are used for risk mitigation purposes. The tables below analyse derivatives between those held as hedging instruments and those that do not meet the hedging criteria within IAS 39.

	Group		Bank	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Fair value of derivative financial assets				
Designated as hedging instruments – related entities (note 11)	**13**	7	**13**	7
Designated as held for trading	**132**	142	**132**	142
Designated as held for trading – related entities (note 11)	**75**	95	**75**	95
	220	244	**220**	244
Fair value of derivative financial liabilities				
Designated as hedging instruments – related entities (note 11)	**245**	204	**148**	119
Designated as held for trading	**25**	35	**25**	35
Designated as held for trading – related entities (note 11)	**278**	412	**278**	412
	548	651	**451**	566

The derivative financial instruments held by the Group are further analysed below with the notional contract amount being the amount from which the cash flows from the derivative contracts are derived and is not an indication of the amounts at risk relating to these contracts.

Group **Total derivative contracts as at 30 September 2014**	**Notional contract amount**	**Fair value of assets**	**Fair value of liabilities**
Derivatives designated as hedging instruments	**£m**	**£m**	**£m**
Cash flow hedges			
Interest rate swaps	**29,355**	**13**	**86**
Cross currency swaps	**251**	**-**	**18**
	29,606	**13**	**104**
Fair value hedges			
Interest rate swaps	**1,458**	**-**	**91**
Cross currency swaps	**982**	**-**	**50**
	2,440	**-**	**141**
Derivatives designated as held for trading			
Foreign exchange rate related contracts			
Spot, forward and futures contracts	**2,423**	**55**	**40**
Cross currency swaps	**457**	**38**	**3**
Options	**520**	**4**	**4**
	3,400	**97**	**47**
Interest rate related contracts			
Swaps	**3,306**	**101**	**236**
Swaptions	**128**	**1**	**1**
Options	**601**	**4**	**15**
	4,035	**106**	**252**
Commodity related contracts	**120**	**4**	**4**
Total derivative contracts	**39,601**	**220**	**548**

14. Derivative financial instruments (continued)

Group Total derivative contracts as at 30 September 2013 Derivatives designated as hedging instruments	Notional contract amount £m	Fair value of assets £m	Fair value of liabilities £m
Cash flow hedges			
Interest rate swaps	21,050	7	49
Fair value hedges			
Interest rate swaps	1,458	-	127
Cross currency swaps	1,194	-	28
	2,652	-	155
Derivatives designated as held for trading			
Foreign exchange rate related contracts			
Spot, forward and futures contracts	3,983	38	54
Cross currency swaps	460	50	2
Options	666	6	6
	5,109	94	62
Interest rate related contracts			
Swaps	20,506	130	357
Swaptions	176	2	2
Options	738	9	24
	21,420	141	383
Commodity related contracts	107	2	2
Total derivative contracts	50,338	244	651

Bank **Total derivative contracts as at 30 September 2014** **Derivatives designated as hedging instruments**	**Notional contract amount £m**	**Fair value of assets £m**	**Fair value of liabilities £m**
Cash flow hedges			
Interest rate swaps	**29,355**	**13**	**86**
Cross currency swaps	**-**	**-**	**-**
	29,355	**13**	**86**
Fair value hedges			
Interest rate swaps	**758**	**-**	**62**
Cross currency swaps	**-**	**-**	**-**
	758	**-**	**62**
Derivatives designated as held for trading			
Foreign exchange rate related contracts			
Spot, forward and futures contracts	**2,423**	**55**	**40**
Cross currency swaps	**457**	**38**	**3**
Options	**520**	**4**	**4**
	3,400	**97**	**47**
Interest rate related contracts			
Swaps	**3,306**	**101**	**236**
Swaptions	**128**	**1**	**1**
Options	**601**	**4**	**15**
	4,035	**106**	**252**
Commodity related contracts	**120**	**4**	**4**
Total derivative contracts	**37,668**	**220**	**451**

14. Derivative financial instruments (continued)

Bank Total derivative contracts as at 30 September 2013 Derivatives designated as hedging instruments	Notional contract amount £m	Fair value of assets £m	Fair value of liabilities £m
Cash flow hedges			
Interest rate swaps	21,050	7	49
Fair value hedges			
Interest rate swaps	758	-	70
Derivatives designated as held for trading			
Foreign exchange rate related contracts			
Spot, forward and futures contracts	3,983	38	54
Cross currency swaps	460	50	2
Options	666	6	6
	5,109	94	62
Interest rate related contracts			
Swaps	20,506	130	357
Swaptions	176	2	2
Options	738	9	24
	21,420	141	383
Commodity related contracts	107	2	2
Total derivative contracts	48,444	244	566

Certain derivative financial assets and liabilities have been booked in consolidated structured entities.

Derivative financial assets and liabilities include those designated as foreign currency hedges for the Group securitisations and interest rate hedges for covered bond programmes. The Group also macro hedges its interest rate exposure using cash flow hedges. The carrying value of the currency liabilities issued through securitisation entities fluctuates as a result of foreign exchange movements. There is a corresponding (and offsetting) movement in the value of the hedging derivatives.

14. Derivative financial instruments (continued)

Cash flow hedged derivatives include vanilla interest rate swaps within macro hedges and one cross currency swap within a structured entity. The Group has the following commitments in the time bands noted:

Nominal values per time period	2014 £m	2013 £m
0 to 6 months	14,305	2,370
6 to 12 months	1,133	925
1 to 2 years	6,165	14,930
2 to 5 years	8,003	2,825
	29,606	21,050

The Group has hedged the following forecast future cash flows, which primarily vary with interest rates. These cash flows are expected to impact the income statement in the following periods, excluding any hedge adjustments that may be applied:

	Forecast receivable cash flows 2014 £m	Forecast payable cash flows 2014 £m	Forecast receivable cash flows 2013 £m	Forecast payable cash flows 2013 £m
within one year	56	68	31	25
between one and two years	71	95	59	19
between two and three years	67	242	29	8
between three and four years	15	23	22	12
between four and five years	2	10	14	15
	211	438	155	79

	2014 £m	2013 £m
Gain/(loss) arising from fair value hedges recognised in income statement (note 6)		
Hedging instrument	14	21
Hedged item attributable to the hedged risk	(7)	(29)
	7	(8)

	2014 £m	2013 £m
Gain/(loss) from cash flow hedges recognised in income due to hedge ineffectiveness (note 6)	2	(3)

15. Loans and advances to customers

	Group		Bank	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Overdrafts	**1,767**	2,024	**1,767**	2,024
Credit cards	**364**	396	**364**	396
Lease finance	**417**	482	**394**	428
Mortgages	**18,444**	16,148	**17,015**	11,674
Other term lending – business	**4,272**	4,427	**4,272**	4,427
Other term lending – retail	**824**	756	**824**	756
Other lending	**33**	32	**33**	32
Gross loans and advances to customers	**26,121**	24,265	**24,669**	19,737
Accrued interest receivable	**79**	65	**74**	50
Unearned income	**(27)**	(44)	**(26)**	(38)
Deferred and unamortised fee income	**(27)**	(37)	**(27)**	(33)
Impairment provisions on credit exposures (note 16)	**(245)**	(289)	**(240)**	(278)
	25,901	23,960	**24,450**	19,438

The Group and Bank have transferred £4,763m and £4,763m respectively (2013: £4,834m and £3,202m) of mortgages through securitisation arrangements that do not qualify for derecognition from the balance sheet (note 17). The mortgages do not qualify for derecognition because the Group and Bank remain exposed to the risks and rewards of ownership on an ongoing basis. Prior to any relevant hedging arrangements the Group and Bank continue to be exposed primarily to the credit risk, liquidity risk and interest rate risk of the mortgages. The Group and Bank are also exposed to the residual rewards of the mortgages as a result of their ability to benefit from the future performance of the mortgages through the receipt of deferred consideration. The carrying amount of the associated liabilities before transactional costs is £2,780m (2013: £2,471m).

Included within Group and Bank loans and advances to customers are £2,007m (2013: £2,751m and £1,660m) of mortgages assigned to a bankruptcy remote structured entity, Clydesdale Covered Bonds No 2 LLP (note 17). These loans provide security for issues of covered bonds made by the Group. These transactions do not qualify for derecognition from the balance sheet. At 30 September 2014 there were £1,063m (2013: £1,041m) and £1,097m (2013: £1,096m) of covered bonds in issue under the covered bond programmes, by the Group and Bank respectively.

The Group also has a portfolio of fair valued business loans and advances (note 13). Combined with the above this is equivalent to total loans and advances of £27,484m (2013: £26,131m).

15. Loans and advances to customers (continued)

Lease finance

The Group and Bank lease a variety of assets to third parties under finance lease arrangements, including vehicles and general plant and machinery. The costs of assets acquired by the Group and Bank during the year for the purpose of letting under finance leases and hire purchase contracts amounted to £2m (2013: £3m) and £269m (2013: £210m) respectively. The total receivables from finance leases for the Group and Bank were £8m and £Nil (2013: £12m and £Nil) respectively. The total receivables from hire purchase contracts in the Group and Bank were £384m and £371m (2013: £437m and £401m).

Finance lease and hire purchase receivables	Group		Bank	
	2014 £m	2013 £m	**2014 £m**	2013 £m
Gross investment in finance lease and hire purchase receivables				
Due within one year	**187**	216	**178**	193
Due within one to five years	**220**	247	**210**	225
Due after more than five years	**10**	19	**6**	10
	417	482	**394**	428
Unearned income	**(25)**	(33)	**(23)**	(27)
Net investment in finance lease and hire purchase receivables	**392**	449	**371**	401

Within the Group and Bank there are specific provisions of £2m and £2m (2013: £3m and £2m) in relation to finance lease and hire purchase receivables, with a collective provision of £Nil and £Nil (2013: £Nil and £Nil) as at 30 September 2014.

Maximum exposure to credit risk

The maximum exposure to credit risk is disclosed in note 38.

15. Loans and advances to customers (continued)

Distribution of loans and advances by credit quality

Group As at 30 September 2014	**Retail overdrafts £m**	**Credit cards £m**	**Lease finance £m**	**Mortgages £m**	**Business lending (1) £m**	**Other retail lending £m**	**Total £m**
Gross loans and advances:							
Neither past due nor impaired	84	349	405	18,045	5,662	713	**25,258**
Past due but not impaired	10	15	6	335	161	17	**544**
Impaired	-	-	6	64	249	-	**319**
	94	**364**	**417**	**18,444**	**6,072**	**730**	**26,121**

Group As at 30 September 2013	Retail overdrafts £m	Credit cards £m	Lease finance £m	Mortgages £m	Business lending (1) £m	Other retail lending £m	Total £m
Gross loans and advances:							
Neither past due nor impaired	110	377	467	15,806	5,987	615	23,362
Past due but not impaired	12	19	6	266	218	19	540
Impaired	-	-	9	76	278	-	363
	122	396	482	16,148	6,483	634	24,265

Bank As at 30 September 2014	**Retail overdrafts £m**	**Credit cards £m**	**Lease finance £m**	**Mortgages £m**	**Business lending (1) £m**	**Other retail lending £m**	**Total £m**
Gross loans and advances:							
Neither past due nor impaired	84	349	389	16,676	5,662	713	**23,873**
Past due but not impaired	10	15	2	286	161	17	**491**
Impaired	-	-	3	53	249	-	**305**
	94	**364**	**394**	**17,015**	**6,072**	**730**	**24,669**

Bank As at 30 September 2013	Retail overdrafts £m	Credit cards £m	Lease finance £m	Mortgages £m	Business lending (1) £m	Other retail lending £m	Total £m
Gross loans and advances:							
Neither past due nor impaired	110	377	425	11,504	5,987	615	19,018
Past due but not impaired	12	19	2	124	218	19	394
Impaired	-	-	1	46	278	-	325
	122	396	428	11,674	6,483	634	19,737

(1) Business lending includes business overdrafts.

Credit quality of loans and advances

The Group has an internally developed credit rating system that uses data drawn from a number of sources to assess the potential risk in lending to the Group's customers. This system assigns an indication of the probability of default for each customer and can be broadly mapped to external agencies rating scales. Impaired assets consist of business lending and secured personal lending where current circumstances indicate that losses of loan principal and/or interest may be incurred.

Notes to the consolidated financial statements (continued)

15. Loans and advances to customers (continued)

Distribution of loans and advances neither past due nor impaired

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed by reference to the Group's standard credit rating system. The credit rating system is supported by a variety of financial analytics, combined with processed market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories and are derived in accordance with the Group's rating policy.

The table below presents the analysis of business lending credit quality of loans and advances that are neither past due nor impaired:

	Group		Bank	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Senior investment grade	**1,244**	1,402	**1,241**	1,393
Investment grade	**1,740**	1,529	**1,735**	1,518
Sub-investment grade	**3,083**	3,523	**3,075**	3,501
	6,067	6,454	**6,051**	6,412

For the business lending analysis, investment grades are determined by the Customer Rating System (eCRS) as defined under the Group's Credit Risk Management policy:

Description	**eCRS**	**PD**
Senior investment grade	1 to 5	0 < 0.11
Investment grade	6 to 11	0.11 < 0.55
Sub-investment grade	12 to 23	0.55 < 99.99

The loan-to-value ratio of retail mortgage lending coupled with the relationship of the debt to customers' income is key to the credit quality of these loans. The table below sets out the indexed loan-to-value analysis of the Group's retail mortgages:

	2014	2013
	%	%
Less than 50%	**27**	24
50% to 75%	**49**	45
76% to 80%	**6**	8
81% to 85%	**5**	6
86% to 90%	**4**	5
91% to 95%	**1**	4
96% to 100%	**1**	2
Greater than 100%	**1**	2
Unknown	**6**	4
	100	100

15. Loans and advances to customers (continued)

Loans and advances which were past due but not impaired

Loans and advances that are past due but are not impaired are classified as such for secured lending where the net current market value of supporting security is sufficient to cover all principal, interest and other amounts (including legal, enforcement, realisation costs etc.) due on the facility. Unsecured retail lending and credit cards are written off when they reach 180 days past due and are not designated as impaired.

The distribution of loans and advances that are past due but not impaired is analysed below:

Group 2014	**Retail overdrafts £m**	**Credit cards £m**	**Lease finance £m**	**Mortgages £m**	**Business lending [1] £m**	**Other retail lending £m**	**Total £m**
1 to 29 days past due	8	7	6	113	93	7	**234**
30 to 59 days past due	1	2	-	76	4	3	**86**
60 to 89 days past due	-	2	-	37	1	2	**42**
Past due 90 days and over	1	4	-	109	63	5	**182**
	10	**15**	**6**	**335**	**161**	**17**	**544**

Group 2013	Retail overdrafts £m	Credit cards £m	Lease finance £m	Mortgages £m	Business lending [1] £m	Other retail lending £m	Total £m
1 to 29 days past due	8	9	4	93	131	8	253
30 to 59 days past due	1	3	1	74	8	3	90
60 to 89 days past due	1	2	-	33	2	2	40
Past due 90 days and over	2	5	1	66	77	6	157
	12	19	6	266	218	19	540

Bank 2014	**Retail overdrafts £m**	**Credit cards £m**	**Lease finance £m**	**Mortgages £m**	**Business lending [1] £m**	**Other retail lending £m**	**Total £m**
1 to 29 days past due	8	7	2	88	93	7	**205**
30 to 59 days past due	1	2	-	72	4	3	**82**
60 to 89 days past due	-	2	-	33	1	2	**38**
Past due 90 days and over	1	4	-	93	63	5	**166**
	10	**15**	**2**	**286**	**161**	**17**	**491**

Bank 2013	Retail overdrafts £m	Credit cards £m	Lease finance £m	Mortgages £m	Business lending [1] £m	Other retail lending £m	Total £m
1 to 29 days past due	8	9	1	40	131	8	197
30 to 59 days past due	1	3	1	36	8	3	52
60 to 89 days past due	1	2	-	16	2	2	23
Past due 90 days and over	2	5	-	32	77	6	122
	12	19	2	124	218	19	394

(1) Business lending includes business overdrafts.

15. Loans and advances to customers (continued)

Loans and advances which were past due but not impaired

During the year, the Group has refined the methodology behind the reporting of 90+ days past due mortgage assets to reflect a number of changes in how the Group assesses the population that should be reported. This includes a redefinition of those accounts that are reported within this category and now includes deceased customer accounts, all expired interest only mortgages which continue to make scheduled interest payments and a broader definition of accounts where revised repayment arrangements are in place. These changes have been applied prospectively by the Group in the above tables and they result in no change to the overall reported mortgage balance within loans and advances to customers. The effect on previous periods, had this refined methodology been in place, would have been to report 90+ days past due mortgage assets of £131m as at 30 September 2013 (originally £66m).

16. Impairment provisions on credit exposures

Group 2014	**Retail overdrafts £m**	**Credit cards £m**	**Lease finance £m**	**Mortgages £m**	**Business lending [1] £m**	**Other retail lending £m**	**Total £m**
Opening balance	10	12	3	31	218	15	**289**
Charge for the year	1	8	2	2	43	18	**74**
Amounts written off	(8)	(14)	(3)	(10)	(82)	(17)	**(134)**
Recoveries of amounts written off in previous years	4	3	-	-	5	4	**16**
Closing balance	**7**	**9**	**2**	**23**	**184**	**20**	**245**
Specific	-	-	2	16	92	-	**110**
Collective	7	9	-	7	92	20	**135**
	7	**9**	**2**	**23**	**184**	**20**	**245**

Group 2013	Retail overdrafts £m	Credit cards £m	Lease finance £m	Mortgages £m	Business lending [1] £m	Other retail lending £m	Total £m
Opening balance	11	14	7	27	221	15	295
Charge for the year	4	12	3	14	99	12	144
Amounts written off	(9)	(18)	(7)	(10)	(110)	(16)	(170)
Recoveries of amounts written off in previous years	4	4	-	-	8	4	20
Closing balance	10	12	3	31	218	15	289
Specific	-	-	3	18	113	-	134
Collective	10	12	-	13	105	15	155
	10	12	3	31	218	15	289

[1] Business lending includes business overdrafts.

16. Impairment provisions on credit exposures (continued)

Bank 2014	**Retail overdrafts £m**	**Credit cards £m**	**Lease finance £m**	**Mortgages £m**	**Business lending [1] £m**	**Other retail lending £m**	**Total £m**
Opening balance	10	12	2	21	218	15	**278**
Charge for the year	1	8	1	6	43	18	**77**
Amounts written off	(8)	(14)	(1)	(9)	(82)	(17)	**(131)**
Recoveries of amounts written off in previous years	4	3	-	-	5	4	**16**
Closing balance	**7**	**9**	**2**	**18**	**184**	**20**	**240**
Specific	-	-	2	13	92	-	**107**
Collective	7	9	-	5	92	20	**133**
	7	**9**	**2**	**18**	**184**	**20**	**240**

Bank 2013	Retail overdrafts £m	Credit cards £m	Lease finance £m	Mortgages £m	Business lending [1] £m	Other retail lending £m	Total £m
Opening balance	11	14	7	17	221	15	285
Charge for the year	4	12	3	8	99	12	138
Amounts written off	(9)	(18)	(8)	(4)	(110)	(16)	(165)
Recoveries of amounts written off in previous years	4	4	-	-	8	4	20
Closing balance	10	12	2	21	218	15	278
Specific	-	-	2	12	113	-	127
Collective	10	12	-	9	105	15	151
	10	12	2	21	218	15	278

[1] Business lending includes business overdrafts.

	Group		**Bank**	
	2014 £m	2013 £m	**2014 £m**	2013 £m
Amounts included in				
Loans and advances to customers (note 15)	**245**	289	**240**	278
Non-accrual loans				
Loans and advances to customers	**319**	363	**305**	325
Specific provisions	**(110)**	(134)	**(107)**	(127)
	209	229	**198**	198

17. Securitisations and covered bonds

Securitisations

The Group has securitised a proportion of its retail mortgage loan portfolio under the Group's master trust securitisation programmes. The securitised mortgage loans have been assigned at principal value to bankruptcy remote structured entities. These structured entities have been funded through the issue of residential mortgage backed debt to third party institutional debt investors. The Group is entitled to any residual income from the vehicles after the debt obligations and senior expenses of the programmes have been met. The securitised debt holders have no recourse to the Group other than the principal and interest (including fees) generated from the securitised mortgage portfolio. The Group continues servicing these mortgage loans in return for an administration fee.

The loans do not qualify for derecognition because the Group and Bank remain exposed to the majority of the risks and rewards of the mortgage portfolio, principally the credit risk associated with the underlying mortgage portfolio. The securitisation structured entities are consolidated and the securitised mortgage loans retained on the Group's balance sheet. The securitised notes in issue are included within debt securities in issue.

Covered bonds

A subset of the Group's retail mortgage portfolio has been ring fenced and assigned to a bankruptcy remote Limited Liability Partnership, associated with the covered bond programme, to provide a guarantee for the obligations payable on the covered bonds issued by the Group. Similar to the securitisation programmes, the Group is entitled to any residual income after all payment obligations due under the terms of the covered bonds and senior programmes expenses have been met.

The residential mortgages do not qualify for derecognition because the Group and Bank retain all of the risks and rewards associated with these mortgage loans. The covered bond partnership is fully consolidated with the loans retained on the Group and Bank balance sheets and the covered bonds issued are included within debt securities in issue. The covered bond holders have dual recourse; first to the Bank on an unsecured basis and second to the guarantee secured against the covered pool mortgage assets. The Group continue servicing these mortgage assets in return for an administration fee.

The balances of assets and liabilities in relation to Securitisation Notes and Covered Bonds in issue at 30 September 2014 within the Group and Bank balance sheets are as follows:

2014	Group			Bank		
	Securitised Notes £m	Covered Bonds £m	Total £m	Securitised Notes £m	Covered Bonds £m	Total £m
At 1 October 2013	2,030	1,041	3,071	-	1,096	1,096
Issuance of debt	601	-	601	-	-	-
Repayments	(216)	-	(216)	-	-	-
Other movements	(45)	22	(23)	-	1	1
At 30 September 2014	**2,370**	**1,063**	**3,433**	**-**	**1,097**	**1,097**
Securitised assets	**4,763**	**2,007**	**6,770**	**4,763**	**2,007**	**6,770**

17. Securitisations and covered bonds (continued)

2013	Group Securitised Notes £m	Group Covered Bonds £m	Group Total £m	Bank Securitised Notes £m	Bank Covered Bonds £m	Bank Total £m
At 1 October 2012	2,079	1,084	3,163	-	1,084	1,084
Issuance of debt	541	-	541	-	-	-
Repayments	(613)	-	(613)	-	-	-
Other movements	23	(43)	(20)	-	12	12
At 30 September 2013	2,030	1,041	3,071	-	1,096	1,096
Securitised assets	4,834	2,751	7,585	3,202	1,660	4,862

Further information on bonds and notes can be found in note 27.

The Bank securitises mortgages which includes those originated by Yorkshire Bank Home Loans Limited ("YBHL"), a subsidiary of the Group. A legal sale agreement between the Bank and YBHL has been put in place to ensure that title of such mortgages are transferred to the Bank prior to the completion of any securitisation transactions, and these mortgages are included in the securitised asset balances disclosed in the table above and are recognised on the Bank balance sheet in the year ended 30 September 2014.

Other movements consist of exchange rate movements on currency denominated bonds and fair value hedge accounting adjustments.

In addition to the securitisation notes disclosed above, there are £410m (2013: £441m) of Lannraig debt securities which are held by NAB and disclosed as a related party transaction (note 11). Assets which support the Lannraig debt are disclosed in the table above.

The following table sets out the carrying amount of financial assets that did not qualify for derecognition and their associated liabilities. Where relevant, the table also sets out the net position of the fair value of financial assets where the counterparty to the associated liabilities has recourse only to the financial assets:

Group	**2014 Securitisation £m**	**2014 Covered bonds £m**	2013 Securitisation £m	2013 Covered bonds £m
Carrying amount of transferred assets	**4,763**	**2,007**	4,834	2,751
Carrying amount of associated liabilities	**2,780**	**1,063**	2,471	1,041

For those liabilities that have recourse only to the transferred assets:

Group	**2014 Securitisation £m**	**2014 Covered bonds £m**	2013 Securitisation £m	2013 Covered bonds £m
Fair value of transferred assets	**4,763**	**-**	4,834	-
Fair value of associated liabilities	**2,780**	**-**	2,471	-
	1,983	**-**	2,363	-

There were no transactions in the year where the Group or Bank transferred financial assets that should have been derecognised in their entirety.

17. Securitisations and covered bonds (continued)

The Group has contractual and non-contractual arrangements which may require it to provide financial support to the following types of consolidated structured entities:

Securitisation vehicles

The Bank provides credit support to the structured entities via reserve funds through subordinated loan arrangements, exposures totalled £17m at the reporting date (2013: £1m). The Bank has a beneficial interest in the securitised mortgage portfolio held by the structured entities as at the reporting date of £690m (2013: £1,067m).

The Bank has an obligation to repurchase mortgage exposures if certain representations and warranties are breached. The Bank has made no such repurchases in the current year.

Looking forward through future reporting periods there are a number of date based calls and put options on the notes issued by the structured entities which could be actioned by them as issuer. These could require the Bank, as sponsor, to provide additional liquidity support.

Covered bonds

The Group has a regulated covered bond programme. A Limited Liability Partnership was established and a ring fenced mortgage portfolio assigned to provide a guarantee under the terms of the covered bonds. At the reporting date the nominal level of over-collateralisation was £1,249m (2013: £1,100m) of the outstanding covered bonds. From time-to-time the obligations of the Group to provide over-collateralisation may increase due to the formal requirements of the programme.

The Bank has an obligation to repurchase mortgage exposures if certain representations and warranties are breached. The Bank has made no such repurchases in the current year.

18. Property, plant and equipment

Group and Bank	Freehold land and buildings £m	Long-term leasehold land and buildings £m	Building improvements £m	Fixtures and equipment £m	Total £m
Cost or valuation					
At 1 October 2012	20	3	144	99	266
Additions	-	-	26	6	32
Disposals	(1)	-	(14)	(21)	(36)
At 30 September 2013	**19**	**3**	**156**	**84**	**262**
Additions	-	-	11	5	16
Disposals	(8)	-	(6)	(6)	(20)
At 30 September 2014	**11**	**3**	**161**	**83**	**258**
Accumulated depreciation					
At 1 October 2012	1	-	78	59	138
Charge for the year	-	-	13	6	19
Disposals	-	-	(8)	(7)	(15)
At 30 September 2013	**1**	**-**	**83**	**58**	**142**
Charge for the year	-	-	13	6	19
Disposals	-	-	(4)	(5)	(9)
At 30 September 2014	**1**	**-**	**92**	**59**	**152**
Net book value					
At 30 September 2014	**10**	**3**	**69**	**24**	**106**
At 30 September 2013	18	3	73	26	120

Valuations

The Group's freehold and long-term leasehold land and buildings are carried at their fair value as determined by independent valuers and the Group's own Directors' valuations. Fair values are determined in accordance with guidance published by the Royal Institution of Chartered Surveyors, including adjustments to observable market inputs reflecting any specific characteristics of the land and buildings (Level 3 of the fair value hierarchy as defined in note 37). Valuations are performed annually in July.

There has been no change to the valuation technique during the year. There were no transfers between levels of the fair value hierarchy during the year.

A comparison of the carrying value under the revaluation basis and if the historical cost basis had been used is shown below:

Group	2014 £m	2013 £m
Carrying value as included under the revaluation basis	**13**	21
Carrying value if the historical cost basis had been used	**11**	19

19. Investment properties

Group and Bank

	2014	2013
	£m	£m
At 1 October	**63**	77
Disposals	**(19)**	(14)
	44	63

Investment properties are stated at fair value, which has been determined based on valuations performed by independent valuers and the Group's own Directors' valuations.

Investment property is compared to property for which there is observable market data about its realisable value on disposal. Adjustments to this observable data are applied for specific characteristics of the property such as the nature, location or condition of the specific asset. Investment properties are classified in Level 3 of the fair value hierarchy as defined in note 37. There has been no change to the valuation technique during the year. There were no transfers between levels of the fair value hierarchy during the year.

During the year 99% (2013: 99%) of the investment properties generated total rental income of £2m (2013: £3m) and incurred operating and administrative expenses of £2m (2013: £2m). The operating and administrative expenses of the investment properties that did not generate rental income were £Nil (2013: £Nil).

20. Property inventory

	Group		**Bank**	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
At 1 October	**6**	9	**6**	7
Disposals	**(4)**	(3)	**(4)**	(1)
	2	6	**2**	6

All properties within property inventory are complete and available for sale. No properties are under construction (2013: £Nil).

21. Investment in controlled entities and associates

	Group		Bank	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
At 30 September	**2**	3	**12**	609

As a part of a Group rationalisation programme, a number of the Bank's subsidiaries were placed into voluntary liquidation with capital returned to the parent.

The table below represents the material subsidiaries of the Group as at 30 September 2014 and 30 September 2013:

Wholly owned subsidiary undertakings	**Nature of business**	**Country of incorporation**
Yorkshire Bank Home Loans Limited	Mortgage finance	England

The details of all subsidiary undertakings will be annexed to the next annual return of the Bank.

Structured entities

The Group sponsors the formation of structured entities, primarily for the purpose of facilitation of asset securitisation and covered bond transactions to accomplish certain narrow and well defined objectives. Although the Bank has no direct or indirect ownership interest in these entities, where it is exposed, or has rights to, variable returns from its involvement with the entities and has the ability to affect those returns through its power over the entity, they are regarded as controlled entities as described in note 2 and are consolidated in the Group's financial statements.

In the current and prior period all structured entities which the Group sponsors, or in which the Group holds an interest, are consolidated. Detail of the Group's interests in consolidated structured entities is set out in note 17.

The following companies are consolidated structured entities:

Other controlled entities as at 30 September 2014	**Nature of business**	**Country of incorporation**
Clydesdale Covered Bonds No. 2 LLP	Acquisition of mortgage loans	England
Lanark Trustees Limited	Mortgages trustee	Jersey
Lanark Funding Limited	Funding company	England
Lanark Master Issuer PLC	Issuer of securitised notes	England
Lannraig Trustees Limited	Mortgages trustee	Jersey
Lannraig Funding Limited	Funding company	England
Lannraig Master Issuer PLC	Issuer of securitised notes	England
Clydesdale Covered Bonds LLP (in liquidation)	Acquisition of mortgage loans	England

All of the above controlled entities have a 30 September financial year end.

Associates

Associates are undertakings over which the Bank exerts significant influence but not control. Investments in associates are accounted for using the equity method. The attributable share of profit and reserves of the associated undertaking is based on the management accounts as at 30 September 2014. The associated undertaking is The Scottish Agricultural Securities Corporation PLC, its country of registration and operations being Scotland. The associated undertaking's principal activity is the provision of finance and the Group's interest of 33.33% in the issued equity capital of £2m is held by the Bank. The associated undertaking has a 31 March year end.

Notes to the consolidated financial statements (continued)

21. Investment in controlled entities and associates (continued)

Significant restrictions

As is typical for a Group of its size, there are restrictions on the ability of certain subsidiary entities to make distributions of cash or other assets to the parent company. These are considered below:

Contractual requirements - asset encumberance

The Group uses its financial assets to raise finance in the form of securitisations and through the liquidity schemes of central banks. Once encumbered, the assets are not available for transfer around the Group. The assets affected are disclosed in the Strategic Report and note 17.

22. Deferred tax

Movement in net deferred tax asset	Group 2014 £m	Group 2013 £m As restated	Bank 2014 £m	Bank 2013 £m As restated
At 1 October	**220**	228	**214**	224
Recognised in the income statement (note 8)	**49**	(1)	**49**	(1)
Recognised directly in equity	**2**	(7)	**2**	(9)
Other	**6**	-	**6**	-
At 30 September	**277**	220	**271**	214

The Group recognises deferred tax attributable to the following items:

	Group 2014 £m	Group 2013 £m	Bank 2014 £m	Bank 2013 £m
Deferred tax assets				
Defined benefit pension liability	**-**	37	-	37
Impairment provision on credit exposures	**8**	9	**8**	9
Employee equity based compensation	**1**	1	**1**	1
Tax losses carried forward	**223**	103	**223**	103
Provisions	**25**	47	**25**	47
Accelerated capital allowances	**26**	20	**20**	20
Cash flow hedge reserve	**4**	-	**4**	-
Other	**-**	10	**-**	4
	287	227	**281**	221
Deferred tax liabilities				
Defined benefit pension asset	**10**	-	**10**	-
Net gain on revaluation of properties	**-**	1	**-**	1
Cash flow hedge reserve	**-**	6	**-**	6
	10	7	**10**	7
Net deferred tax asset	**277**	220	**271**	214

The Group considers it probable that sufficient future taxable profits will be available against which the underlying deductible temporary differences can be utilised. The largest deferred tax asset held within the Group relates to tax losses carried forward. The tax losses carried forward have been assessed for recoverability against the Group's forecasts which include adjustments for future strategic changes, the future economic outlook and regulatory change. Current UK tax legislation does not specify a maximum forecast horizon to utilise losses. The group expects that the recognised deferred tax asset of £223m in respect of tax losses will be recovered within four to six years. A twenty percent reduction in forecast profits would extend the recovery period by one year.

The statutory rate of UK corporation tax reduced from 24% to 23% on 1 April 2013 and to 21% on 1 April 2014. The enactment of Finance Act 2013 in July 2013 further reduced the corporation tax rate to 20% from 1 April 2015. Under IAS 12 deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. Accordingly, as the future reductions of the corporation tax rate to 21% and 20% were enacted on 17 July 2013, the deferred tax balances at 30 September 2014 have been reflected at the tax rates they are expected to be realised or settled.

Notes to the consolidated financial statements (continued)

23. Other assets

	Group 2014 £m	Group 2013 £m As restated	Bank 2014 £m	Bank 2013 £m As restated
Prepayments and accrued income	20	23	27	23
Other [1]	217	358	177	316
	237	381	204	339

[1] Other includes items in the course of collection.

24. Due to other banks

	Group 2014 £m	Group 2013 £m	Bank 2014 £m	Bank 2013 £m
Transaction balances with other banks	4	6	4	6
Securities sold under agreements to repurchase	644	-	644	-
Deposits from other banks	266	515	266	515
	914	521	914	521

25. Due to customers

	Group 2014 £m	Group 2013 £m	Bank 2014 £m	Bank 2013 £m
Non-interest bearing demand deposits	1,849	1,687	1,849	1,687
Interest bearing demand deposits	16,346	15,278	16,346	15,278
Term deposits	5,587	6,801	5,587	6,801
Other wholesale deposits	119	380	119	380
	23,901	24,146	23,901	24,146
Accrued interest payable	172	209	172	209
	24,073	24,355	24,073	24,355

26. Provisions

	Group 2014 £m	Group 2013 £m	Bank 2014 £m	Bank 2013 £m
Payment Protection Insurance redress provision				
Opening balance	**152**	108	**152**	108
Charge to the income statement (note 7)	**420**	130	**420**	130
Provision utilised	**(57)**	(86)	**(57)**	(86)
Closing balance	**515**	152	**515**	152
Customer redress and other provisions				
Opening balance	**118**	58	**118**	56
Charge to the income statement [1]	**376**	108	**376**	108
Provision utilised	**(81)**	(48)	**(81)**	(46)
Closing balance	**413**	118	**413**	118
Restructuring provision				
Opening balance	**33**	126	**33**	126
Provision utilised	**(8)**	(73)	**(8)**	(73)
Transfer to surplus lease space provision	**(7)**	(20)	**(7)**	(20)
Closing balance	**18**	33	**18**	33
Surplus lease space provision				
Opening balance	**12**	-	**12**	-
Charge to the income statement	**-**	2	**-**	2
Provision utilised	**(13)**	(10)	**(13)**	(10)
Transfer from restructuring provision	**7**	20	**7**	20
Closing balance	**6**	12	**6**	12
Total provisions	**952**	315	**952**	315

[1] The income statement effect of the interest rate hedging products provisioning is nil as it is offset by a receivable from NAB.

A provision is recognised when there is a present obligation as a result of a past event, it is probable that the obligation will be settled and it can be reasonably estimated. The most significant provisions held are in relation to conduct risk related liabilities.

The Group has provided its best estimate of conduct risk related liabilities at 30 September 2014 which have arisen as a result of its historical products and past sales practices.

To arrive at best estimates, management have exercised significant judgement around the key assumptions that underpin the estimates and used estimation techniques to quantify them. Ongoing regulatory review and input, as well as rulings from the Financial Ombudsman Service ("FOS") over time, and the Group's internal reviews and assessments of customer complaints will continue to impact upon the nature and extent of conduct-related customer redress and associated costs for which the Group may ultimately become liable in future periods. Accordingly the total cost associated with such conduct-related matters remains inherently uncertain.

Payment Protection Insurance ("PPI") redress

The Group has reassessed the level of provision that is considered appropriate to meet current and future expectations in relation to the mis-selling of PPI policies and has concluded that additional provisions of £420m should be recognised for the year ended 30 September 2014.

The total provision raised to date in respect of PPI is £806m (September 2013: £386m); with £515m of this remaining as at 30 September 2014 (September 2013: £152m).

26. Provisions (continued)

In common with the wider UK retail banking sector, the Group continues to deal with complaints and redress issues arising out of historic sales of PPI. The Group remains in regular dialogue with the Financial Conduct Authority ("FCA") regarding its approach to dealing with these issues and is subject to an enforcement process with the FCA in relation to its previous complaints handling process, the outcome of which is not yet known. Additionally, the Group is making modifications to its approach to PPI complaint handling, where appropriate, to reflect operational experience and ongoing discussions with the FCA, the FOS and third party professional advisers.

The increase in provisions includes amounts required for PPI redress in relation to the implementation of a revised complaints handling process, which has resulted in increased operational and administrative costs; higher than expected levels of new complaints; increased redress payments in respect of new complaints, costs associated with the ongoing enforcement process and additional operational and redress costs likely to be incurred as a result of reviewing previously handled complaints. The level of complaints received has declined compared to the prior year albeit the actual rate of decline is lower than previously anticipated and the month on month volatility has increased. The number of complaints received is monitored against past experience and future expectations.

The provision is based on a number of assumptions derived from a combination of past experience, estimated future experience, industry comparison and the exercise of judgement. There remain risks and uncertainties in relation to these assumptions and consequently in relation to the ultimate costs of redress and related costs, including the number of PPI claims (and the extent to which this is influenced by the activity of claims management companies), the number of those claims that ultimately will be upheld, the amount that will be paid in respect of those claims, any additional amounts that may need to be paid in respect to previously handled claims, any requirements to undertake further proactive customer contact and the outcome of the FCA enforcement process including the possibility of fines. These factors mean that the eventual costs of PPI redress and complaint handling may therefore differ materially from that estimated and further provision could be required. Accordingly, the final amount required to settle the Group's potential PPI liabilities remains uncertain.

The table below sets out the key assumptions and the effect on the provision of future, potential, changes in key assumptions:

Assumptions	**Change in assumption %**	**Sensitivity [(1)] £m**
Number of expected future customer initiated complaints	+/-10%	£13m
Uphold rates		
Future complaints yet to be received	+/-10%	£21m
Existing complaints to be reviewed	+/-10%	£50m
Customer contact response rate [(2)]	-10%	£(24)m
Average redress costs	+/-10%	£59m

(1) There are inter-dependencies between several of the key assumptions which add to the complexity of the judgements the Group has to make. This means that no single factor is likely to move independently of others; however, the sensitivities disclosed above assume all other assumptions remain unchanged.

(2) Existing complaints review.

The Group will continue to reassess the adequacy of the provision for this matter and the assumptions underlying the provision calculation based upon experience and other relevant factors as matters develop.

The requirement for further proactive customer contact will be determined by the Group undertaking a past business review. Where systemic sales failings are identified and there was a risk of mis-sale, proactive mailing to customers will be undertaken. At this stage the extent to which proactive mailings will be required as a result of the past business review and the outcome of the FCA enforcement process in relation to the Group's previous complaints handling processes, are, as yet, unknown. It has therefore not been possible to reliably estimate the extent of additional liabilities, if any, which may result and these matters are considered to be contingent liabilities.

26. Provisions (continued)

Customer redress and other provisions

A provision for customer redress is held in those instances where the Group expects to make payments to customers whether on an ex-gratia or compensatory basis. Provisions can arise as a result of legal or regulatory action and incorporate the costs of skilled persons, and where appropriate other elements of administration.

On 29 June 2012 the Financial Services Authority ("FSA") announced that it had reached agreement with a number of UK banks in relation to a review and redress exercise on sales of certain interest rate hedging products to small and medium businesses. The Group agreed to participate in this exercise, as announced by the FSA on 23 July 2012, and has embarked on a formal programme to identify small and medium sized customers that may have been affected and where due, pay financial redress. The exercise incorporates certain of the Group's tailored business loan products as well as the standalone hedging products identified in the FSA's notice. The Group is also dealing with a number of claims by customers in relation to tailored business loans not currently in scope of the review.

In the year to 30 September 2014, the Group has continued to review the cases originally identified and to respond and react to further guidance provided by the FCA and the FOS. It has also commenced settlement payments.

The Group has reassessed the level of provision considered necessary in light of the current and future expected claims for these matters and concluded that a further provision of £364m (30 September 2013: £49m) is appropriate at this time. This brings the total provisions raised in respect of interest rate hedging products to £431m (September 2013: £67m); with £362m of this remaining as at 30 September 2014 (September 2013: £49m).

The increase in provision is driven by a number of factors relating to offers of redress, compensation, offers of alternative products and costs. These factors could result in the total cost of the review and redress exercise and associated costs varying materially from the Group's estimate. The final amount required to settle the Group's potential liabilities in this matter is therefore uncertain and further provision could be required. The income statement effect of these provisions is nil due to the recognition of an offsetting receivable from NAB.

Other provisions include amounts provided in respect of legal proceedings, a number of individually less significant conduct related matters, and claims arising in the ordinary course of the Group's business. A net charge of £12m was recognised in the period to 30 September 2014. They include our contribution to the banking industry response to the CPP Scheme of Arrangement as well as a number of other matters.

Restructuring provision

Following the announcement of the results of the UK Banking strategic review on 30 April 2012, a restructuring provision of £139m was raised in May 2012. The provision covers redundancy payments, property vacation costs and associated enablement costs. In the period to 30 September 2014, £8m was utilised (2013: £73m).

Surplus lease space provision

The Group provides for committed rental expense on surplus lease space in line with the expected years' exposure on individual leases where the property is unoccupied. The level of surplus lease space increased as a result of the UK Banking strategic review as highlighted above. The provision will be utilised over the remaining life of the leases or until the leases are assigned. The provision is measured at present values by discounting anticipated future cash flows.

27. Bonds and notes

	Group 2014 £m	Group 2013 £m	Bank 2014 £m	Bank 2013 £m
Residential mortgage backed securities	**2,421**	2,039	**-**	-
Covered bonds	**1,097**	1,096	**1,097**	1,096
	3,518	3,135	**1,097**	1,096
Fair value hedge adjustments	**(85)**	(64)	**-**	-
Total securitised notes and covered bonds (note 17)	**3,433**	3,071	**1,097**	1,096
Accrued interest payable	**20**	14	**11**	14
	3,453	3,085	**1,108**	1,110

On 19 March 2014, €300m and £350m of residential mortgage backed securities were issued through Lanark 2014-1.

Details of the terms and conditions of the notes issued by Clydesdale Bank PLC to parties outside of the NAB Group as at 30 September 2014 were as follows:

Issue date	Currency	Carrying value £m	Coupon rate	Maturity date
Class A residential mortgage backed securities				
28 February 2012	EUR	351	3M EURIBOR + 1.95%	22 May 2015
27 July 2012	USD	401	3M USD LIBOR + 1.40%	22 May 2016
27 July 2012	GBP	523	3M GBP LIBOR + 1.63%	22 November 2017
13 July 2013	USD	178	3M USD LIBOR + 0.50%	22 August 2016
13 July 2013	GBP	337	3M GBP LIBOR + 0.45%	22 August 2016
19 March 2014	EUR	232	3M EURIBOR + 0.40%	22 August 2017
19 March 2014	GBP	348	3M GBP LIBOR + 0.50%	22 November 2018
		2,370		
Covered bonds				
31 May 2012	GBP	664	4.63%	08 June 2026
31 May 2012	GBP	399	3M GBP LIBOR + 1.70%	08 June 2015
		1,063		
		3,433		

28. Retirement benefit obligations

The Bank operates both defined benefit and defined contribution arrangements. The Bank is the sponsoring employer in one funded defined benefit scheme, the Yorkshire and Clydesdale Bank Pension Scheme ("the Scheme"). The Scheme was established under trust on 30 September 2009 as the result of the merger of the Clydesdale Bank Pension Scheme and the Yorkshire Bank Pension Fund. The assets of the Scheme are held in a trustee administered fund, the trustee is responsible for the operation and governance of the Scheme, including making decisions regarding the Scheme's funding and investment strategy.

The Scheme is subject to the funding legislation outlined in the Pensions Act 2004 which came into force on 30 December 2005. This, together with documents issued by the Pensions Regulator, sets out the framework for funding defined benefit occupational pension plans in the UK.

The Group also provides post-retirement health care under a defined benefit scheme for pensioners and their dependent relatives for which provision has been made. This is a closed scheme and the provision will be utilised over the life of the remaining scheme members. A one percentage point change in the assumed rate of increase in healthcare costs would change the defined benefit pension obligation by £0.3m (2013: £0.3m) and would have no material impact upon service costs and interest costs.

The following table provides a summary of the present value of the defined benefit obligation and fair value of plan assets for the Scheme:

	2014 **£m**	2013 £m
Active members defined benefit obligation	**(775)**	(1,004)
Deferred members defined benefit obligation	**(1,160)**	(889)
Pensioner and dependent members defined benefit obligation	**(1,285)**	(1,022)
Total defined benefit obligation	**(3,220)**	(2,915)
Fair value of scheme assets	**3,269**	2,718
Net defined benefit pension asset/(obligation)	**49**	(197)
Post-retirement medical benefits obligations	**(4)**	(5)
Retirement benefits obligation	**(4)**	(202)

IAS19 allows the recognition of an asset, which reflects the Group's ability to recover a surplus either through reduced contributions in the future or through refunds from the Scheme following the settlement of plan assets once all members have left the Scheme.

The Group has implemented a number of reforms to the Scheme to manage the liability. It closed the Scheme to new members in 2004 and has determined benefits accruing after April 2006 on a career average revalued earnings basis. The principal pension available to new employees since the closure of the Scheme is a defined contribution scheme, "Total Pension". The Total Pension income statement charge for the year is shown in note 7.

The Group implemented additional reforms to the Scheme which were effective from April 2012. These included changing the inflation index used to determine benefit increases from the Retail Price Index ("RPI") to the Consumer Price Index ("CPI") for future accruals and introducing member based contributions into the Scheme, increasing annually over a three year period. As an alternative to contributions, employees have the option of reducing their future annual rate of accrual from 1/60th of salary to 1/80th.

The last scheme funding valuation was at 30 September 2013 and revealed a deficit of £450m. In the recovery plan dated 7 May 2014 the Bank agreed to make the following contributions to eliminate the deficit: £65m on 1 October 2013; £150m by 30 June 2014; £50m on 1 October 2017; thereafter £50m annually until 1 October 2021; and £55m on 1 October 2022.

28. Retirement benefit obligations (continued)

Reconciliation of the net defined benefit pension asset/(liability)	2014 £m	2013 £m As restated
Opening net defined benefit pension scheme liability	(197)	(301)
Service cost	(23)	(38)
Interest on net defined benefit asset/(liability)	(3)	(8)
Remeasurement effects recognised in SOCI	24	21
Employer contributions	252	134
Administrative expenses	(4)	(5)
Closing fair value of net defined benefit pension scheme asset/(liability)	49	(197)

Reconciliation of the defined benefit pension scheme assets	2014 £m	2013 £m As restated
Opening fair value of defined benefit pension scheme assets	2,718	2,485
Interest income on scheme assets at discount rate	129	110
Return on scheme assets greater than discount rate	254	80
Employer contributions (note 11)	252	134
Benefits paid	(77)	(83)
Transfer payments	(3)	(3)
Administrative costs paid	(4)	(5)
Closing fair value of defined benefit pension scheme assets	3,269	2,718

Reconciliation of the defined benefit pension scheme obligations	2014 £m	2013 £m As restated
Opening defined benefit pension scheme obligations	(2,915)	(2,786)
Current service cost	(21)	(25)
Past service cost	(2)	(13)
Interest expense on the defined benefit obligation	(132)	(118)
Actuarial gain - experience adjustments	31	4
Actuarial (loss) – demographic assumptions	(23)	-
Actuarial (loss) – financial assumptions	(238)	(63)
Benefits paid from scheme assets	77	83
Transfer payments	3	3
Closing defined benefit pension scheme obligations	(3,220)	(2,915)

28. Retirement benefit obligations (continued)

The major categories of plan assets for the Scheme, stated at fair value, are as follows:

	2014 £m	2013 £m
Quoted		
Equities	**853**	725
Government bonds	**1,346**	924
Global sovereign bonds	**102**	103
Corporate bonds	**699**	717
Other [1]	**70**	64
Cash	**27**	92
Secure income alternatives	**62**	-
Unquoted		
Property	**110**	93
Fair value of defined benefit pension scheme assets	**3,269**	2,718

(1) Includes amounts held in an Emerging Market Currency fund

The Scheme is not invested in any of the Group's own financial instruments. The Property value above includes £16m in respect of the Group's offices at Merrion Way, Leeds.

Through its defined benefit pension plan and post-employment medical plan, the Group is exposed to a number of risks. The main risk to the Bank is that additional contributions are required if the Scheme's assets are not sufficient to pay for the benefits (which will be influenced mainly by inflation and the longevity of members). The level of equity returns will be a key factor in the overall investment return. The investment portfolio is also subject to a range of other risks typical of the assets held, in particular credit risk on bonds and exposure to the property market.

The Trustee has implemented an investment structure (including physical assets and derivatives) that seeks to reduce the Scheme's exposure to inflation and interest rate risks. The current hedge ratio is 50% of liabilities when measured on a self-sufficiency basis. This strategy reflects the Scheme's liability profile and the Trustee's and the Group's attitude to risk. The Trustee monitors the investment objectives and asset allocation policy on a regular basis.

Amounts recognised in the income statement	2014 £m	2013 £m As restated
Current service cost	**21**	25
Past service cost	**2**	13
Net interest on net defined benefit liability/(asset)	**3**	8
Defined benefit expense for the year	**26**	46
Administration costs incurred	**4**	5
Cost recognised in the income statement	**30**	51

In the current and prior period the past service cost relates to pension enhancements, which were agreed as part of redundancy and early retirement entitlements and in both periods these were fully offset in the income statement by a corresponding release from the restructure provision.

28. Retirement benefit obligations (continued)

Amounts recognised in the statement of comprehensive income	2014 £m	2013 £m As restated
Opening cumulative actuarial losses	(674)	(695)
Actuarial gain due to liability experience adjustments	31	4
Actuarial loss due to liability assumption changes	(261)	(63)
Return on scheme assets greater than discount rate	254	80
Cumulative actuarial losses recognised in the statement of comprehensive income	(650)	(674)

Actuarial assumptions	2014 % p.a.	2013 % p.a.
Financial assumptions		
Discount rate	4.10	4.60
Inflation (RPI)	3.15	3.25
Inflation (CPI)	2.15	2.25
Career average revalued earnings ('CARE') revaluations:		
Pre 31 March 2012 benefits (RPI)	3.15	3.25
Post 31 March 2012 benefits (CPI capped at 5% per annum)	2.15	2.25
Pension increases (capped at 2.5% per annum)	2.10	2.25
Pension increases (capped at 5% per annum)	3.00	3.10
Rate of increase for pensions in deferment	2.15	2.25

Demographic assumptions

Post retirement mortality:	2014 years	2013 years
Current pensioners at 60 – male	27.5	28.0
Current pensioners at 60 – female	29.4	28.5
Future pensioners at 60 – male	29.0	29.5
Future pensioners at 60 – female	30.9	30.0

28. Retirement benefit obligations (continued)

The table below sets out the sensitivity of the defined benefit obligation and pension cost to realistic changes in the key actuarial assumptions:

Assumption change	Impact on defined benefit obligation £m	Impact on pension cost £m
Discount rate		
+0.25%	(157)	(9)
-0.25%	169	9
Inflation		
+0.25%	142	7
-0.25%	(133)	(7)
Life expectancy		
+0.25%	98	5
-0.25%	(99)	(5)

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, changes in some of the assumptions may be correlated.

The discounted mean term of the defined benefit obligation at 30 September 2014 is 22 years. The expected contributions for the year ended 30 September 2015 are £38m and expected benefit payments for the year ended 30 September 2015 are £81m.

29. Other liabilities

	Group		Bank	
	2014 £m	2013 £m As restated	**2014 £m**	2013 £m As restated
Accruals and deferred income	**48**	48	**48**	48
Notes in circulation	**1,831**	1,709	**1,831**	1,709
Other	**178**	203	**138**	225
	2,057	1,960	**2,017**	1,982

30. Called up share capital

Group and Bank

Allotted, called up and fully paid	**2014 £m**	2013 £m
Ordinary shares of £1 each		
Opening ordinary share capital	**1,442**	1,442
Issued during the year	**600**	-
Closing ordinary share capital	**2,042**	1,442
Preference shares of £1 each		
Opening preference share capital	**300**	300
Redeemed during the period	**(300)**	-
Preference shares of £1 each	**-**	300
Closing called up share capital	**2,042**	1,742

In accordance with the Articles of Association ("Articles") of the Bank, and with the non-objection of the Prudential Regulation Authority, the Bank obtained the consent of NAGE ("the Holder") to redeem:

- 100,000,000 non-cumulative preference shares of £1 issued by the Bank on 11 December 2008 and held by the Holder; and
- 200,000,000 non-cumulative preference shares of £1 issued by the Bank on 20 December 2010 and held by the Holder.

The aforementioned preference shares were redeemed on 20 December 2013.

On 20 December 2013, 300,000,000 ordinary shares of £1 were issued. A further 300,000,000 ordinary shares of £1 were issued on 27 March 2014. All ordinary shares issued in the period were at par and fully paid up.

The holders of ordinary shares are entitled to dividends as declared from time to time and are entitled to one vote per share at meetings of the shareholders of the Bank. All shares in issue at 30 September 2014 rank equally with regard to the Company's residual assets.

31. Total equity

	Group		**Bank**	
	2014 £m	2013 £m	**2014 £m**	2013 £m
Share capital (note 30)	**2,042**	1,742	**2,042**	1,742
Share premium account	**243**	243	**243**	243
Total share capital and share premium	**2,285**	1,985	**2,285**	1,985
Merger reserve	**338**	338	**338**	338
Share option reserve	**2**	2	**2**	2
Asset revaluation reserve	**2**	2	**2**	2
Available for sale investments reserve	**8**	5	**8**	5
Cash flow hedge reserve	**(16)**	23	**(16)**	23
Total other reserves	**334**	370	**334**	370
Retained earnings	**(114)**	55	**(144)**	30
Total equity	**2,505**	2,410	**2,475**	2,385

31. Total equity (continued)

Merger reserve

The merger reserve arose as a result of the transfer of the entire business and undertakings of Yorkshire Bank PLC to Clydesdale Bank PLC on 1 December 2004. As no consideration was paid in relation to the transfer the only impact arising was the crystallisation of the Yorkshire Bank PLC share capital and share premium into a merger reserve in the combined entity.

Share option reserve

The Bank's share option reserve represents the outstanding fair value amount in respect of share based payment expense recharged by its ultimate parent that has been charged through the income statement and adjusted for deferred tax.

Asset revaluation reserve

The asset revaluation reserve includes the gross revaluation increments and decrements arising from the revaluation of land and buildings.

Available for sale investments reserve

The available for sale investments reserve records the gains and losses arising from changes in the fair value of available for sale investments.

Cash flow hedge reserve

The cash flow hedge reserve records fair value revaluations of derivatives designated as cash flow hedging instruments to the extent that they are effective.

As at 30 September 2014 the cash flow hedge reserve comprises the remaining crystallised fair value gains arising from the de-designated cash flow hedge in 2013 (£27m) offset by deferred losses on interest rate swaps in ongoing cash flow hedges (£47m). The balance on the cash flow hedge reserve is net of tax.

£48m (2013: £51m) was recycled into the income statement in relation to the de-designated hedge in the period. £2m (2013: £Nil) was transferred to the income statement due to ineffectiveness arising from cash flow hedges.

32. Contingent liabilities and commitments

The table below sets out the contractual amounts of contingent liabilities and commitments. Contingent liabilities and commitments are credit-related instruments which include acceptances, letters of credit, guarantees and commitments to extend credit. The contractual amounts do not represent the amounts at risk at the balance sheet date but the amounts that would be at risk should the contracts be fully drawn upon and the client default. Since a significant portion of guarantees and commitments are expected to expire without being drawn upon, the total of the contract amounts is not representative of future liquidity requirements.

	Group		Bank	
Contingent liabilities	**2014**	2013	**2014**	2013
	£m	£m	**£m**	£m
Guarantees and assets pledged as collateral security:				
At call	**-**	1	**-**	1
Due in less than 3 months	**32**	34	**32**	34
Due between 3 months and 1 year	**25**	63	**25**	63
Due between 1 year and 3 years	**9**	12	**9**	12
Due between 3 years and 5 years	**3**	4	**3**	4
Due after 5 years	**61**	90	**61**	90
No specified maturity	**6**	9	**6**	9
	136	213	**136**	213
Other credit commitments				
Undrawn formal standby facilities, credit lines and other commitments to lend at call	**8,463**	8,696	**8,424**	8,664

Capital commitments

The Group and Bank had future capital expenditure which had been contracted for but not provided for in the financial statements at 30 September 2014 of £2.2m (2013: £0.7m).

Operating lease commitments

Group and Bank

	2014	2013
Leases as lessor	**£m**	£m
Future minimum lease payments under non-cancellable operating leases are:		
within 1 year	**2**	2
between 1 year and 5 years	**6**	3
over 5 years	**2**	2
	10	7
Leases as lessee		
Future minimum lease payments under non-cancellable operating leases are:		
within 1 year	**30**	31
between 1 year and 5 years	**94**	91
over 5 years	**121**	115
	245	237

Notes to the consolidated financial statements (continued)

32. Contingent liabilities and commitments (continued)

Other contingent liabilities

Financial Services Compensation Scheme

The UK Financial Services Compensation Scheme ("FSCS") provides compensation to depositors in the event that a financial institution is unable to repay amounts due. Following the failure of a number of financial institutions, the FSCS has raised borrowings from the UK Government to cover compensation in relation to protected deposits. These borrowings are anticipated to be largely repaid from the realisation of the assets of the institutions. During the last year, the FSCS has also invoiced institutions for the first of three annual levies to cover capital repayments to the UK Government. The principal of these borrowings which remains after the three annual levies have been paid is anticipated to be repaid from the realisation of the assets of the defaulted institutions. The FSCS has however confirmed that the size of the future levies will be kept under review in light of developments from the insolvent estates.

The FSCS has estimated levies due to 31 March 2015 and an accrual of £7m (2013: £7m) is held for the Group's calculated liability to that date, with £6m of the current year charge having already been paid. The ultimate FSCS levy is uncertain.

Conduct risk related matters

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 26 to the annual report and consolidated financial statements reflecting the Group's current position in relation to redress for the PPI and interest rate hedging products. 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.

Legal claims

The Group is named in and is defending a number of legal claims arising in the ordinary course of business. No material adverse impact on the financial position of the Group is expected to arise from the ultimate resolution of these legal actions.

33. Notes to the statements of cash flows

	Group		Bank	
	2014	2013	2014	2013
	£m	£m	£m	£m
		As restated		As restated
Adjustments included in the loss before tax				
Interest receivable	(1,135)	(1,209)	(1,126)	(1,162)
Interest payable	364	453	445	453
Depreciation (note 7)	19	19	19	19
Profit on sale of tangible fixed assets [1]	(7)	(1)	(7)	(1)
Transfer from cash flow hedge reserve	(2)	3	(2)	3
Derivative financial instruments fair value movements	(9)	11	(2)	11
Impairment losses on credit exposures (note 16)	74	144	77	138
Dividends received from subsidiaries	-	-	(26)	(116)
Movement in share option reserve	-	(3)	-	(3)
	(696)	(583)	(622)	(658)
Changes in operating assets				
Net decrease/(increase) in:				
Balances with supervisory central banks	1	(12)	1	(12)
Due from other banks	171	(170)	171	(171)
Derivative financial instruments	(26)	247	(9)	281
Financial assets at fair value through profit or loss	585	636	585	636
Loans and advances to customers	(2,001)	307	(5,065)	178
Due from customers on acceptances	(1)	3	(1)	3
Other assets	80	(107)	59	(128)
Assets held for sale	-	5,225	-	5,225
	(1,191)	6,129	(4,259)	6,012
Changes in operating liabilities				
Net increase/(decrease) in:				
Due to other banks	395	(55)	395	(55)
Derivative financial instruments	(135)	(289)	(146)	(315)
Financial liabilities at fair value through profit or loss	(31)	(27)	(31)	(27)
Due to customers	(245)	(2,235)	(245)	(2,235)
Liabilities on acceptances	1	(3)	1	(3)
Provisions (note 26)	637	23	637	25
Defined benefit pension obligations	(223)	(83)	(223)	(83)
Other liabilities	164	175	140	161
Liabilities associated with assets held for sale	-	(142)	-	(142)
	563	(2,636)	528	(2,674)

[1] Tangible fixed assets include property, plant and equipment, investment properties and property inventory.

For the purposes of the statement of cash flows, cash and cash equivalents comprise the following balances with less than three months maturity from the date of acquisition.

	Group		Bank	
	2014	2013	2014	2013
	£m	£m	£m	£m
Cash and balances with central banks (note 10)	5,929	6,672	5,929	6,672
Other assets	143	178	143	178
Due to other banks	(26)	(28)	(26)	(28)
Due to related entities	(108)	(182)	(108)	(182)
Other liabilities	(58)	(95)	(58)	(95)
	5,880	6,545	5,880	6,545

34. Employees

The average number of full time equivalent employees of the Group during the year was made up as follows:

	2014 Number	2013 Number
Managers	992	1,131
Clerical staff	3,529	3,439
	4,521	4,570

The average number of staff employed in the UK Banking operating division of NAB in the year to 30 September 2014 was 7,123 (2013: 6,798). All staff are contracted employees of NAGE and its subsidiary undertakings. The numbers above disclose the staff remunerated directly by the Group but exclude employees working within other NAGE subsidiaries who provide support services to the Group.

35. Equity based compensation

Share incentive plans, share offers, performance options and performance rights are used to provide short-term and long-term incentives to employees. These incentives are an integral part of the Group's remuneration strategy in rewarding employees' current and future contribution to the Group's performance. All UK awards are made in accordance with the principles set out within the Prudential Regulation Authority's Remuneration Code.

The plans described below involve the provision of shares, performance options and performance rights to employees, senior management and Directors of the Group.

Short term incentive ("STI")

The STI plan has an element of deferral to provide an appropriate level of reward aligned with sound risk management principles. STI deferral encourages longer-term sustainable decision making and assurance of individual and business performance. Deferral applies to all levels of performance across the organisation. Deferral is in the form of NAB shares, rights or cash. The deferred amount is subject to forfeiture conditions including forfeiture as a result of resignation, termination by NAB or failure to meet compliance requirements. A reduction or forfeiture of deferred amounts can also be determined by the Principal Board, at its absolute discretion. Such a determination may be made in relation to the NAB Group, a business unit, executive committee, role or individual.

Recognition and retention shares

These shares enable retention and recognition awards to be provided in the form of shares, rather than in cash. Such awards are made on a very limited basis with NAB Group Principal Board Remuneration Committee approval, to individuals in significant key roles where retention is critical over a medium-term timeframe (two to three years). Awards under the programme may also be provided to individuals accepting significant project leadership or additional responsibilities for a limited period of time with no related increase in their fixed remuneration. The provision of shares under this plan is desired over the use of cash payments, as it provides a stronger retention and shareholder value link to the reward. The shares are subject to forfeiture conditions including forfeiture as a result of resignation, or retirement or failure to meet compliance requirements. The minimum restriction period is until the final key date or milestone has been achieved.

Commencement shares

These shares enable 'buyout' of evidenced equity from previous employment for significant new hires. Shares are provided under this programme or commencement performance options and performance rights if more appropriate. The shares are subject to forfeiture conditions including forfeiture as a result of resignation, termination by NAB or failure to meet compliance requirements.

35. Equity based compensation (continued)

UK Share Incentive Plan

The UK Share Incentive Plan is an approved HM Revenue and Customs share plan. Employees are entitled to purchase up to £1,800 worth of NAB shares each year through the Partnership Share Plan. Participants contribute each month and the trustee uses the contributions to purchase shares on the market which are then held in trust for the participants. Participants are entitled to receive dividends and exercise voting rights in respect of these shares and there is no risk of forfeiture. In addition, up to £3,000 of free shares may be awarded by the employer to employees per annum.

General employee shares

Up to a target value of A$1,000 of NAB shares are offered to each eligible employee when the NAB Group's performance is on target, measured against a scorecard of objectives for the financial year. These shares are held in trust, restricted from dealing for three years and in the UK these shares are forfeited if an employee is summarily dismissed prior to the end of three years.

Long-term incentives ("LTI")

LTI taking the form of shares, performance options or performance rights, help to drive management decisions focused on the long-term prosperity of the NAB Group through the use of challenging performance hurdles. The Executive LTI programme is awarded to senior executives across the Group. A LTI target is set with reference to external and internal relativities for each executive who must also meet minimum performance and compliance thresholds. Performance hurdles (both internal and external) are measured at the end of a three to five year restriction period and during the restriction period an executive's performance rights or performance options will lapse (or their shares will be forfeited) for cessation of employment (if the Board so determines) or, if compliance requirements or performance hurdles are not met.

For historical awards a variety of performance measures are used for different grants of long-term incentives including Total Shareholder Return ("TSR") compared against peer companies, and regional or NAB Group ROE and cash earnings. The measures used depend on the level and impact of the participant's role, the business or region in which they work and the relevant program.

Vesting of an LTI award generally occurs to the extent that the relevant performance hurdle is satisfied (as determined by the NAB Board Remuneration Committee). The performance options and performance rights generally have an expiry date between three and six years from the effective date, if they remain unexercised.

Each performance option or performance right is exchanged for one fully paid ordinary share in NAB Limited upon exercise, subject to standard adjustments for capital actions. The exercise price for performance options is generally the market price for NAB Limited's fully paid ordinary shares as at the date the performance option was granted or such other relevant date determined by the NAB Board Remuneration Committee. No exercise price is payable by the holder on exercise of performance rights.

Notes to the consolidated financial statements (continued)

35. Equity based compensation (continued)

The movement in performance options and performance rights granted and exercised during the year was as follows:

Performance options	2014 Number	2014 Weighted average exercise price A$	2013 Number	2013 Weighted average exercise price A$
Outstanding at 1 October	85,715	19.89	278,946	26.12
Granted during the year	-	-	-	-
Forfeited and lapsed during the year	(4,947)	19.89	(55,527)	30.65
Exercised during the year	(80,768)	19.89	(41,177)	19.89
Expired during the year	-	-	(96,527)	31.70
Outstanding at 30 September	-		85,715	19.89
Exercisable at 30 September	-		-	

The number of performance options exercised during the year was 80,768 (2013: 41,177). There are no performance options outstanding at 30 September 2014 and the weighted average remaining contractual life of those outstanding at 30 September 2013 was 0.79 years. The exercise price for performance options outstanding at 30 September 2013 was A$19.89.

Performance rights	2014 Number	2013 Number
Outstanding at 1 October	186,119	145,729
Granted during the year	197,835	61,258
Forfeited and lapsed during the year	(124,861)	(20,868)
Exercised during the year	-	-
Expired during the year	-	-
Outstanding at 30 September	259,093	186,119
Exercisable at 30 September	-	-

No performance rights were exercised during the year (2013: Nil). For performance rights outstanding at 30 September 2014, the weighted average remaining contractual life is 4.04 years (2013: 2.87 years). No exercise price is payable by the holder on exercise of performance rights.

Fair value of share options and performance rights

No performance options were granted during the year ended 30 September 2014 (2013: Nil). 197,835 performance rights were granted during the year ended 30 September 2014 (2013: 61,258). Included within personnel expenses (note 7) is a fair value of goods or services to the value of £2.1m, which was measured indirectly by reference to the fair value on the performance rights granted during the year (2013: £0.8m).

36. Directors' emoluments

2014 £'000	Salary and fees [1]	Benefits and allowances [2]	Performance related pay: Short term incentive schemes [3]: Upfront (cash)	Deferred (shares)	Total short term	Long term incentive schemes[5]: Deferred (cash)	Deferred (performance rights)	Deferred (shares)	Total long term	Total emoluments
Executive Directors										
Cameron Clyne [4] [8]	-	-	-	-	-	-	-	-	-	-
Debbie Crosbie [6]	127	28	15	46	61	-	38	1	39	255
John Hooper	400	63	100	100	200	-	-	-	-	663
Mark Joiner [4] [8]	-	-	-	-	-	-	-	-	-	-
Richard Sawers [4]	-	-	-	-	-	-	-	-	-	-
David Thorburn	450	99	45	135	180	-	225	1	226	955
Total Executive	**977**	**190**	**160**	**281**	**441**	**-**	**263**	**2**	**265**	**1,873**
Non-executive Directors										
David Allvey	82	-	-	-	-	-	-	-	-	82
David Browne	80	-	-	-	-	-	-	-	-	80
Richard Gregory OBE	140	-	-	-	-	-	-	-	-	140
Barbara Ridpath	70	-	-	-	-	-	-	-	-	70
James Pettigrew [7]	119	-	-	-	-	-	-	-	-	119
Alexander Shapland	70	-	-	-	-	-	-	-	-	70
Total Non-executive	**561**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**561**
Total Directors	**1,538**	**190**	**160**	**281**	**441**	**-**	**263**	**2**	**265**	**2,434**

In addition to amounts shown in the above table, social security costs were payable in respect of emoluments for Directors amounting to £305,000 (2013: £405,000) and in respect of emoluments for the highest paid Director of £130,118 (2013: £175,000).

Notes to the consolidated financial statements (continued)

36. Directors' emoluments (continued)

2013 £'000			Performance related pay							
			Short term incentive schemes [3]			Long term incentive schemes[5]				
	Salary and fees [1]	Benefits and allowances [2]	Upfront (cash)	Deferred (shares)	Total short term	Deferred (cash)	Deferred (performance rights)	Deferred (shares)	Total long term	Total emoluments
Executive Directors										
Cameron Clyne [4] [8]	-	-	-	-	-	-	-	-	-	-
John Hooper	591	242	70	211	281	267	267	1	535	1,649
Mark Joiner [4] [8]	-	-	-	-	-	-	-	-	-	-
Richard Sawers [4]	-	-	-	-	-	-	-	-	-	-
David Thorburn	450	101	63	253	316	338	338	1	677	1,544
Total Executive	1,041	343	133	464	597	605	605	2	1,212	3,193
Non-executive Directors										
David Allvey	78	-	-	-	-	-	-	-	-	78
David Browne	78	-	-	-	-	-	-	-	-	78
Richard Gregory OBE	138	-	-	-	-	-	-	-	-	138
James Pettigrew [7]	80	-	-	-	-	-	-	-	-	80
Barbara Ridpath	69	-	-	-	-	-	-	-	-	69
Alexander Shapland	69	-	-	-	-	-	-	-	-	69
Total Non-executive	512	-	-	-	-	-	-	-	-	512
Total Directors	1,553	343	133	464	597	605	605	2	1,212	3,705

The table above includes deferred cash and deferred performance rights awarded on 20 February 2013 in respect of the previous financial year.

36. Directors' emoluments (continued)

Notes

(1) Salary costs include salaries paid to Executive Directors and fees paid to Non-executive Directors.

(2) Benefits and allowances include cash payments in lieu of pension contributions and other taxable allowances and benefits. Retirement benefits accrued to two Directors (2013: one) under a defined benefit pension plan. Pension contributions amounting to £50,013 (2013: £16,730) were paid during the year. The highest paid director is a deferred member of the defined benefit pension plan.

(3) Performance related pay relates to the respective financial year. The short-term incentive scheme includes a cash element to be paid in the forthcoming year and the deferred amount represents rights and shares deferred for six months to two years. The highest paid Director received 5,656 shares (2013: 110,331) that vested during the year, with a fair value of £65,307 (2013: £422,940).

(4) Cameron Clyne, Mark Joiner and Richard Sawers were remunerated as employees of NAB, and did not receive incremental remuneration in respect of their duties as Directors of the Bank. The Directors believe it would be appropriate to apportion A$618,000 (2013: A$782,000) of their remuneration as being in respect of their duties to the Bank.

(5) The long-term incentive scheme amounts principally represent deferred performance rights for services rendered during the year which require the achievement of performance hurdles and/or milestones before they vest. The performance period is four years. The value attributed is the fair value of the shares at the date of granting. Two Directors (2013: two) received benefits under an executive long-term incentive scheme.

(6) Debbie Crosbie was appointed as an Executive Director on 12 May 2014 and accordingly the figures in the table above represent her emoluments from this date.

(7) James Pettigrew was appointed as Non-executive Chairman on 1 August 2014. He was a Non-executive Director for the full year.

(8) Mark Joiner resigned as a Director on 31 December 2013. Cameron Clyne resigned as a Director and as Chairman on 1 August 2014.

(9) The table below shows, for the highest paid Director in the given year, the number of shares in respect of share options, performance rights, short term incentive, long term incentive and other employee share plans (including free shares, commencement shares, recognition shares).

2014 **Number**	**Performance options**	**Performance rights**	**Short term incentive shares**	**Long term incentive shares**	**Other employee share plans**
Outstanding at 1 October	-	47,894	-	9,205	76
Granted during the year	-	51,322	1,657	-	26
Exercised/disposed during the year	-	-	(1,657)	(3,953)	-
Expired during the year	-	-	-	-	-
Forfeited and lapsed during the year	-	(36,016)	-	(5,252)	-
Restrictions ceased	-	-	-	-	-
Outstanding at 30 September	**-**	**63,200**	**-**	**-**	**102**

2013 Number	Performance options	Performance rights	Short term incentive shares	Long term incentive shares	Other employee share plans
Outstanding at 1 October	245,716	21,146	17,802	29,790	8,219
Granted during the year	-	12,060	-	-	36
Exercised/disposed during the year	(33,802)	-	(5,728)	(4,774)	-
Expired during the year	(90,216)	-	-	-	-
Forfeited and lapsed during the year	(51,334)	-	-	(8,314)	-
Restrictions ceased	-	-	(6,347)	-	-
Outstanding at 30 September	70,364	33,206	5,727	16,702	8,255

37. Fair value of financial instruments

(a) Fair value of financial instruments carried at amortised cost

The tables below show a comparison of the carrying amounts, as reported on the balance sheet, and fair values of those financial assets and liabilities measured at the amortised cost where the carrying value amounts of the financial assets and financial liabilities recorded at amortised cost in the balance sheet are not approximately equal to their fair value.

Analysis of the fair value disclosures uses a hierarchy that reflects the significance of inputs used in measuring the fair value. The level in the fair value hierarchy within which a fair value measurement is categorised is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. The fair value hierarchy is as follows:

- Level 1 fair value measurements - quoted prices (unadjusted) in active markets for identical financial assets or liabilities.
- Level 2 fair value measurements - inputs other than quoted prices within Level 1 that are observable for the financial asset or liability, either directly (as prices) or indirectly (derived from prices).
- Level 3 fair value measurements - inputs for the financial asset or liability that are not based on observable market data (unobservable inputs).

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The estimated fair values are based on relevant information available at the reporting date and involve judgement. The methodologies and assumptions used in the fair value estimates are described in the footnotes to the tables.

There are various limitations inherent in this fair value disclosure particularly where prices may not represent the underlying value due to dislocation in the market. Not all of the Group's financial instruments can be exchanged in an active trading market. The Group obtains the fair values for investment securities from quoted market prices where available. Where securities are unlisted and quoted market prices are not available, the Group obtains the fair value by means of discounted cash flows and other valuation techniques that are commonly used by market participants. These techniques address factors such as interest rates, credit risk and liquidity. The difference between carrying value and fair value is relevant in a trading environment, but is not relevant to assets held to maturity and loans and advances.

Group	30 September 2014					30 September 2013	
			Fair value measurement using:				
	Carrying value	Fair value	Quoted market prices (Level 1)	Valuation techniques (observable inputs) (Level 2)	Valuation techniques (significant non-observable inputs) (Level 3)	Carrying value	Fair value
	£m	£m	£m	£m	£m	£m	£m
Financial assets							
Loans and advances to customers	**25,901**	**25,734**	-	**1,293**	**24,441**	23,960	24,004
Financial liabilities							
Due to customers	**24,073**	**24,083**	-	**24,083**	-	24,355	24,402
Due to related entities	**2,452**	**2,435**	-	**2,435**	-	2,860	2,860
Bonds and notes	**3,453**	**3,534**	-	**3,534**	-	3,085	3,088

37. Fair value of financial instruments (continued)

Bank	30 September 2014					30 September 2013	
			Fair value measurement using:				
	Carrying value	Fair value	Quoted market prices (Level 1)	Valuation techniques (observable inputs) (Level 2)	Valuation techniques (significant non-observable inputs) (Level 3)	Carrying value	Fair value
	£m	£m	£m	£m	£m	£m	£m
Financial assets							
Investments - Held to maturity	1,483	1,505	-	874	631	1,415	1,415
Loans and advances to customers	24,450	24,324	-	1,293	23,031	19,438	19,474
Financial liabilities							
Due to customers	24,073	24,083	-	24,083	-	24,355	24,402
Due to related entities	6,465	6,427	-	6,427	-	6,931	6,931
Bonds and notes	1,108	1,196	-	1,196	-	1,110	1,111

The Group and Bank's fair values disclosed for financial instruments at amortised cost are based on the following methodologies and assumptions:

(a) *Cash and balances with central banks, Due from and to other banks, Due from customers on acceptances, Liabilities on acceptances, Other assets and Other liabilities* – Carrying values approximate fair value as they are short term in nature and or receivable or payable on demand.

(b) *Amounts due from related entities* – Amounts due from related entities are repayable on demand or within twelve months. As a result, the carrying value approximates the fair value.

(c) *Investments held to maturity* – The Group obtains the fair value by means of a discounted cash flow model based upon observable market data and non-observable inputs as appropriate to the nature and type of the underlying instrument.

(d) *Loans and advances to customers* – The fair value of loans and advances is determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity and incorporating behavioural adjustments where appropriate.

(e) *Amounts due to related entities* – The fair value of subordinated loans due to; and notes issued to related entities is determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity. All other amounts due to related entities are repayable under varying maturities but are materially repriced every 3-6 months relative to market rates, as a result, the carrying value approximates the fair value.

(f) *Due to customers* – The fair value of deposits is determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity.

(g) *Bonds and notes* – The fair value is determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity.

Notes to the consolidated financial statements (continued)

37. Fair value of financial instruments (continued)

(b) Fair value measurements recognised on the balance sheet

The following tables provide an analysis of financial instruments that are measured subsequent to initial recognition at fair value, using the fair value hierarchy described in note 37(a) above.

Group	Fair value measurement as at 30 September 2014				Fair value measurement as at 30 September 2013			
	Quoted market prices (Level 1) £m	Valuation techniques (observable inputs) (Level 2) £m	Valuation techniques (significant non-observable inputs) (Level 3) £m	Total £m	Quoted market prices (Level 1) £m	Valuation techniques (observable inputs) (Level 2) £m	Valuation techniques (significant non-observable inputs) (Level 3) £m	Total £m
Financial assets								
Derivative financial assets	-	220	-	**220**	-	244	-	244
Investments – available for sale – listed	1,161	-		**1,161**	968	-	-	968
Investments – available for sale – unlisted	-		7	**7**	-	-	7	7
Other financial assets at fair value	-	-	1,583	**1,583**	-	-	2,171	2,171
Total financial assets measured at fair value	**1,161**	**220**	**1,590**	**2,971**	968	244	2,178	3,390
Financial liabilities								
Derivative financial liabilities	-	548	-	**548**	-	651	-	651
Other financial liabilities at fair value	-	-	91	**91**	-	-	123	123
Total financial liabilities measured at fair value	**-**	**548**	**91**	**639**	-	651	123	774

37. Fair value of financial instruments (continued)

Bank	Fair value measurement as at 30 September 2014				Fair value measurement as at 30 September 2013			
	Quoted market prices (Level 1) £m	Valuation techniques (observable inputs) (Level 2) £m	Valuation techniques (significant non-observable inputs) (Level 3) £m	Total £m	Quoted market prices (Level 1) £m	Valuation techniques (observable inputs) (Level 2) £m	Valuation techniques (significant non-observable inputs) (Level 3) £m	Total £m
Financial assets								
Derivative financial assets	-	220	-	**220**	-	244	-	244
Investments – available for sale – listed	1,161	-	-	**1,161**	968	-	-	968
Investments – available for sale – unlisted	-	-	7	**7**	-	-	7	7
Other financial assets at fair value	-	-	1,583	**1,583**	-	-	2,171	2,171
Total financial assets measured at fair value	**1,161**	**220**	**1,590**	**2,971**	968	244	2,178	3,390
Financial liabilities								
Derivative financial liabilities	-	451	-	**451**	-	566	-	566
Other financial liabilities at fair value	-	-	91	**91**	-	-	123	123
Total financial liabilities measured at fair value	**-**	**451**	**91**	**542**	-	566	123	689

The Group and Bank's fair values for financial instruments, that are measured subsequent to initial recognition at fair value, are based on the following methodologies and assumptions:

(a) *Investments* – The fair values of listed investments are based on quoted closing market prices. For unlisted equity investments the Group's share of the net asset value of the undertaking is considered the best representation of the fair value of the investment.

(b) *Other financial assets and liabilities at fair value* – Fair values are based on quoted market prices and data or valuation techniques based upon observable market data and non-observable inputs as appropriate to the nature and type of the underlying instrument. Derivatives which did not meet the requirements for hedge accounting and that are related to loans held at fair value through profit or loss are accounted for as held for trading derivative financial instruments (note 14).

(c) *Derivative financial assets and liabilities* – The fair value of derivatives, including foreign exchange contracts, interest rate swaps, interest rate and currency option contracts, and currency swaps, are obtained from quoted closing market prices as at the balance sheet date, discounted cash flow models or option pricing models as appropriate.

There were no transfers between Level 1 and 2 in the period.

Notes to the consolidated financial statements (continued)

37. Fair value of financial instruments (continued)

Assets and liabilities measured at fair value based on valuation techniques for which any significant input is not based on observable market data (Level 3):

Level 3 movements analysis: Group and Bank	**2014**		
	Investments – available for sale £m	**Other financial assets at fair value £m**	**Other financial liabilities at fair value £m**
Balance at the beginning of the period	**7**	**2,171**	**123**
Total gains/(losses)			
In profit or loss [1]	**-**	**(44)**	**(4)**
Settlements	**-**	**(544)**	**(28)**
Balance at the end of the period	**7**	**1,583**	**91**

Level 3 movements analysis: Group and Bank	2013		
	Investments – available for sale £m	Other financial assets at fair value £m	Other financial liabilities at fair value £m
Balance at the beginning of the period	7	4,266	147
Total gains/(losses)			
In profit or loss [1]	-	(176)	(5)
Sales	-	(1,452)	-
Settlements	-	(467)	(19)
Balance at the end of the period	7	2,171	123

[1] Net gains or losses were recorded in other operating income, interest income or interest expense and impairment losses as appropriate.

There were no transfers out of Level 3 in the year ended 30 September 2014 (2013: Nil).

The total gains or losses for the year ended 30 September 2014 includes an unrealised loss of £44m (2013: £176m) relating to financial assets that are measured at fair value at the end of each reporting period. Such fair value gains or losses are included in non-interest income (note 6).

37. Fair value of financial instruments (continued)

The table below lists key unobservable inputs to Level 3 financial instruments, and provides the range of those inputs as at 30 September 2014.

Group	Fair value £m	Valuation technique	Unobservable inputs	Low range	High range
Financial assets					
Investments – available for sale					
Unlisted	7	Underlying/net asset value	Price	Nil	Market value on disposal
Other financial assets at fair value	1,583	Discounted cash-flow	Portfolio lifetime probability of default	5.0%	11.2%

The unlisted available for sale investments primarily relates to the Group's holding of shares in Vocalink Limited, an unquoted company registered in England and Wales which operates the BACS and direct debits schemes in the UK as well as connecting ATMs using the LINK network. This represents the Group's percentage holding in this entity. The valuation is based on the net asset value in the most recent set of publically available financial statements for the company and represents the fair value of the investment.

The Group has £91m of financial liabilities at fair value classed as Level 3 which represent a portfolio of term deposits that are directly linked to the customer loans, which are also held at fair value and classed as Level 3. Their relationship to the fair value assets is such that should the liability be settled, the amount payable would be net of the fair value asset.

Sensitivity of Level 3 fair value measurements to reasonably possible alternative assumptions

Where valuation techniques use non-observable inputs that are significant to a fair value measurement in its entirety, changing these inputs will change the resultant fair value measurement.

The most significant exposure to Level 3 fair value measurements is in respect of the Group's fair value loan portfolio.

The most significant inputs impacting the carrying value of the loans other than interest rates are future expectations of credit losses and the expected payment profile of the loans. If the loans were to be repaid six months earlier than currently predicted the loan carrying value would decline by £5m. If lifetime expected losses were 20% greater than predicted, the carrying value of the loans would decrease by £15m and vice versa. There are inter-dependencies between a number of the key assumptions which add to the complexity of the judgements the Group has to make which mean that no single factor is likely to move independent of others, however, the sensitivities disclosed above assume all other assumptions remain unchanged.

Other than these significant Level 3 measurements, the Group has a limited remaining exposure to Level 3 fair value measurements, and changing one or more of the inputs for fair value measurements in Level 3 to reasonable alternative assumptions would not change the fair value significantly with respect to profit or loss, total assets, total liabilities or equity on these remaining Level 3 measurements.

38. Financial risk management

Strategy in using financial instruments

By their nature, the Group's activities are principally related to the use of financial instruments including derivatives. The Group accepts deposits from customers at both fixed and floating rates for various periods, and seeks to earn interest margins by investing these funds in assets. The Group seeks to improve these margins by consolidating short-term funds and lending for longer periods at higher rates, while maintaining sufficient liquidity to meet all claims that might fall due.

Fair value hedges

The Group hedges part of its existing interest rate and foreign currency risk, resulting from potential movements in the fair value of fixed rate assets and liabilities, attributable to both interest rate and foreign currency risk using interest rate and cross currency swaps. The net fair value of these swaps is disclosed in note 14. There were no transactions for which fair value hedge accounting had to be discontinued in the year.

Cash flow hedges

The Group hedges a portion of the variability in future cash flows attributable to interest rate and foreign currency risk arising from variable interest rate assets and liabilities using cross currency and interest rate swaps. There were no transactions for which cash flow hedge accounting had to be discontinued in the year as a result of the highly probable cash flows no longer being expected to occur. The fair value of derivatives entered into is also disclosed in note 14.

Credit risk

Credit risk is inherent within any transaction that creates an actual or potential obligation for a borrower to pay the Group.

The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral, corporate, and personal guarantees where appropriate.

Derivatives

The Group maintains control limits on net open derivative positions (i.e. the difference between purchase and sale contracts), by both amount and term. 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 exposure is managed as part of the overall lending limits with customers, 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, the credit risk associated with the favourable contracts is reduced by a master netting arrangement to the extent that if a 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.

38. Financial risk management (continued)

Credit risk (continued)

Credit-related commitments

Credit-related commitments are facilities where the Group is under a legal obligation to extend credit unless some event occurs, which gives the Group the right, in terms of the commitment letter of offer or other documentation, to withdraw or suspend the facilities. The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry similar credit risk to loans.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss of an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. In the event of a deterioration of a customer's circumstances lending can often be withdrawn. The Group monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

Forbearance

Identification and classification

Forbearance is considered to take place when the Group grants concessions to assist customers who are experiencing, or who are about to experience, difficulties in meeting their financial commitments to the Group.

A concession refers to either of the following actions:

- a modification of the previous terms and conditions of a debt; and/or
- a total or partial refinancing of a contract.

Typically, concessions will include the granting of more favourable terms and conditions than those provided either at drawdown of the facility or which would not ordinarily be available to others with a similar risk profile. Loans that have been renegotiated and/or restructured for solely commercial reasons, where there is no financial difficulty are not treated as forborne.

In the current period, the Group has implemented revised forbearance policies and definitions in order to align the reporting of forbearance with the guidance established by the European Banking Authority ("EBA") for FINREP reporting which first applies on 30 September 2014. Comparative forbearance disclosures for the prior period which are presented in this note have not been restated following the policy change. In order to aid comparability with the prior year, the Group has chosen to present the current year forbearance tables for retail mortgage lending and non-retail on both a current policy and a historic policy basis. The revised policies and definitions include an extension to the minimum period after which loans can exit forborne status (to two years), resulting in a number of loans which would have previously been deemed to have exited forbearance being brought into scope for disclosure. Where there are significant variances in forborne exposures as a result of the changes in policy, further details are provided in the footnotes to the tables in this note.

The Group recognises that forbearance alone is not necessarily an indicator of impaired status but is a trigger for the review of the customer's credit profile. The Group grants forbearance when it believes that there is a realistic prospect of the customer continuing to be able to repay all facilities in full. If there is any concern over future cash flows and the Group incurring a loss, then forborne loans will also be classified as impaired in accordance with the Group's impairment policy.

38. Financial risk management (continued)

Credit risk (continued)

Forbearance (continued)

Identification and classification (continued)

Depending on circumstances and when operated within robust parameters and controls, the Group believes forbearance can help support the customer in the short to medium-term.

A range of parameters are considered when the Group looks to identify those customers to whom forbearance would be applicable and these parameters are regularly reviewed and refined as necessary to ensure they are consistent with the latest industry guidance and prevailing practice as well as ensuring that they adequately capture and reflect the most recent customer behaviours and market conditions. The Group continues to make every effort to follow its principles of treating customers fairly and aligns its forbearance practices to those principles.

The Group operates a range of forbearance measures depending on the type of customer and exercises forbearance in two distinct areas: retail and non-retail.

Exit from forbearance

Exposures classified as forborne and performing at the date forbearance measures are granted, continue to be reported as subject to forbearance for a minimum period of two years from that date (the 'probation period').

In addition, each of the following requirements need to be met at the end of the two year probation period referred to above for the exposure to exit from being classified as forborne:

- none of the exposures to the customer are more than 30 days past due at the end of the probation period; and
- regular payments of more than an insignificant aggregate amount of principal or interest have been made during at least half of the probation period. This assessment is based on the forbearance terms for repayment.

When the conditions are not met at the end of the probation period, the exposure shall continue to be identified as a performing forborne exposure until all of the conditions are met.

Exposures classified as forborne and which are non-performing when, or after, customers were granted forbearance cannot exit non-performing status for a minimum of twelve months from the date forbearance was granted, and cannot exit forbearance status for a further two years from the date of returning to performing status (three years in total).

Retail forbearance

Forbearance may be extended to retail customers (primarily on residential mortgages) when they have been identified as experiencing, or are about to experience, difficulties in meeting their financial commitments to the Group. The Group makes every effort to work with customers in times of financial difficulty in order to find a solution that brings customer facilities back into a sustainable position which, for residential mortgages, also means keeping customers in their homes.

Forbearance is exercised on retail customers in a number of different ways and is specific to the individual customer and their circumstances. Customers may potentially be subject to more than one forbearance strategy at any one time where this is considered to be the most appropriate course of action. The Group has implemented appropriate policies and procedures to ensure consistent application of forbearance. The operation, maintenance and governance surrounding these policies are regularly reviewed to confirm they remain relevant, appropriate and, most importantly, of value to our retail customers who have been identified as requiring forbearance.

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38. Financial risk management (continued)

Credit risk (continued)

Forbearance (continued)

Retail forbearance (continued)

At an operational level, the majority of forbearance measures are granted by Mortgage Collections who seek to negotiate positive outcomes for customers who have fallen into arrears. Forbearance is also exercised from within a dedicated Financial Management and Customer Solutions Team (FMCST), part of whose remit is to assist retail customers in financial difficulty to manage their finances more effectively on a case by case basis. The support provided by FMCST is tailored specifically for individual customers and includes an income and expenditure assessment along with other relevant financial management support.

The Group classifies the forbearance measures offered to retail customers into the following categories:

Formal arrangements: A permanent change which could include capitalisation of arrears, or arrangement with the customer to repay arrears over a shorter period than capitalisation would involve;

Temporary arrangements: Short term measures that allow a period of relief for customers in financial difficulty, these can include short-term payment holidays;

Interest only conversion: A permanent or temporary conversion to interest only repayments, allowing the customer to maintain payments with the intention that the capital balance outstanding would be recovered at the end of the term;

Term extension: A permanent change to the loan term allowing the customer to make lower repayments whilst still repaying the outstanding balance in full, over a longer period;

Other: A segment of forbearance exposures specifically dealt with through FMCST, which includes product switches;

Legal: Court mandated forbearance exposures;

Where the Group has made a demand for repayment, the customers facilities have been withdrawn or where a debt repayment process has been initiated, the exposure is classified as forborne if the debt is subject to any of the forbearance concessions above.

Forbearance measures including formal arrangements and temporary arrangements, are exercised within Mortgage Collections, while other tools such as conversion to interest only payments, term extensions and other arrangements are part of the suite of forbearance available from FMCST.

Retail forbearance - Mortgage lending

The tables below summarise the number of arrangements in place and the loan balances and impairment provisions associated with those arrangements. The Group reports retail forbearance at the exposure level. Where a customer is subject to more than one forbearance measure, they have been categorised into the primary method of forbearance:

38. Financial risk management (continued)

Credit risk (continued)

Forbearance (continued)

Retail forbearance (continued)

As at 30 September 2014 – Current policy basis [1] [2]

	Total loans and advances subject to forbearance measures			Impairment allowance on loans and advances subject to forbearance measures	
	Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance £m	Coverage %
Formal arrangements	2,282	189	1.03	3.7	1.97
Temporary arrangements	581	49	0.27	1.1	2.24
Interest only conversion	40	7	0.04	-	0.02
Term extension	72	6	0.03	-	0.03
Other	6	1	-	-	0.61
Legal	221	25	0.14	2.0	7.90
	3,202	277	1.51	6.8	2.46

As at 30 September 2014 – Historic policy basis [3]

	Total loans and advances subject to forbearance measures			Impairment allowance on loans and advances subject to forbearance measures	
	Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance £m	Coverage %
Formal arrangements	500	37	0.20	0.4	1.13
Temporary arrangements	175	18	0.10	0.1	0.57
Interest only conversion	28	6	0.03	-	0.01
Term extension	49	4	0.02	-	0.04
	752	65	0.35	0.5	0.80

38. Financial risk management (continued)

Credit risk (continued)

Forbearance (continued)

Retail forbearance (continued)

As at 30 September 2013 [(3)] [(4)]

	Total loans and advances subject to forbearance measures			Impairment allowance on loans and advances subject to forbearance measures	
	Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance £m	Coverage %
Formal arrangements	585	41	0.26	1.0	2.44
Temporary arrangements	173	15	0.09	-	-
Interest only conversion	12	1	0.01	-	-
Term extension	26	2	0.01	-	-
Other	6	-	-	-	-
	802	59	0.37	1.0	1.69

(1) All forbearance is reported as at the balance sheet date.

(2) The revised exit criteria introduced as part of the EBA's FINREP reporting guidance and stated in the 'Exit from forbearance' section above has been applied retrospectively.

(3) Under the historic policy forborne loans dealt with by Mortgage Collections were deemed to exit forborne status immediately after forbearance measures ceased to apply, where formal arrangements have been broken by the customer, those loans continue to be reported as forbearance until they are removed from the arrangement classes. Forbearance provided by FMCST reflected only those exposures where forbearance was granted within that reporting period.

(4) Not restated.

The key change in the Group's forbearance policy for retail customers between current policy basis and historic policy basis is the exit criteria. The current policy basis retrospectively applies the minimum two year exit criteria stated in the 'Exit from Forbearance' section of this note. Under the historic policy basis, forborne loans dealt with by Mortgage Collections were deemed to exit forborne status immediately after forbearance measures ceased to apply and forbearance provided by FMCST reflected only those exposures where forbearance was granted within that reporting period.

38. Financial risk management (continued)

Credit risk (continued)

Forbearance (continued)

Retail forbearance (continued)

The change in forbearance policy is the significant factor in the increase in the value of forborne balances disclosed. Using the Bank's historic policy, the level of forborne retail mortgage assets increased by £6m or 10.17%.

The Group also has a number of customers with interest only mortgages past maturity, not subject to forbearance. The Group has formal processes embedded to pro-actively track and facilitate pre-maturity customer engagement to bring the cases to a formal conclusion which is generally aimed to be achieved within six months after the loan has reached maturity. Complex cases can take longer than this to reach conclusion. At 30 September 2014, the Group had 162 (2013: 210) customers with interest only mortgages not subject to forbearance and which were post six month maturity with a total value of £20m (2013: £29m).

A further forbearance reserve of £4m (2013: £4m) is presently held within the overall collective provision. The effect of this on the above tables would be to increase the impairment allowance noted above to £11m and to increase overall coverage to 4.0%.

When all other avenues of resolution including forbearance have been explored the Group will take steps to repossess and sell underlying collateral. In the period to 30 September 2014 there were 155 repossessions of which 53 were voluntary (2013: 174 including 39 voluntary).

Retail forbearance – consumer credit

The Group currently exercises limited forbearance strategies in relation to other types of consumer credit, including money transmission accounts, unsecured loans and credit cards. Forbearance strategies implemented on consumer credit are of low financial significance in the context of the Group's overall lending operations. The Group reports consumer credit forbearance at the exposure level.

The group has assessed the total loan balances subject to forbearance on other types of consumer credit to be £22m at 30 September 2014 (2013: £31m), representing 1.87% of the total portfolio (2013: 2.65%). Impairment provisions on forborne balances totalled £6m at 30 September 2014 (2013: £8m), providing overall coverage of 27.03% (2013: 25.33%).

38. Financial risk management (continued)

Credit risk (continued)

Forbearance (continued)

Non-retail forbearance

Forbearance may be extended to non-retail customers for reasons relating to the actual, or apparent, financial stress of the customer or when they have been identified as experiencing, or are about to experience, difficulties in meeting their financial commitments to the Group. Authority to grant forbearance measures for non-retail customers is held by the Group's Strategic Business Services unit and is exercised, where appropriate, on the basis of detailed consideration of a customer's financial position and prospects.

The Group reports non-retail forbearance at a customer level, with customers that have forbearance granted on one or more facilities recorded as a single customer, but at a value which incorporates all facilities and the related impairment allowance irrespective of whether each individual facility is subject to forbearance. Where a customer is part of a larger group, forbearance is exercised and reported across the group at the individual entity level. Forbearance is considered to exist where one or more of the following occurs, on a non-commercial basis, for reasons relating to the actual or apparent stress of a customer:

- *Term extension* - Extending of loan facility payment term or the term of an overdraft which is not fluctuating (e.g. where a Term Loan has matured and the balance passed to an overdraft which is then extended on a non-commercial basis, then forbearance is considered to exist).
- *Deferral of contracted capital repayments* – Includes capital repayment holiday, conversion to interest only for an extended period, or rescheduling, but still repaying within the remaining contracted term.
- *Reduction in the contracted interest rate* – Includes a reduction in the level of accrued interest or amendment to original fee structure.
- *Alternative forms of payment* - Including debt for equity, asset transfer and repayment made by taking possession of collateral.
- *Debt forgiveness* – Total or partial debt forgiveness by write-off of the debt.
- *Refinancing* - A complete or partial repayment of a loan with a new contract granted on or up to 3 months after the day when the original contract expires. In the case of partial repayment both the original and new loans shall be classified as forborne.

Where the Group has made a demand for repayment, where the customers facilities have been withdrawn or where a debt repayment process has been initiated this will be classified as forbearance if the debt is subject to any of the forbearance concessions above.

Where modification of the terms and conditions of an exposure meeting the criteria for classification as forbearance results in derecognition of loans and advances from the balance sheet and the recognition of a new exposure, the new exposure shall be treated as forborne.

38. Financial risk management (continued)

Credit risk (continued)

Forbearance (continued)

Non-retail forbearance (continued)

The tables below summarise the total number of arrangements in place and the loan balances and impairment provisions associated with those arrangements. Where a customer is subject to more than one forbearance measure, they have been categorised into the primary method of forbearance:

As at 30 September 2014 – Current policy basis [1] [2]

	Total loans and advances subject to forbearance measures			Impairment allowance on loans and advances subject to forbearance measures	
	Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance £m	Coverage %
Term extension	**491**	**387**	**4.78**	**44.2**	**11.43**
Deferral of contracted capital repayments	**158**	**198**	**2.44**	**37.4**	**18.90**
Reduction in contracted interest rate	**22**	**16**	**0.20**	**3.4**	**20.97**
Alternative forms of payment	**11**	**27**	**0.33**	**12.7**	**47.07**
Debt forgiveness	**32**	**73**	**0.90**	**18.6**	**25.59**
Refinancing	**41**	**29**	**0.36**	**1.7**	**5.78**
	755	**730**	**9.01**	**118.0**	**16.17**

As at 30 September 2014 – Historic Policy basis [1] [3]

	Total loans and advances subject to forbearance measures			Impairment allowance on loans and advances subject to forbearance measures	
	Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance £m	Coverage %
Term extension	296	292	3.61	35.3	12.08
Deferral of contracted capital repayments	71	130	1.61	28.1	21.53
Reduction in contracted interest rate	11	11	0.14	1.0	9.05
Alternative forms of payment	7	24	0.29	9.5	40.10
Debt forgiveness	18	64	0.80	16.6	25.74
	403	521	6.45	90.5	17.34

38. Financial risk management (continued)

Credit risk (continued)

Forbearance (continued)

Non-retail forbearance (continued)

As at 30 September 2013 (1) (3) (5)

	Total loans and advances subject to forbearance measures			Impairment allowance on loans and advances subject to forbearance measures	
	Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance £m	Coverage %
Term extension	281	220	2.41	21.9	10.00
Deferral of contracted capital repayments	112	144	1.58	28.6	20.14
Reduction in contracted interest rate	7	6	0.07	2.0	33.33
Alternative forms of payment	7	43	0.47	8.6	20.93
Debt forgiveness	16	34	0.37	6.8	20.59
	423	447	4.90	67.9	15.44

(1) All forbearance is reported at the balance sheet date.

(2) The revised 2 year exit criteria introduced as part of the EBA's FINREP reporting guidance and stated in the 'Exit from forbearance' section above in the note has been applied retrospectively.

(3) Forborne loans were deemed to exit forborne status immediately after forbearance measures ceased to apply.

(4) Where the Group has made a demand for repayment, where the customers facilities have been withdrawn or a debt repayment process initiated this will be classified as forbearance if the debt is subject to any of the forbearance concessions above. In 2013, amounts meeting these criteria were not classified as subject to forbearance but were included within defaulted assets.

(5) Not restated.

The key changes in forbearance policy for non-retail customers between the current policy basis and historic policy basis are shown below:

- The current policy basis exit criteria stated in this note have been applied retrospectively for the current period. Under the historic policy, forborne loans were deemed to exit forborne status immediately after forbearance measures ceased to apply.

- Under the current policy, where the Group has made a demand for repayment and where the customers facilities have been withdrawn and a debt repayment process initiated, this will be classified as forbearance if the debt is subject to any of the forbearance concessions above. Under the historic policy, exposures meeting these criteria were not classified as subject to forbearance, but solely as defaulted assets.

The change in forbearance policy is the significant factor in the increase in the value of forborne balances disclosed. Using the Bank's historic policy, the level of forborne non-retail assets increased by £74m or 16.6%.

Included in other financial assets at fair value is a portfolio of loans which are included in the above table. The value of fair value loans subject to forbearance at 30 September 2014 is £133m (2013: £55m), representing 1.65 % of the total non-retail portfolio (2013: 0.60%). Impairment allowances on these amounts totalled £28.9m (2013: £15m), a coverage of 21.69 % (2013: 26.34%).

38. Financial risk management (continued)

Credit risk (continued)

Forbearance (continued)

Non-retail forbearance (continued)

The Group has identified a number of situations that in isolation are not considered to be forbearance:

- The waiver of a financial covenant breach, or amendment to the terms of a financial covenant. Typically, financial covenants are set at levels where the ability to repay has yet to be adversely affected but permit rights of action at an earlier stage of credit deterioration. They are designed to allow the Group time to work with the customer to develop and agree solutions which are effective and appropriate to both the Group and the customer. Where financial covenant breaches have occurred which could imply that the customer is in financial difficulty, normal impaired asset review procedures are followed.
- Facilities that have been temporarily extended pending review and no concession has been granted for reasons relating to the actual or apparent financial stress of a customer.
- A reduction in asset quality to a level where actual, or apparent, financial stress is not evident.
- Where changes are made to the terms of a borrower's interest structure or repayment arrangement on a commercial basis.

Maximum exposure to credit risk

The Group has comprehensive credit risk management policies that restrict the level of exposure to any one borrower or group of borrowers, industries and countries. Unless otherwise noted, the amount that best represents the maximum credit exposure at the reporting date is the carrying value of the financial asset.

The table below shows the maximum exposure to credit risk for the components of the balance sheet, including derivatives. The maximum exposure is shown gross, before the effect of mitigation through use of master netting and collateral agreements. The table also shows the maximum amount of commitments from its banking operations.

	Group		Bank	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Cash and balances with central banks (note 10)	**5,971**	6,715	**5,971**	6,715
Due from related entities (note 11)	**1,495**	1,417	**3,010**	5,979
Due from other banks	**13**	184	**13**	184
Investments – available for sale (note 12)	**1,168**	975	**1,168**	975
Investments – held to maturity (note 12)	**-**	-	**1,483**	1,415
Other financial assets at fair value (note 13)	**1,583**	2,171	**1,583**	2,171
Derivative financial assets (note 14)	**220**	244	**220**	244
Loans and advances to customers (note 15)	**25,901**	23,960	**24,450**	19,438
Due from customers on acceptances	**5**	4	**5**	4
	36,356	35,670	**37,903**	37,125
Contingent liabilities (note 32)	**136**	213	**136**	213
Other credit commitments (note 32)	**8,463**	8,696	**8,424**	8,664
Maximum credit risk exposure	**44,955**	44,579	**46,463**	46,002

38. Financial risk management (continued)

Credit risk (continued)

Offsetting of financial assets and liabilities

The table below illustrates the amounts for financial instruments that have been offset on the balance sheet and also those amounts that are covered by enforceable netting arrangements (i.e. offsetting agreements and any related financial collateral). The table excludes financial instruments not subject to offset and that are only subject to collateral arrangements (e.g. Loans and advances).

The "net amounts" presented in the table are not intended to represent the Group's exposure to credit risk, as the Group will use a wide range of strategies to mitigate credit risk in addition to netting and collateral.

The offsetting and collateral arrangements and other credit risk mitigation strategies are further explained in the following sections of this note.

2014

	Amounts subject to enforceable netting arrangements						
	Effect of offsetting on balance sheet			Related amounts not offset			
Group	Gross amount £m	Amount offset £m	Net amount reported on balance sheet £m	Financial instruments (1) (2) (3) £m	Cash collateral (2) (3) £m	Net amount £m	Amounts not subject to enforceable netting arrangements £m
Assets							
Derivative financial instruments (4)	88	-	88	(88)	-	-	132
Liabilities							
Derivative financial instruments (4)	522	-	522	(88)	(317)	117	26
Securities sold under repurchase agreements (5)	644	-	644	(644)	-	-	-
Total liabilities	1,166	-	1,166	(732)	(317)	117	26

38. Financial risk management (continued)

Credit risk (continued)

Offsetting of financial assets and liabilities (continued)

2013

Group	Amounts subject to enforceable netting arrangements: Effect of offsetting on balance sheet: Gross amount £m	Amount offset £m	Net amount reported on balance sheet £m	Related amounts not offset: Financial instruments (1) (2) (3) £m	Cash collateral (2) (3) £m	Net amount £m	Amounts not subject to enforceable netting arrangements £m
Assets							
Derivative financial instruments (4)	103	-	103	(103)	-	-	141
Liabilities							
Derivative financial instruments (4)	615	-	615	(103)	(408)	104	36

2014

Bank	**Amounts subject to enforceable netting arrangements: Effect of offsetting on balance sheet: Gross amount £m**	**Amount offset £m**	**Net amount reported on balance sheet £m**	**Related amounts not offset: Financial instruments (1) (2) (3) £m**	**Cash collateral (2) (3) £m**	**Net amount £m**	**Amounts not subject to enforceable netting arrangements £m**
Assets							
Derivative financial instruments (4)	88	-	88	(88)	-	-	132
Total assets	**88**	**-**	**88**	**(88)**	**-**	**-**	**132**
Liabilities							
Derivative financial instruments (4)	426	-	426	(88)	(317)	21	25
Securities sold under repurchase agreements (5)	644	-	644	(644)	-	-	-
Total liabilities	**1,070**	**-**	**1,070**	**(732)**	**(317)**	**21**	**25**

38. Financial risk management (continued)

Credit risk (continued)

Offsetting of financial assets and liabilities (continued)

2013

Bank	Amounts subject to enforceable netting arrangements: Effect of offsetting on balance sheet			Related amounts not offset			Amounts not subject to enforceable netting arrangements
	Gross amount £m	Amount offset £m	Net amount reported on balance sheet £m	Financial instruments (1) (2) (3) £m	Cash collateral (2) (3) £m	Net amount £m	£m
Assets							
Derivative financial instruments (4)	103	-	103	(103)	-	-	141
Liabilities							
Derivative financial instruments (4)	531	-	531	(103)	(408)	20	35

(1) Financial instruments includes both recognised financial instruments and unrecognised financial instruments (i.e. non-cash collateral).

(2) Amounts relate to master netting and collateral agreements which have been determined to be legally enforceable but do not meet all criteria required for net presentation within the consolidated statement of financial position.

(3) Collateral amounts (cash and non-cash financial collateral) are reflected at their fair value; however this amount is limited to the net balance sheet exposure in order not to include any over-collateralisation.

(4) Derivative financial instruments comprise of both trading and hedging derivative assets and liabilities.

(5) Securities sold under repurchase agreements are reported on the Group and Bank's balance sheet within due to other banks.

Derivative assets and liabilities

Derivative financial instrument contracts are typically subject to 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, or derivative exchange or clearing counterparty agreements if contracts are settled via an exchange or clearing house. The amounts included in the Financial Instruments column refer to amounts that are subject to relevant close out netting arrangements under a relevant ISDA agreement.

Repurchase agreements

Repurchase agreements will typically be subject to Global Master Repurchase Agreements (GMRAs) or similar agreements whereby all outstanding transactions with the same counterparty can be offset and closed out upon a default or insolvency event (i.e. close out netting).

Where the Group has a right of offset on default or insolvency only, the related financial instruments comprise of highly liquid securities pledged, which can be realised in the event of a default or insolvency by the counterparty.

38. Financial risk management (continued)

Credit quality of financial assets

An assessment of the credit quality of loans and advances to customers can be found in note 15 with an assessment of the credit quality of investments contained in note 12.

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 in an orderly fashion. The proceeds are used to reduce or repay the outstanding claim. 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 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 business rules and confidence levels. The loan to value ratio of our mortgage portfolio is disclosed in note 15.

Commercial property

Commercial property is the Group's main source of collateral on commercial lending and means of mitigating loss in the event of default credit risk inherent in its commercial portfolios. 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

Apart from Residential and Commercial Property based security, the Group also takes other forms of collateral when lending and 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.

38. Financial risk management (continued)

Collateral held as security and other credit enhancements (continued)

Non-property related collateral (continued)

The following table shows the total non-property collateral held at 30 September 2014 in terms of cash, guarantees (these guarantors are predominantly other financial institutions who are considered to be of a high quality) and netting. The exposure amount shown below is the total gross exposure (before any Credit Risk Mitigation and Credit Conversion Factors have been applied where applicable) for arrangements which have some form of associated collateral held against them and is not the total exposure for each asset class, as disclosed in the Strategic Report.

	Cash £m	Guarantee £m	Netting £m	Total £m	Exposure £m
Central Governments or Central Banks	49	-	-	49	51
Corporates	88	-	80	168	230
Institutions	910	68	-	978	1,034
Past Due Items	1	-	1	2	13
Regional Governments or Local Authorites	-	-	138	138	144
Secured by Mortgages on Commercial Real Estate	35	-	34	69	165
Secured by Mortgages on Residential Property	5	-	7	12	33
	1,088	**68**	**260**	**1,416**	**1,670**

Corporates is the largest sector for other risk mitigation techniques, with all three methods utilised dependent on credit quality. The extent to which these will be used will be dependent on the specific circumstances of the customer.

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 limit exposure to a single entity/counterparty.

Eurozone risk

The Group and Bank have no material operations outside the UK and have no direct sovereign exposure to any Eurozone countries (2013: Nil). The Group and Bank had an exposure to the European Investment Bank of £100m at 30 September 2014 (2013: £100m).

38. Financial risk management (continued)

Credit risk (continued)

Industry concentration of assets

The following tables show the levels of industry concentration of credit risk as at 30 September:

Gross loans and advances to customers including loans designated at fair value through profit or loss	Group 2014 £m	Group 2013 £m	Bank 2014 £m	Bank 2013 £m
Government and public authorities	55	35	55	35
Agriculture, forestry, fishing and mining	1,677	1,758	1,677	1,758
Financial, investment and insurance	421	553	421	553
Property – construction	394	516	394	516
Manufacturing	733	723	733	723
Instalment loans to individuals and other personal lending (including credit cards)	1,712	1,902	1,712	1,902
Property – mortgage	18,444	16,148	17,015	11,674
Asset and lease financing	417	482	394	428
Other commercial and industrial	3,851	4,319	3,851	4,319
	27,704	26,436	26,252	21,908

Contingent liabilities and credit related commitments	Group 2014 £m	Group 2013 £m	Bank 2014 £m	Bank 2013 £m
Government	8	-	8	-
Agriculture, forestry, fishing and mining	1,031	1,006	1,031	1,006
Financial, investment and insurance	44	56	44	56
Property – construction	75	98	75	98
Manufacturing	189	228	189	228
Instalment loans to individuals and other personal lending (including credit cards)	3,759	3,939	3,759	3,939
Property – mortgage	2,107	2,010	2,068	1,978
Other commercial and industrial	1,386	1,572	1,386	1,572
	8,599	8,909	8,560	8,877

38. Financial risk management (continued)

Credit risk (continued)

Available for sale and held to maturity investments	Group		Bank	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Government and public authorities	**1,161**	968	**1,161**	968
Financial, investment and insurance	**7**	7	**1,490**	1,422
	1,168	975	**2,651**	2,390

Comparative disclosures have been amended to conform with current year presentation.

Market risk

Market risk is the risk that movements in market factors, including foreign exchange rates, interest rates, credit spreads and equity prices, will reduce income or portfolio values.

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 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. These risks are managed to a de minimus risk position in accordance with the Bank's Trading Policy Statement.

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.

Interest rate risk in the banking book ("IRRBB")

IRRBB is measured, monitored, and managed from both an internal management and regulatory perspective. The risk management framework incorporates both market valuation and earnings based approaches in accordance with the NAB Group IRRBB policy. Risk measurement techniques include: 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:

- 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; three month holding period.
- Economic capital is allocated for IRRBB based on a higher confidence interval and a longer holding period.
- EaR utilises a twelve month forecast period.
- Eight years of business day historical data.
- VaR methodology is based on proportional rather than absolute changes in historical interest rates.
- Investment term for capital is modelled with an established benchmark term of between one and five years.
- Investment term for core "non-interest" bearing assets and liabilities is modelled on a behavioural basis with an established benchmark term of between one and five years.

38. Financial risk management (continued)

Market risk (continued)

Model parameters and assumptions are reviewed and updated on at least an annual basis. Material changes require the approval of UK Asset & Liability Committee ("UK ALCO").

Interest rate risk	Value at risk 2014 £m	Value at risk 2013 £m	Earnings at risk 2014 £m	Earnings at risk 2013 £m
As at 30 September	36	30	2	7
Average value during the year	37	32	3	9
Minimum value during the year	32	29	2	3
Maximum value during the year	48	35	8	20

The following table shows the Group's principal financial assets and liabilities and the main non-traded market risk types they are exposed to:

	2014 £m	Liquidity risk	Interest rate risk	Foreign exchange risk	Credit risk
Assets					
Cash and balances with central banks	5,971				✔
Available for sale investments	1,168	✔	✔		✔
Loans and advances to customers	25,901	✔	✔	✔	✔
Derivative financial instruments	220	✔	✔	✔	✔
Other financial assets at fair value	1,583	✔	✔		✔
Liabilities					
Due to customers	24,073	✔	✔	✔	
Due to other banks	914	✔	✔	✔	
Derivative financial instruments	548	✔	✔	✔	
Other financial liabilities at fair value	91	✔	✔		
Bonds and notes	3,453	✔	✔	✔	

Prepayment risk

Customers may prepay certain loans and advances ahead of the contractual repayment schedule. This form of optionality gives rise to prepayment risk for the Bank whereby the expected timing of cashflows from loan repayments differs from the actual experience. The impact on the Bank would differ according to changes in the level of interest rates.

The Group assesses the risks arising from prepayment behaviour in order to show the potential impact on future cashflows. The impact is also managed through terms and conditions within loans and advances.

38. Financial risk management (continued)

Maturity analysis of assets and liabilities

The following tables represent a breakdown of the Group's balance sheet according to the assets and liabilities contractual maturity. Many of the longer-term monetary assets are variable rate products, with actual maturities shorter than the contractual terms. Accordingly, this information is not relied upon by the Group in its management of interest rate risk.

The Group has disclosed certain term facilities with a revolving element at the maturity of the facility as this best reflects their contractual maturity.

Group 2014	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Assets							
Cash and balances with central banks	4,670	-	-	-	-	1,301	**5,971**
Due from related entities	1,495	-	-	-	-	-	**1,495**
Due from other banks	13	-	-	-	-	-	**13**
Investments – available for sale	-	2	1	101	1,058	6	**1,168**
Other financial assets at fair value	3	33	105	589	853	-	**1,583**
Derivative financial assets	2	29	59	47	83	-	**220**
Loans and advances to customers	2,519	293	769	4,063	17,893	364	**25,901**
Due from customers on acceptances	-	5	-	-	-	-	**5**
All other assets	143	70	33	-	-	481	**727**
Total assets	**8,845**	**432**	**967**	**4,800**	**19,887**	**2,152**	**37,083**
Liabilities							
Due to other banks	-	664	250	-	-	-	**914**
Other financial liabilities at fair value	-	2	6	65	18	-	**91**
Derivative financial liabilities	2	36	60	170	280	-	**548**
Due to customers	17,872	2,039	2,464	1,698	-	-	**24,073**
Liabilities on acceptances	-	5	-	-	-	-	**5**
Due to related entities	183	9	346	838	1,076	-	**2,452**
Bonds and notes	-	20	730	2,039	664	-	**3,453**
All other liabilities	1,888	130	42	-	-	982	**3,042**
Total liabilities	**19,945**	**2,905**	**3,898**	**4,810**	**2,038**	**982**	**34,578**
Off balance sheet items							
Contingent liabilities	-	32	25	12	61	6	**136**
Other credit commitments	8,463	-	-	-	-	-	**8,463**
Total off balance sheet items	**8,463**	**32**	**25**	**12**	**61**	**6**	**8,599**

38. Financial risk management (continued)

Maturity analysis of assets and liabilities (continued)

Group 2013 As restated	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Assets							
Cash and balances with central banks	5,508	-	-	-	-	1,207	6,715
Due from related entities	1,408	-	-	9	-	-	1,417
Due from other banks	19	100	65	-	-	-	184
Investments – available for sale	-	2	-	101	866	6	975
Other financial assets at fair value	11	87	242	530	1,301	-	2,171
Derivative financial assets	-	23	24	106	91	-	244
Loans and advances to customers	2,880	346	722	4,089	15,527	396	23,960
Due from customers on acceptances	-	4	-	-	-	-	4
All other assets	178	187	39	-	-	419	823
Total assets	10,004	749	1,092	4,835	17,785	2,028	36,493
Liabilities							
Due to other banks	-	484	37	-	-	-	521
Other financial liabilities at fair value	-	3	9	52	59	-	123
Derivative financial liabilities	1	54	53	184	359	-	651
Due to customers	16,659	2,656	2,515	2,525	-	-	24,355
Liabilities on acceptances	-	4	-	-	-	-	4
Due to related entities	496	61	-	1,227	1,076	-	2,860
Bonds and notes	-	14	-	2,429	642	-	3,085
All other liabilities	1,804	85	48	-	-	547	2,484
Total liabilities	18,960	3,361	2,662	6,417	2,136	547	34,083
Off balance sheet items							
Contingent liabilities	1	34	63	16	90	9	213
Other credit commitments	8,696	-	-	-	-	-	8,696
Total off balance sheet items	8,697	34	63	16	90	9	8,909

38. Financial risk management (continued)

Maturity analysis of assets and liabilities (continued)

Bank 2014	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Assets							
Cash and balances with central banks	4,670	-	-	-	-	1,301	**5,971**
Due from related entities	3,010	-	-	-	-	-	**3,010**
Due from other banks	13	-	-	-	-	-	**13**
Investments – available for sale	-	2	1	101	1,058	6	**1,168**
Investments – held to maturity	-	-	-	399	1,084	-	**1,483**
Other financial assets at fair value	3	33	105	589	853	-	**1,583**
Derivative financial assets	2	29	59	47	83	-	**220**
Loans and advances to customers	2,476	292	762	4,002	16,554	364	**24,450**
Due from customers on acceptances	-	5	-	-	-	-	**5**
All other assets	143	70	33	-	-	452	**698**
Total assets	**10,317**	**431**	**960**	**5,138**	**19,632**	**2,123**	**38,601**
Liabilities							
Due to other banks	-	664	250	-	-	-	**914**
Other financial liabilities at fair value	-	2	6	65	18	-	**91**
Derivative financial liabilities	2	18	36	145	250	-	**451**
Due to customers	17,872	2,039	2,464	1,698	-	-	**24,073**
Liabilities on acceptances	-	5	-	-	-	-	**5**
Due to related entities	217	9	346	4,816	1,077	-	**6,465**
Bonds and notes	-	11	-	399	698	-	**1,108**
All other liabilities	1,865	130	42	-	-	982	**3,019**
Total liabilities	**19,956**	**2,878**	**3,144**	**7,123**	**2,043**	**982**	**36,126**
Off balance sheet items							
Contingent liabilities	-	32	25	12	61	6	**136**
Other credit commitments	8,424	-	-	-	-	-	**8,424**
Total off balance sheet items	**8,424**	**32**	**25**	**12**	**61**	**6**	**8,560**

38. Financial risk management (continued)

Maturity analysis of assets and liabilities (continued)

Bank 2013 As restated	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Cash and balances with central banks	5,508	-	-	-	-	1,207	6,715
Due from related entities	5,970	-	-	9	-	-	5,979
Due from other banks	19	100	65	-	-	-	184
Investments – available for sale	-	2	-	101	866	6	975
Investments – held to maturity	-	-	-	332	1,083	-	1,415
Other financial assets at fair value	11	87	242	530	1,301	-	2,171
Derivative financial assets	-	23	24	106	91	-	244
Loans and advances to customers	2,647	326	708	3,874	11,487	396	19,438
Due from customers on acceptances	-	4	-	-	-	-	4
All other assets	178	183	236	-	-	779	1,376
Total assets	14,333	725	1,275	4,952	14,828	2,388	38,501
Liabilities							
Due to other banks	-	484	37	-	-	-	521
Other financial liabilities at fair value	-	3	9	52	59	-	123
Derivative financial liabilities	1	66	53	154	292	-	566
Due to customers	16,659	2,656	2,515	2,525	-	-	24,355
Liabilities on acceptances	-	4	-	-	-	-	4
Due to related entities	486	641	-	4,728	1,076	-	6,931
Bonds and notes	-	14	-	454	642	-	1,110
All other liabilities	1,804	126	48	-	-	528	2,506
Total liabilities	18,950	3,994	2,662	7,913	2,069	528	36,116
Off balance sheet items							
Contingent liabilities	1	34	63	16	90	9	213
Other credit commitments	8,664	-	-	-	-	-	8,664
Total off balance sheet items	8,665	34	63	16	90	9	8,877

Comparative disclosures have been amended to conform with current year presentation.

38. Financial risk management (continued)

Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with financial liabilities when they fall due. The Group manages liquidity and funding risk through a combination of positive cash flow management, the maintenance of portfolios containing high quality liquid assets, maintenance of a prudent funding strategy and diversification of its funding base. The Group undertakes a conservative approach by imposing internal limits, including stress and scenario testing that are in addition to regulatory requirements.

Cash flows payable under financial liabilities by contractual maturities

Group 2014	**Call £m**	**3 months or less £m**	**3 to 12 months £m**	**1 to 5 years £m**	**Over 5 years £m**	**No specified maturity £m**	**Total £m**
Due to other banks	-	665	250	-	-	-	**915**
Other financial liabilities at fair value	-	3	9	79	20	-	**111**
Derivative financial liabilities	2	36	24	74	275	-	**411**
Due to customers	17,873	2,050	2,487	1,721	-	-	**24,131**
Liabilities on acceptances	-	5	-	-	-	-	**5**
Bonds and notes	-	40	782	2,214	880	-	**3,916**
All other financial liabilities	1,504	-	-	-	-	-	**1,504**
Hedging derivatives							
Contractual amounts payable	-	85	481	840	34	-	**1,440**
Contractual amounts receivable	-	(55)	(429)	(705)	-	-	**(1,189)**
	19,379	**2,829**	**3,604**	**4,223**	**1,209**	**-**	**31,244**

Group 2013	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Due to other banks	-	484	37	-	-	-	521
Other financial liabilities at fair value	-	4	14	71	65	-	154
Derivative financial liabilities	1	54	53	107	340	-	555
Due to customers	16,659	2,667	2,553	2,559	-	-	24,438
Liabilities on acceptances	-	4	-	-	-	-	4
Bonds and notes	-	34	57	2,627	751	-	3,469
All other financial liabilities	1,344	-	-	-	-	-	1,344
Hedging derivatives							
Contractual amounts payable	-	66	172	1,109	78	-	1,425
Contractual amounts receivable	-	(59)	(173)	(1,002)	-	-	(1,234)
	18,004	3,254	2,713	5,471	1,234	-	30,676

38. Financial risk management (continued)

Liquidity risk (continued)

Bank 2014	**Call £m**	**3 months or less £m**	**3 to 12 months £m**	**1 to 5 years £m**	**Over 5 years £m**	**No specified maturity £m**	**Total £m**
Due to other banks	-	665	250	-	-	-	**915**
Other financial liabilities at fair value	-	3	9	79	20	-	**111**
Derivative financial liabilities	2	47	24	74	275	-	**422**
Due to customers	17,873	2,050	2,487	1,721	-	-	**24,131**
Liabilities on acceptances	-	5	-	-	-	-	**5**
Bonds and notes	-	21	28	530	917	-	**1,496**
All other financial liabilities	1,504	-	-	-	-	-	**1,504**
Hedging derivatives							
Contractual amounts payable	-	20	34	89	6	-	**149**
	19,379	**2,811**	**2,832**	**2,493**	**1,218**	**-**	**28,733**

Bank 2013	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Due to other banks	-	484	37	-	-	-	521
Other financial liabilities at fair value	-	4	14	71	65	-	154
Derivative financial liabilities	1	66	53	154	293	-	567
Due to customers	16,659	2,667	2,553	2,559	-	-	24,438
Liabilities on acceptances	-	4	-	-	-	-	4
Bonds and notes	-	24	31	536	949	-	1,540
All other financial liabilities	1,374	-	-	-	-	-	1,374
Hedging derivatives							
Contractual amounts payable	-	-	12	109	1	-	122
	18,034	3,249	2,700	3,429	1,308	-	28,720

The balances in the cash flow tables above will not agree directly to the balances in the consolidated balance sheet as the table incorporates all cash flows, on an undiscounted basis, related to both principal as well as those associated with all future coupon payments.

39. Management of risk

Effective management of risk is a key capability for a successful financial services provider and is fundamental to the Group's strategy, as well as that of its parent entity NAB. The key components of the Group's risk management strategy are detailed below:

Risk control and management

Risk culture

Establishing and maintaining an appropriate risk culture within the Group is a key objective. The 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 which aligns to, and supports, the strategic objectives of the Group. The Bank's strategic priorities refer to embedding a "strong risk culture in our people" and the Bank has also established a conduct strategy in which an explicit objective is to develop a "customer centric culture". Together, these provide guidance and support to staff on what is expected of them.

Further initiatives that support the appropriate risk culture include: messaging from the CEO and Executive Committee members; the Group's performance management framework which incorporates a balanced assessment of factors (including risk management, behaviour and a transparent compliance gateway assessment); training; and escalation procedures (both through the management hierarchy or anonymously through the Group's whistle-blower facility) allowing staff to raise concerns quickly and appropriately.

Underpinning the risk management operating model, and at the heart of the Group's risk culture, is the notion of personal accountability for risk management at source. This is enabled through a risk management accountability model (which articulates specific accountabilities for core elements of risk management across the Group) and a formal delegation framework through which staff are able to make risk based decisions.

Strategic planning and risk appetite

The Board have established a formal Risk Appetite Statement ("RAS"). This places an overall limit on the total amount and types of risk that the Group is prepared to take. This is set with respect to the returns that the Group is seeking to provide to its shareholder, the credit rating that the Bank is seeking to maintain and the Group's capital position and desired capital ratios.

This informs the Group's risk, capital and business limits and policies. It is regularly reviewed by the Board as a part of the strategic planning process, or otherwise as the commercial circumstances of the Group change.

Risk Management Framework

The Group's approach to risk management is based on an overriding principle that risk management capability must be embedded within the businesses' front-line teams to be effective. This overriding principle embodies the following concepts:

- all business decisions proactively consider risk and the impact on the Group's customers;
- business managers use the Risk Management Framework which assists in the appropriate balancing of both the risk and reward components; and
- all employees are responsible for risk management in their day-to-day activities.

Within this context, the Group manages risk within a "three lines of defence" framework. Control is exercised through clearly defined delegation of authority, with clear and rapid communication and escalation channels throughout the organisation. The first line of defence comprises the business units managing the risks associated with their activities. The second line encompasses dedicated risk functions who are accountable for establishing risk policy, standards and the oversight of risk management effectiveness within the business. The third line of defence is Internal Audit who are responsible for independently reviewing, monitoring, and testing business unit compliance and regularly assessing the overall effectiveness of the Risk Management Framework.

39. Management of risk (continued)

Risk control and management (continued)

Risk Governance

The Group's risk governance structure strengthens risk evaluation and management, while also positioning the Group to manage the changing regulatory environment in an efficient and effective manner.

The NAB Group Risk and Reward Management Committee, chaired by the NAB Group Chief Executive Officer, serves as the principal risk strategy and policy decision making body within the NAB Group, and provides the Principal Board with assurance on the performance of the overall Risk Management Framework. This Committee is supported by three sub-committees - the NAB Group Credit Risk Committee, the NAB Group Asset and Liability Committee, and the NAB Group Capital Committee - each with a specialised focus.

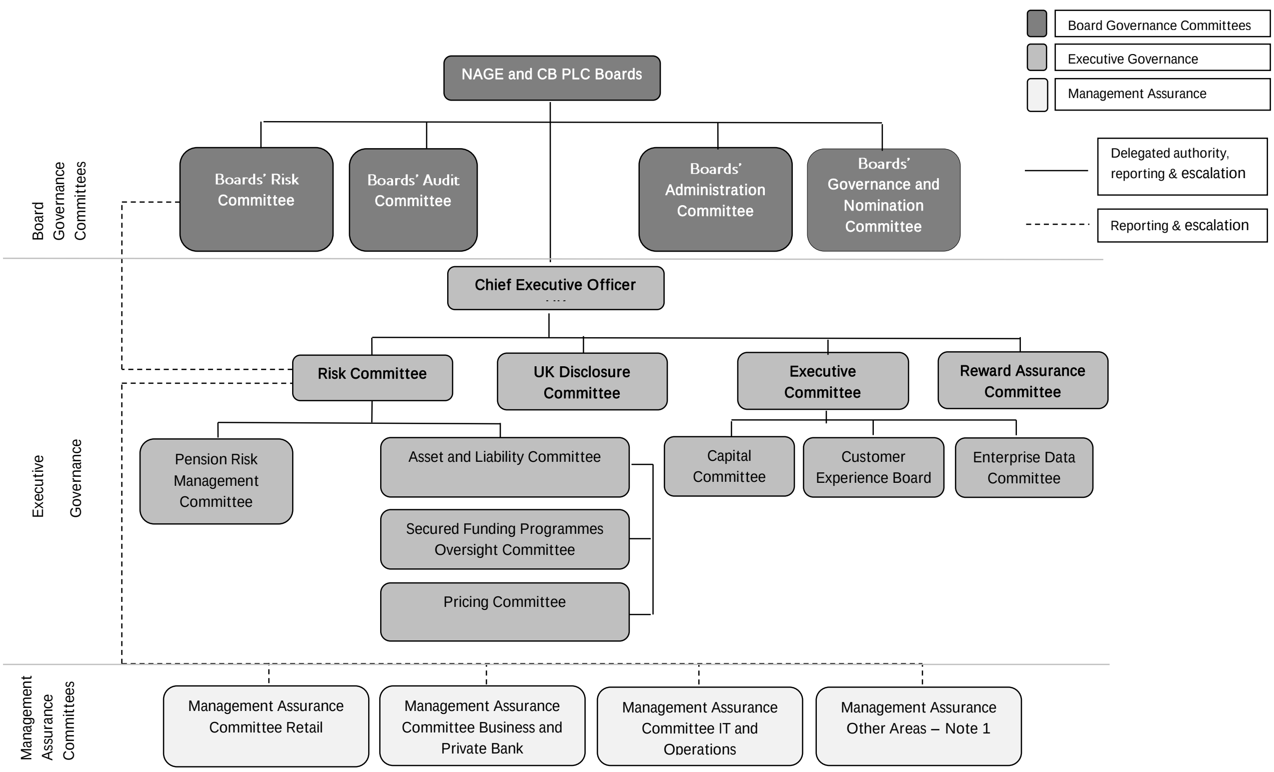
Within the UK, Board oversight of risk management is facilitated by the Boards' Risk and Audit Committees, the Boards approve the Group's overall governance, risk and control frameworks and risk appetite. Refer to the Group's Corporate Governance statement on the Group's website (www.cbonline.co.uk) for further information on Board committees. The table below details the Bank's Executive and Management Assurance Commitees and their risk focus.

The following Executive Governance Committees have been established under the authority of the Chief Executive Officer UK (CEO)	
Committees	**Risk Focus**
Risk Committee	The UK Risk Committee (UKRC) supports the CEO in respect of his risk and control accountabilities and serves to provide leadership focus on key risk issues including: • Devising the Risk Appetite Statement for approval by the Boards; • Overseeing and challenging the enterprise wide risk performance and control environment of the Bank and business units, including the effective use of policy, frameworks and tools; • Monitoring the status of regulatory relationships, the reputation of the Bank in relation to its regulators and the changing state of the regulatory landscape including the impacts for and readiness of the Bank; • 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 Bank.
UK Disclosure Committee	The UK Disclosure Committee is responsible for ensuring the Group complies with its continuous disclosure obligations as a subsidiary of National Australia Bank Limited (NAB) under the rules of the Australian Securities Exchange in relation to NAB securities and in relation to debt securities listed on the London, Luxembourg and Channel Islands stock exchanges.
Executive Committee	The UK Executive Committee supports the CEO UK to lead the Bank to be a strong, customer focused bank for our communities by focusing on four business priorities; Customer, Risk and Control, Sustainable Returns and People.
Reward Assurance Committee	The Reward Assurance Committee provides oversight of the application of NAB Group remuneration policies and frameworks in the Bank.
The Risk Committee is supported by	
Pension Risk Management Committee	The Pension Risk Management Committee is responsible for overseeing pension risk management and strategy. This committee also oversees and governs interaction with UK pension scheme trustees.
Asset and Liability Committee	Responsible for monitoring the performance of the Bank against the Boards' approved Capital and Funding Plans. The committee focuses on the Bank's non-traded market risks including capital, funding, liquidity, interest rate risk and pension risk to ensure that the Bank's activity complies with regulatory and corporate governance requirements and also delivers Group policy objectives.
Pricing Committee	The Pricing Committee is responsible for managing pricing decisions in relation to business lending, retail lending and deposits.
The Executive Committee is supported by	
Capital Committee	The Capital Committee is responsible for ensuring effective governance of UK capital usage and performance. This includes monitoring key capital and related performance metrics; development of infrastructure to deliver key capital measures out to business functions; and optimising capital efficiencies.
Customer Experience Board	The Customer Experience Board is responsible for championing the end to end customer experience ensuring appropriate and consistent execution, whilst ensuring Treating Customers Fairly principles are adhered to.
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.
First line responsibility for risk management resides with Management Assurance Committees which provide reports to the UKRC and Boards Risk committees	
Management Assurance Committee (Retail; Business and Private Bank; IT & Operations; Other Areas)	Each major business unit has established a Management Assurance Committee, which supports the business unit Director to lead the business unit in respect of risk matters and provides advice, guidance, challenge and recommendations. This includes recommending the business unit Risk Appetite Statement to the UKRC; monitoring performance against risk settings and tolerances; reviewing the strength of the control environment and risk capability; and monitoring the effectiveness of risk culture and on-going compliance with regulatory requirements.

39. Management of risk (continued)

Risk control and management (continued)

The Group's risk management structure is diagrammatically represented below:



Note 1: for other business areas the responsibilities of the Management Assurance Committee will be discharged through either existing Leadership Team or Management Fora focussing on risk.

The UK Risk Management team independently monitors and systematically assesses the risk profile within the Group against established risk appetite parameters. They also assist the front line business units in the design and implementation of appropriate risk management policies and strategies and work with the business units to promote awareness of the need to manage risk.

Stress testing within the Group's risk governance and capital framework

Stress testing within the Group has been developed to inform future business and risk planning initiatives, strategic risk management (including Risk Appetite setting) and capital management. Specifically, stress testing is used or considered in informing the following management decisions:

Risk appetite and strategic business planning - As part of an annual assessment of future opportunities for, and threats to, the Group, stress testing outputs are used to inform the strategic planning process and to develop risk posture and risk appetite settings.

Capital planning ("ICAAP") - Stress testing informs the assessment and quantification of risk exposures in the course of calculating capital requirements as part of the ICAAP process.

Liquidity management ("ILAA") - Scenarios provide insight into potential vulnerabilities in the Group's funding strategies and leverage profile. Regular stress tests are undertaken to understand and monitor exposure to liquidity risk with their regularity being aligned to the nature of, and exposure to, the risk type.

39. Management of risk (continued)

Risk control and management (continued)

Stress testing within the Group's risk governance and capital framework (continued)

Recovery & resolution plan ("RRP") – the RRP helps inform both stress testing and reverse stress testing scenario development. Reverse stress testing explores circumstances, or a set of circumstances, that render the Group's business model unviable, moving the Group into a resolution by the authorities. As a result, these stresses are recognised as a required risk management tool in the form of an early warning indicator of potential stress events.

Strategic risk management - Stress testing informs the nature and level of risk carried by the Group arising from opportunistic assessments such as investments, divestments and acquisitions through emerging material risks posed by trends in, or changes to, the business environment.

Stress Testing Oversight and Governance

Capital Committee - The UK Capital Committee ensures, through its remit as the primary capital stress testing review forum, that results are sufficiently debated and discussed. Outputs are challenged as appropriate before being endorsed and presented to the UK Executive Committee and the Board.

Asset and Liability Committee ("ALCO") - The UK ALCO reviews the scenarios, assumptions and results of liquidity stress testing. These are reported monthly using the liquidity stress scenarios approved by the Board as part of the ILAA.

Executive Committee - UK Executive Committee members are engaged in stress testing to provide an appropriate level of review, discussion and debate into the scenario selection process, utilising their business knowledge as Heads of each business unit. The committee also consider and assess results in the context of future strategic decision making, contingency planning, capital and business planning.

Board of Directors - The Board comprises Non-executive and Executive Directors of the Group with members engaged at critical points of the stress testing cycle to provide a robust and strategic challenge in relation to scenario selection and development. In addition, the Board considers how the results are integrated into the future strategic decision making, contingency planning, capital and business planning and risk appetite.

Credit risk

Credit risk is the potential that a borrower or a counterparty will fail to meet its obligations in accordance with agreed terms. The Group's credit risk management infrastructure is framed to provide sound management principles and practices for the maintenance of appropriate asset quality.

The management of credit risk within the Group is achieved through both approval and monitoring of individual transactions and asset quality, analysis of the performance of the various credit risk portfolios and the independent oversight of credit portfolios across the Group. Portfolio monitoring techniques cover such areas as industry or geographic concentrations and delinquency trends. Roles and responsibilities within the Group are clearly defined.

Significant credit risk strategies and policies are approved, and reviewed annually, by the NAB Board, and the NAB Group Credit and Market Risk Committee. Through such policies the NAB Board establishes the NAB Group's tolerance for risk. For complex credit products and services, the NAB Group Chief Credit Officer (and associated teams) 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 within the UK, with appropriate oversight through the UK executive governance committees.

The Group's 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.

Single large exposure policies are in place within the Group. Overall composition and quality of credit portfolio exposures are monitored and periodically reported to the Board, and, where required, to the relevant supervisory authorities.

39. Management of risk (continued)

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed processes, people or systems or from external events. This includes legal risks as well as operational risk components associated with other risks categories (e.g. credit, traded market, non-traded market).

To assist with the management of operational risk, risk categories aligned to Basel II are used to categorise and facilitate the consistent identification, assessment, mitigation, monitoring and reporting of risks and events. These risk categories are defined as follows:

- Customer, products and sales practices ("conduct risk") – the treatment of customers and the management of customers impacts on all the Group's core activities. This is a principal focus of the Board, Senior Management and the regulators and the Group seeks to ensure customers are treated fairly, products are designed and sold to meet their needs, that customer expectations are met and complaints are dealt with effectively and fairly. Consideration of customer outcomes is embedded within the Group's operating processes and metrics are regularly monitored to ensure outcomes are appropriate.
- Regulatory environment and market practices – the Group is required to comply with a large volume of laws and regulations and the regulatory environment has also been subject to substantial change in recent years. This is likely to continue and represents an on-going focus of the Group's management in ensuring the Group continues to operate within prudential parameters and that the conduct of the Group's activities meets the expectations of the Group's customers, shareholders and regulators. The Group operates a zero tolerance for regulatory breaches and organises its activities to ensure controls over regulatory risk are maintained in addition to maintaining a strong, open and trusted relationship with its regulators.
- Monitoring, reporting and oversight – effective controls over business operations are essential for the protection of the Group's customers and shareholders and is a key responsibility of all employees and managers. The Group continues to reinforce frameworks, standards and oversight arrangements to enhance the quality of risk management in the organisation. Each business unit maintains a risk profile with embedded controls and actions to manage inherent risks.
- Payments and process management – the Group processes a large volume of transactions for customers every day and manages the risks in this and other operations to ensure these activities are conducted safely and efficiently. However, in all operational activity there is a potential risk of established procedures not being followed, a failure to detect errors or that inadequate controls are in place.
- External fraud and criminal activities – the Group takes seriously its responsibilities to protect customers against financial crime. This includes preventing fraud activities in all channels through which customers transact; the prevention of money laundering; and compliance with legal sanctions requirements. Fraud management is an ongoing challenge for the financial services industry and presents a constant risk to the Group as criminal activities evolve on a national and global basis. The Group takes steps to ensure its systems and controls remain appropriate to mitigate against the risks faced.
- Cyber attack – the Group recognises the risk of cyber attack against its services and data. Dealing with cyber attacks is an ongoing challenge for the financial services industry and presents a constant risk to the Group as the motivations constantly change, the techniques become more sophisticated and the resources used in the attacks become more readily available as a commodity service. The Bank has implemented industry standard tools and internal controls to help prevent external intrusions of the Bank's systems and loss of sensitive information; these controls ensure compliance with regulation. The Group takes steps to ensure its systems and controls remain appropriate to mitigate against the risks faced.
- Internal fraud and criminal activities – The Group recognises the risk of internal fraud associated with internal acts intended to defraud, misappropriate funds, information and physical assets, and circumvent policy. The Group has zero tolerance for internal fraud and has a strong control framework in place to mitigate this risk.
- Workplace practices and environment – providing a safe environment for customers and colleagues is important for the success of the business and the Group seeks to ensure adequate safeguards are in place and are operating effectively.
- Systems and infrastructure – There is a risk of service interruption due to failure of the Group's systems leading to a period of service disruption. The Group has a strong framework of controls over the continuity of service provision for all critical processes including recovery procedures in the event of unplanned service interruption.

39. Management of risk (continued)

Operational risk (continued)

- Third party providers - Failure to manage third party providers effectively may also impact on the level of service available to customers. The Group's controls to mitigate this risk include regular oversight of third party processes and assurance testing of the effectiveness of relationship management.

Responsibility for the management of operational risk rests with the business managers with oversight from the risk management function and independent assurance activities undertaken by Internal Audit. The Group has an established Operational Risk Framework which operates across the Group. It is an essential element of the business strategy which underpins all operational risk management activities that could impact the achievement of business objectives or impact core business processes and includes:

- an established governance structure that is used to ensure consistent application, control and reporting of the Operational Risk Management process. This element also includes the establishment and communication of the Group's operational risk appetite; and
- a structured process to facilitate the identification, quantification and management of risks underpinned by clear policies and guidelines. Material risks are reported monthly to the Management Assurance Committees and the UK Risk Committee, and to each Boards' Risk Committee to provide visibility and understanding of the Group's overall risk profile.

Non-traded market risk

Non-traded market risks include liquidity and funding risk, structural interest rate risk, foreign exchange risk and risks associated with the Group's defined benefit pension scheme. The primary objective for the management and oversight of non-traded market 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.

Policies relating to non-traded market risks are approved by the Board of the NAB Group. The consistent application of NAB Group polices across the Group is the responsibility of the Group's Board with the support of executive management governance committees. In relation to non-traded market risks, the primary management committee is the UK ALCO.

Risk appetite and limits are approved for non-traded market risk by the Bank's Board, with authority delegated to the UK ALCO for their subsequent implementation and monitoring.

The UK ALCO meets monthly and reports to the UK Risk Committee. The Group's Treasury division is responsible for the development and execution of strategy subject to oversight from UK Risk.

Liquidity and funding risk

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.

Liquidity within the Group is managed in accordance with the ILAA that is approved by the Board. The ILAA includes the manner in which the Group meets all regulatory requirements of the PRA and includes the Group's policy for the management of liquidity risk, including the Group's Overall Liquidity Adequacy Rule. Oversight of liquidity risk is undertaken by the UK ALCO. In recognition of the global nature of liquidity risk the liquidity position of entities across the NAB Group is also monitored by the NAB Group ALCO in accordance with the NAB Group Non-Traded Market Risk Policy. To meet the requirements of local regulatory authorities the liquidity of the Group is managed on a daily basis as a stand-alone undertaking 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. The UK ALCO delegates daily management responsibilities to the Group's Treasury division within agreed tolerances. The Group has a Contingency Funding Plan which is used to detail actions to be taken in the event of an escalated liquidity requirement.

39. Management of risk (continued)

Non-traded market risk (continued)

Liquidity and funding risk (continued)

A contingency plan has also been established for management of an escalated liquidity requirement if the Group or the NAB 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, currency, counterparty, term structure and market.

The Group's main sources of funding include the following:

- Retail, SME, corporate deposits.
- Commercial paper programme.
- Access to sterling money markets through cash deposits and certificates of deposit.
- Medium Term Note programme.
- "Lanark" residential mortgage securitisation programme (owner occupied).
- "Lannraig" buy-to-let mortgage securitisation programme.
- Regulated Covered Bond programme.
- Access to the facilities within the Bank of England Sterling Monetary Framework.

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. The Group's securitisation and covered bond programmes offer investors the opportunity to purchase mortgage backed debt.

Structural interest rate risk

Structural interest rate risk comprises the sensitivity of the Group's current and future net interest income to movements in market interest rates.

Interest rate risk is principally managed through the use of interest rate swaps. All products are used within approved mandates, with strategies subject to monthly reporting to UK ALCO and NAB Group ALCO.

There are three major contributors to interest rate risk:

- the investment of non-interest bearing deposits and equity into interest-bearing assets;
- the mismatch between repricing dates of interest-bearing assets and liabilities; and
- the inability of the pricing 'basis' for customer asset and liability products to be replicated in the financial markets i.e. basis risk.

Within the 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.

Interest rate risk management across the Group is directed by UK ALCO with delegation of day-to-day management to the Group's Treasury division. The UK Risk Committee, through UK ALCO oversight, monitors risk to ensure it remains within approved policy, limits and Board requirements.

Basis risk is managed through a combination of wholesale market basis risk products, pricing strategies and product innovation.

39. Management of risk (continued)

Non-traded market risk (continued)

Structural interest rate risk (continued)

A key feature of the risk management and oversight framework is the use of VaR as a measure of interest rate risk, along with EaR to measure the impact on future net interest income. Limits for VaR and EaR are complemented by sensitivity and scenario analysis.

Oversight of interest rate risk is conducted by the Group's Balance Sheet & Liquidity Risk Oversight team that is independent of the Treasury division.

Foreign exchange risk

Exposures arise if future cash flows can only be converted to Sterling at rates that are different than at the time of the original transaction. The Group's policy is to fully hedge these exposures at the time of commitment for all exposures that are considered to be of a marketable size.

The transactional currency exposures principally arise from dealings with customers and the Group maintains a matched position through transactions with a range of counterparties including the NAB Group in order to comply with the Group's Trading Policy Statement.

Pension risk

Pension risk is the risk that, at any point in time, the available assets to meet pension liabilities are at a value below current and future scheme obligations. The operation of a pension scheme gives rise to a number of risks, e.g. movements in equity valuations, changes in bond yields and life expectancy of scheme members. The Scheme is managed by independent Trustees. However, the impact of the Scheme on the Group is subject to management by the Group and corresponding risk oversight. The Group's Pension Risk Management Committee reports to the UK Risk Committee on pension risks.

40. Capital management overview

The Group is governed by NAB Group's Capital Management Policy. The objectives of the NAB Group's Capital Management Policy are to efficiently manage the capital base to optimise shareholder returns whilst maintaining robust capital adequacy, meeting Regulators' requirements and managing the ratings agencies assessment of the Group. The UK Capital Plan is approved by the UK Boards on an annual basis. The UK Assets and Liabilities Committee ("UK ALCO") monitors the capital plan and forecast positions on a monthly basis. This ensures that in the event that further capital is deemed necessary to meet regulatory requirements or support future strategy, the issue is proactively escalated to Senior Management and the UK Boards, as well as the NAB Group Treasury, to determine the most appropriate strategy for the Bank to achieve the desired capital outcome.

The Group implemented Basel II requirements from 1 January 2008 in measuring operational and credit risks under the standardised approach. Under Pillar I of Basel II, the Group calculates its minimum capital requirements based on 8% of RWAs. The PRA then adjusts this requirement to cover risks under Pillar II of Basel II and generates an Individual Capital Guidance ("ICG") and a Capital Planning Buffer ("CPB"). The CPB is designed to be available to absorb losses and / or to cover increased capital requirements in adverse circumstances that are outside the Group's normal and direct control.

The ultimate responsibility for capital adequacy rests with the Board of Directors. The UK ALCO, which consists of the Chief Executive Officer, Chief Operating Officer, the Chief Financial Officer and other senior executives, is responsible for the management of the capital process including approving policy, overseeing internal controls and setting internal limits over capital ratios.

The Group actively manages its capital position and reports this on a regular basis to senior management through the UK ALCO and other governance committees, including the Capital Committee which is responsible for ensuring effective governance of UK capital usage and performance. Capital requirements are included within an annual capital management plan which is presented to and approved by the Board of Directors.

40. Capital management overview (continued)

The Financial Services (Banking Reform) Act 2013 received Royal Assent in December 2013. The Act seeks to protect deposit holders and ensure the PRA can hold banks to account. The reforms may affect the structure of banks and the amount of capital held. The key aspect of the Act is to establish the concept of ring fenced bodies ("RFB"). A RFB is defined by reference to its core retail deposits which fall within the ring fence and which cannot be allowed to leak outside the ring fence. One of the thresholds for inclusion as a RFB is minimum core customer deposits of £25bn. The PRA has since released a Consultation Paper (The Implementation of ring-fencing: consultation on legal structure, governance and the continuity of services and facilities). A working group has been established to consider the impacts on the Bank.

The PRA issued a Policy Statement, known as PS7/13 which has implemented CRD IV in the UK from 1 January 2014. This included the need to make certain deductions from CET1 capital in full from 1 January 2014 with no transitional relief, including certain Deferred Tax Assets and the IAS19 Defined Benefit Pension Deficit. This approach has resulted in the injection of £300m of ordinary shares into the Bank on 27 March 2014 to offset the impact of these deductions (note 30).

CRD IV also provides for new regulatory capital buffers including a Capital Conservation Buffer (CCB) and Counter-Cyclical Buffer (CCyB) to replace the existing Capital Planning Buffer (CPB). With effect from May 2014, the Financial Policy Committee (FPC) at the Bank of England assumed formal responsibility for setting the CCyB each quarter. At its June 2014 meeting, the FPC discussed the appropriate setting for the first time and decided to set the first quarterly CCyB rate for UK exposures to 0%. Under CRD IV the CCB will, when fully adopted in 2019, equate to 2.5% of RWAs. Further detail on the Group's regulatory capital is included on pages 12 to 16 of the Strategic Report.

41. Pillar 3 disclosures

Basel III Capital Requirements Directive IV

Pillar 3 disclosure requirements are set out in Part Eight of the Capital Requirements Regulation (CRR). Article 13(3) of the CRR allows for the application of disclosure requirements on a consolidated basis, where equivalent disclosures are made by a parent undertaking.

The Group relies on the following references to comparable National Australia Bank Limited consolidated disclosure to satisfy its Pillar 3 disclosure obligations. It has already included additional capital resources disclosure on pages 12 to 16 of these financial statements.

National Australia Bank Limited 2014 Pillar 3 Report: http://www.nab.com.au/about-us/shareholder-centre/financial-disclosuresandreporting.

In addition disclosures on the Risk Management and Risk Profile of the Group are contained within the Strategic Report on pages 19 to 21 of these financial statements.

The information contained in these qualitative disclosures has not been audited by the Group's external auditors except to the extent that they are equivalent to those made under accounting requirements.

PRA remuneration Pillar 3 disclosures

Remuneration Pillar 3 disclosure requirements are set out in Article 450 of the Capital Requirements Regulation (CRR). The Group relies on the following references to equivalent National Australia Bank Limited consolidated disclosures plus additional aggregate disclosures for UK Code Staff to satisfy the Pillar 3 disclosure obligations.

UK Code Staff disclosures are available at: http://www.nab.com.au/about-us/shareholder-centre/financial-disclosuresandreporting/regulatory-disclosures

National Australia Bank Limited 2014 Pillar 3 Report: http://www.nab.com.au/about-us/shareholder-centre/financial-disclosuresandreporting.

The remuneration report is held within the Report of the Directors of the National Australia Bank Limited 2014 Annual Financial Report.

National Australia Bank Limited 2014 Annual Financial Report: http://www.nab.com.au/about-us/shareholder-centre/financial-disclosuresandreporting.

Notes to the consolidated financial statements (continued)

42. Events after the balance sheet date

There have been no subsequent events which have occurred since 30 September 2014 that would require disclosure in the annual report and financial statements of Clydesdale Bank PLC.

Enhanced disclosure task force recommendations

Below is a tabular overview of how the Group has responded to the EDTF recommendations as referred to on page 22 of the annual report and consolidated financial statements. The Group already provides risk disclosures in accordance with International Financial Reporting Standards which can predominantly be found in notes 38, 39 and 40 to the financial statements and the appropriate cross reference between these and the relevant EDTF recommendation is provided, as necessary, to avoid duplicating information.

EDTF recommendation	Description	The Group's approach
1	Amalgamate all risk related information and if not possible provide an aid to help users locate risk disclosures	Risk disclosures are included within the Strategic Report and notes 38, 39 and 40 of the annual report and consolidated financial statements.
2	Define the Group's risk terminology and risk measures	Relevant definitions are included within the glossary to the annual report and consolidated financial statements.
3	Describe and discuss top and emerging risks	Commentary on the Group's top and emerging risks can be found within the Strategic Report starting on page 4.
4	Outline plans to meet each new key regulatory ratio once the applicable rules are finalised. These include: • net stable funding ratio ("NSFR"); • liquidity coverage ratio ("LCR"); and • leverage ratio	The ratios which will be introduced under the Basel III regime, including LCR, NSFR and the Leverage ratio, are being actively monitored and managed by the Group. They are reported at key governance committees and are disclosed within 'Key Measures' in the strategic report.
5	Summarise the Group's risk management organisation	The Group's risk management organisation is described and diagrammatically represented in note 39.
6	Describe the Group's risk culture and how procedures and strategies are applied to support the culture	Commentary on the Group's risk culture can be found in note 39.
7	Describe the Group's key risks from the business model and activities along with the Group's risk appetite and how these risks are managed	Commentary on the Group's business model risks can be found within the Strategic Report starting on page 4.
8	Describe the use of stress testing within the Group's risk governance and capital frameworks	Commentary on the use of stress testing within the Group's risk governance and capital frameworks is provided in note 39

Enhanced disclosure task force recommendations (continued)

9	Provide minimum Pillar 1 capital requirements, including any capital surcharges or capital conversion buffers, or the minimum internal ratio	The Group's Pillar 1 requirements can be found in the capital position section within the Strategic Report starting on page 4.
10	Summarise composition of capital and provide a reconciliation of the accounting balance sheet to the regulatory balance sheet	The Group provides a summary of its Tier 1 capital position along with a reconciliation of regulatory capital to statutory equity in the capital position section within the Strategic Report starting on page 4.
11	Present a flow statement of movements in regulatory capital for the year, including changes in common equity tier 1, tier 1 and tier 2 capital	The Group's regulatory capital flow statement can be found in the capital position section within the Strategic Report starting on page 4.
12	Capital planning within a more general discussion of management's strategic planning	An overview of the Group's capital management approach can be found in note 40 to the annual report and consolidated financial statements which highlights that it is governed by NAB Group's Capital Management Policy. The Group is a wholly owned subsidiary with a significant Global parent. The Group operates a UK Risk Appetite Framework to support the Group's strategic planning and capital planning processes. The framework identifies material risks to which the business is exposed to and for which capital needs to be held. The UK Risk Appetite Statement is the formal articulation of the risk bearing capacity of the Group, it is approved annually by the Board, and supports the strategic planning process.
13	How do RWAs relate to business activities and related risks	The Group provides an analysis of RWAs in the capital position section within the Strategic Report starting on page 4. This breaks down the RWA figure into our key business activities with the risks calculated on a standardised basis.
14	Capital requirements for calculating RWAs for credit risk for each Basel asset class including the major portfolios within those classes	The Group's capital requirements for calculating RWAs for credit risk for each Basel asset class can be found in the capital position section within the Strategic Report starting on page 4.
15	Tabulate credit risk in the banking book for Basel asset classes and major portfolios within the Basel asset classes	A table analysing the credit risk in the banking book for Basel asset classes can be found in the capital position section within the Strategic Report starting on page 4. The table discloses our exposure consistent with the standardised approach.

Enhanced disclosure task force recommendations (continued)

16	RWA flow statement	An RWA flow analysis is presented within the Strategic Report starting on page 4.
17	Contextualising Basel Pillar 3 back-testing requirements	As detailed in note 41, the Group will rely on comparable National Australia Bank Limited consolidated disclosure to satisfy its Pillar 3 disclosure obligations.
18	Potential liquidity needs management and the components of the liquidity reserve held to meet these needs	Notes 38 and 39 to the annual report and consolidated financial statements contain information in relation to liquidity risk and non-traded market risk (specifically liquidity and funding risk) respectively. The funding and liquidity section within the Strategic Report starting on page 4 also describes the Group's year end liquidity position.
19	Encumbered and unencumbered assets by balance sheet categories including collateral	The Group's encumbered and unencumbered assets position is shown within the funding and liquidity section within the Strategic Report starting on page 4.
20	Consolidated total assets, liabilities and off-balance sheet commitments by remaining contractual maturity	A table with the Group's consolidated assets, liabilities and off balance sheet commitments by remaining contractual maturity can be found within note 38 of the annual report and consolidated financial statements.
21	The Group's funding strategy including key sources and any funding concentrations	Commentary on the Group's funding strategy can be found in the liquidity and funding section within note 39.
22	Linking balance sheet and balance sheet line items with positions included in the trading market and non-trading market disclosures	A table showing the balance sheet with values combined with the principal non-traded risk types that affect each significant balance sheet line item can be found within note 39 of the annual report and consolidated financial statements.

Enhanced disclosure task force recommendations (continued)

23	Significant trading and non-market trading risk factors	The Group does not operate a trading portfolio. There is no appetite for traded market risk other than de minimus positions arising from the timing of hedging transactions. Market risk is defined as positions in financial instruments, including derivative products and other off-balance sheet instruments, held with trading intent. Interest rate risk is the most significant non-traded market risk the Group faces. Further comment on interest risk and prepayment risk can be found in note 38 to the annual report and consolidated financial statements with additional non-traded market risk factors contained in note 39.
24	Significant market risk measurement model limitations	Note 38 to the annual report and consolidated financial statements provides a summary of key features of the internal interest rate risk management model that is used for non-traded portfolios. The Group does not operate traded portfolios.
25	Primary risk management techniques employed to measure and assess the risk of loss beyond reported risk measures and parameters	Note 38 to the annual report and consolidated financial statements provides detail on the value at risk and earnings at risk methods and also on a series of supporting measures for interest rate risk. As explained above the Group does not operate a trading portfolio.
26	Credit risk profile including any significant credit risk concentrations	Tables showing the levels of industry concentrations (including both on and off-balance sheet commitments) can be found in note 38 to the annual report and consolidated financial statements.
27	Policies for identifying impaired or non-performing loans including forbearance	The Group discusses its approach to identifying impaired or non-performing loans in note 15 to the annual report and consolidated financial statements. The Group has aligned its forbearance definitions and policy forbearance with FINREP reporting as of 30 September 2014. Current levels and types of forbearance are included in the relevant section within note 38 along with discussion of the changes to forbearance policy.
28	Reconciliation of non-performing and impaired loans including the allowance for loan losses	The Group's distribution of non-performing (past due but not impaired) and impaired loans and advances across product types can be found in note 15 to the financial statements with the associated impairment allowances in note 16 to the financial statements.
29	Counterparty credit risk that arises from derivative transactions	The Group's disclosures on derivative transactions can be found in note 14 of the annual report and consolidated financial statements. The Group's principal non customer derivative counterparty is NAB.

Enhanced disclosure task force recommendations (continued)

30	Credit risk mitigation, including collateral held for all sources of credit risk	A description of the Group's risk mitigation techniques; quantitative analysis on the non-property collateral held; disclosures on collateral held as security, and other credit enhancements can be found in note 38.
31	"Other risk" types including how these are identified, governed, measured and managed	The Group has not identified other risk types that are deemed to be material for disclosure purposes.
32	Publically known risk events related to other risks, including operational, regulatory compliance and legal risks, where material or potentially material loss events have occurred	The Group is exposed to a number of risks that are in the public domain, particularly around conduct related matters. These are discussed within note 26 to the annual report and consolidated financial statements and in the relevant sections of the Strategic Report starting on page 4.

Glossary

Term	Definition
Additional Tier (AT1) securities	Securities that are considered additional tier 1 (AT1) capital in the context of CRD IV.
APRA	Australian Prudential Regulatory Authority.
Arrears	A customer is in arrears when they fail to adhere to their contractual payment obligations resulting in an outstanding loan that is unpaid or overdue.
Average assets	Represents the average of assets over the year adjusted for any disposed operations.
Bank	Clydesdale Bank PLC.
Bank Levy	This is applicable to certain UK financial institutions and UK operations of foreign banks from 1 January 2011. The amount due is based on a percentage of the chargeable equity and liabilities for each applicable entity as at the balance sheet date.
Basel II	The capital adequacy framework issued by the Basel Committee on Banking Supervision in June 2006 in the form of the "International Convergence of Capital Measurement and Capital Standards".
Basel III	In December 2010, the Basel Committee issued final rules "Basel III: A global regulatory framework for more resilient banks and banking systems" and "Basel III: International framework for liquidity risk measurement, standards and monitoring". Together these documents present the Basel Committee's reforms to strengthen global capital and liquidity rules with the goal of promoting a more resilient banking sector. The new requirements are being phased in starting 1 January 2014 with full implementation by 1 January 2019.
Business lending	Lending to non-retail customers, including overdrafts, asset and lease financing, term lending, bill acceptances, foreign currency loans, international and trade finance, securitisation and specialised finance.
Cash earnings	A non-IFRS key performance measure that excludes certain items within the calculation of net profit attributable to owners of the Group. It is also a key performance measure used by the Australian peers of the ultimate parent with a similar business portfolio. These specified items are excluded in order to better reflect what is considered to be the underlying performance of the Group. Net profit attributable to owners of the Group adjusted for (where appropriate): • Distributions • Treasury shares • Fair value and hedge ineffectiveness • Restructure costs • Litigation expense • Property revaluation • Goodwill impairment • Software impairment
Collateral	The assets of a borrower that are used as security against a loan facility.
Collective impairment provision	Impairment assessment on a collective basis for homogeneous groups of loans that are not considered individually significant and to cover losses which have been incurred but have not yet been identified on loans subject to individual assessment.
Commercial paper	An unsecured promissory note issued to finance short term credit requirements. These instruments have a specified maturity date and stipulate the face amount to be paid to the investor on that date.

Glossary (continued)

Conduct risk	The risk that the Group's behaviours (culture, governance, systems and controls) have led to inappropriate customer outcomes.
Contractual maturities	The date on which the final payment of any financial instrument is due to be paid or received, at which point all the remaining outstanding principal and interest have been repaid in full.
Common Equity Tier 1 capital ("CET1")	The highest quality form of regulatory capital that comprises total shareholders' equity (excluding preference shares issued) and related non-controlling interests, less goodwill and intangible assets and certain other regulatory adjustments.
Covered bonds	A corporate bond with primary recourse to the institution and secondary recourse to a pool of assets that act as security for the bonds on issuer default. Covered bonds remain on the issuer's balance sheet and are a source of term funding for the Group.
CRD IV	The European Union's ("EU") proposal to implement Basel III, the international agreement on bank capital standards agreed at G20 level. It replaces the EU's earlier capital requirements directives with a revised package consisting of a new Capital Requirements Directive and a new Capital Requirements Regulation. The CRD IV package raises capital and liquidity requirements for European banks and harmonises the European framework for bank supervision.
CRE	Commercial real estate.
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 adjustment	An adjustment to the valuation of financial instruments held at fair value to reflect the creditworthiness of the counterparty. Also known as a credit valuation adjustment ("CVA").
Customer deposits	Interest bearing, non-interest bearing and term deposits (including retail and corporate deposits).
Customer funding index ("CFI")	An internal NAB metric expressing customer deposits divided by core assets (gross loans and advances including acceptances, financial assets at fair value and held to maturity investments) as a percentage.
Debt restructuring	A restructuring by which the terms and provisions of outstanding debt agreements are changed. This is often done in order to improve cash flow and the ability of the borrower to repay the debt. It can involve altering the repayment schedule as well as debt or interest charge reduction.
Defined Liquidity Group	The defined liquidity group includes all material operating entities within the Group, excluding consolidated securitisation entities. It reflects the regulatory view with respect to oversight of the Group's liquidity position and resources.
Delinquency	See "Arrears".
Derivative	A derivative financial instrument is a contract or agreement whose value is related to the value of an underlying instrument, reference rate or index.
Earnings at risk ("EaR")	A measure of the quantity by which net interest income might change in the event of an adverse change in interest rates.
Effective interest rate method ("EIR")	The method used to measure the carrying value of certain financial instruments which amortises the relevant fees over the expected life of the instrument.
Exposure	A claim, contingent claim or position which carries a risk of financial loss.

Glossary (continued)

Fair value	The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions.
Fair value adjustment	An adjustment to the fair value of a financial instrument which is determined using a valuation technique (Level 2 and Level 3) to include additional factors that would be considered by a market participant that are not incorporated within the valuation model.
FCA	Financial Conduct Authority. The FSA was replaced as the UK's financial regulator on 1 April 2013 by two new regulatory bodies: the PRA and the FCA. The FCA is responsible for the regulation of conduct in retail, as well as wholesale, financial markets and the infrastructure that supports those markets.
Forbearance	The term generally applied to the facilities provided to assist borrowers, both retail and non-retail, who are experiencing a period of financial stress and can take a variety of forms such as negotiating an arrangement or short term promise to pay, transfer to interest only terms, or term extensions. The granting of a forbearance measure to a borrower is as a consequence of concerns about the borrower's ability to meet their contractual payments when due and specifically relates to such instances where the changes to the existing arrangement have been made on terms that the Group would not ordinarily consider to be on a commercial basis.
Forborne performing loans	Loans to which forbearance measures have been granted and which are less than or up to ninety days past due and do not otherwise meet the criteria of forborne non-performing loans.
Forborne non-performing loans	Forborne non-performing loans to which forbearance measures have been granted and which are more than ninety days past-due, or where the debtor is assessed as unlikely to pay its credit obligations in full without realisation of collateral, regardless of the existence of any past-due amount or of the number of days past due.
FSA	Financial Services Authority. The FSA was replaced as the UK's financial regulator on 1 April 2013 by the Prudential Regulation Authority ("PRA") and the Financial Conduct Authority ("FCA").
FSCS	Financial Services Compensation Scheme.
Funding risk	A form of liquidity risk arising when the liquidity needed to fund illiquid asset positions cannot be obtained at the expected terms and when required.
Group	Clydesdale Bank PLC and its controlled entities.
Hedge ineffectiveness	Represents the extent to which the income statement is impacted by changes in fair value of hedging instruments not being fully offset by changes in fair value of hedged items.
Housing lending	Mortgages secured by residential properties as collateral.
IFRS	International Financial Reporting Standards as issued by the International Accounting Standards Board ("IASB").
Impaired loans	Retail mortgages with security insufficient to cover principal and arrears of interest revenue; business lending where there is sufficient doubt about the ultimate collectability of principal and interest; and off-balance sheet credit exposures where current circumstances indicate that losses may be incurred.

Glossary (continued)

Impairment losses	Where an asset's recoverable amount is less than its carrying value and the difference recognised in the income statement with the carrying value of the asset reduced by creating an impairment allowance. This may be assessed at either the individual level or collectively.
Impairment allowances	A provision held on the balance sheet to recognise that a loan is impaired. This can be at either the individual or collective level.
Individual Liquidity Adequacy Assessment ("ILAA")	The ILAA documents the Bank's assessment and management of balance sheet risks relating to funding and liquidity.
Interest rate risk	The risk to the Group's financial performance and position caused by changes in interest rates.
Internal Capital Adequacy Assessment Process ("ICAAP")	The Bank's own assessment of the levels of capital that it needs to hold through an examination of its risk profile from regulatory and economic capital viewpoints.
Internal ratings-based approach ("IRB")	A method of calculating credit risk capital requirements using internal, rather than supervisory, estimates of risk parameters.
Investments - AFS	Investments - available for sale.
Investment grade	This is the highest possible range of credit ratings, from "AAA" to "BBB", as measured by external credit rating agencies.
IRRBB	Interest rate risk in the banking book.
Key management personnel	Directors of the Group, members of the UK Executive Committee and PRA approved persons with a controlled function 1 – 28 (as defined in SUP 10B.4.3 within the PRA handbook available at: https://fshandbook.info/FS/html/handbook/SUP/10B/4) and FCA approved persons with an FCA controlled function 1 – 29 (as defined in SUP 10A.4.4 within the FCA handbook available at: https://fshandbook.info/FS/html/handbook/SUP/10A/4#DES95
Level 1 fair value measurements	Financial instruments whose fair value is derived from unadjusted quoted prices for identical instruments in active markets.
Level 2 fair value measurements	Financial instruments whose fair value is derived from quoted prices for similar instruments in active markets and financial instruments valued using models where all significant inputs are observable.
Level 3 fair value measurements	Financial instruments whose fair value is derived from valuation techniques where one or more significant inputs are unobservable.
Leverage ratio	This is a new regulatory standard ratio proposed by the Basel III reforms and is the Tier 1 capital divided by the total on and off balance sheet exposures expressed as a percentage. The Basel Committee has proposed to test a minimum requirement of 3% for the leverage ratio during a parallel run period from 1 January 2013 to 1 January 2017, with a view to migrating to a Pillar 1 treatment on 1 January 2018 based on appropriate review and calibration.
LIBOR	London Interbank Offered Rate.

Glossary (continued)

Liquidity coverage ratio ("LCR")	This is a new regulatory standard ratio proposed by the Basel III reforms and is the stock of high quality liquid assets divided by the total net stressed cash outflows over the next 30 calendar days expressed as a percentage. The Basel Committee intends to introduce the LCR on 1 January 2015 and phase in minimum requirements with full compliance due from 1 January 2019.
Liquidity risk	The risk that the Group does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash flows.
Loan to value ("LTV")	A mathematical calculation that expresses the amount of a loan as a percentage of the value of security. A high LTV indicates that there is less of a cushion to protect the lender against asset price falls or increases in the loan if repayments are not made and interest is added to the outstanding loan balance.
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.
Medium Term Notes ("MTNs")	MTNs are issued by corporates, including financial institutions, across a range of maturities. MTNs are frequently issued by investment grade corporates in senior unsecured form under MTN Programmes whereby notes are offered on a regular and continuous basis to investors.
NAB	National Australia Bank Limited. A company incorporated in the State of Victoria, Australia. The ultimate parent of Clydesdale Bank PLC.
NAGE	National Australia Group Europe Limited. A company incorporated in the UK and registered in England. The immediate parent of Clydesdale Bank PLC.
Net interest income	The amount of interest received or receivable on assets net of interest paid or payable on liabilities.
Net interest margin	Net interest income as a percentage of average interest earning assets.
Net profit/(loss) attributable to owners of the Group	Represents the Group's statutory profit/(loss) after tax and reflects the amount of net profit/(loss) that is attributable to owners.
Net promoter score	This is an externally collated customer loyalty metric that measures loyalty between a Provider, who in this context is the Bank, and a consumer.
Net stable funding ratio ("NSFR")	This is a new regulatory standard ratio proposed by the Basel III reforms and is the total amount of available stable funding divided by the total amount of required stable funding, expressed as a percentage. The NSFR is currently subject to an observation period, with the Basel Committee intending that it will become a minimum standard by 1 January 2018.
Non-impaired assets 90+ days past due	Consist of well-secured assets that are more than 90 days past due and portfolio-managed facilities that are not well secured and between 90 and 180 days past due.
Operational risk	The risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk.
Past due loans and advances	Loans and advances on which repayments are overdue.

Glossary (continued)

Pension risk	The risk that, at any point in time, the available assets to meet pension liabilities are at a value below current and future scheme obligations.
PPI	Payment Protection Insurance.
PRA	Prudential Regulation Authority. The FSA was replaced as the UK's financial regulator on 1 April 2013 by two new regulatory bodies: the PRA and the FCA. The PRA, a subsidiary of the Bank of England, is responsible for promoting the stable and prudent operation of the financial system through regulation of all deposit-taking institutions, insurers and investment banks.
Probability of default ("PD")	The probability that an obligor will default (usually within a one-year time horizon).
Property revaluation	Represents revaluation increments and decrements of land and buildings based on Directors' valuations to reflect fair value.
Regulatory capital	The capital which the Group holds, determined in accordance with rules established by APRA for the consolidated NAB Group and by local regulators (in the UK the PRA) for individual Group companies.
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).
Restructured loans	A restructured loan is where the terms and conditions of a loan contract have been varied that may involve one or both of the following: • the original scheduled repayment contract has been re-written by changing the frequency and pattern of repayments with a lengthening of the final repayment/maturity profile on a non-commercial basis (e.g. non-market extension of principal repayment period); • the Group has previously made a specific provision for the customer/obligor and written off the debt in part or converted the debt to a changed obligation in exchange for realisable assets not previously held or a debt for equity swap. See also forbearance.
Retail loans	Money lent to individuals rather than institutions. This includes both secured and unsecured loans such as residential mortgages, overdrafts and credit card balances.
Risk appetite	An assessment of the types and quantum of risks to which the Group wishes to be exposed.
Return on assets ("ROA")	Profit/(loss) of the Group as a percentage of total assets.
Risk-weighted assets ("RWAs")	On and off balance sheet assets of the Group are allocated a risk weighting based on the amount of capital required to support the asset.
Sale and repurchase agreement ("repo")	A short-term funding agreement that allows a borrower to create a collateralised loan by selling a financial asset to a lender. As part of the agreement, the borrower commits to repurchase the security at a date in the future repaying the proceeds of the loan. For the counter-party (buying the security and agreeing to sell in the future) it is a reverse repurchase agreement or a reverse repo.
Securitisation	The practice of pooling similar types of contractual debt and packaging the cash flows from the financial asset into securities that can be sold to institutional investors in debt capital markets. It provides the Group with a source of secured funding than can achieve a reduction in funding costs by offering typically AAA rated securities secured by the underlying financial asset.

Glossary (continued)

Sovereign exposures	Exposures to governments, ministries, departments of governments, embassies, consulates and exposures on account of cash balances and deposits with central banks.
Structured entities ("SE")	An entity created to accomplish a narrow well-defined objective (e.g. securitisation of financial assets). An SE may take the form of a corporation, trust, partnership or unincorporated entity. SEs are often created with legal arrangements that impose strict limits on the activities of the SE.
Specific impairment provision	A specific provision relates to a specific loan, and represents the estimated shortfall between the carrying value of the asset and the estimated future cash flows, including the estimated realisable value of securities after meeting securities realisation costs.
Stable funding index ("SFI")	An internal NAB metric of the customer funding index ("CFI") plus the term funding index ("TFI") expressed as a percentage.
Standardised approach	In relation to credit risk, a method for calculating credit risk capital requirements using External Credit Assessment Institutions ("ECAI") ratings and supervisory risk weights. In relation to operational risk, a method of calculating the operational capital requirement by the application of a supervisory defined percentage charge to the gross income of eight specified business lines.
Subordinated liabilities	Liabilities which rank after the claims of other creditors of the issuer in the event of insolvency or liquidation.
Term funding index ("TFI")	An internal NAB metric expressing term wholesale funding (with a remaining maturity to first call date greater than 12 months) divided by core assets (gross loans and advances including acceptances, financial assets at fair value and held to maturity investments) as a percentage.
Tier 1 capital	A component of regulatory capital which is able to absorb losses, is permanent and available when required, ranks for repayment upon winding up/administration or similar procedures after all other debts and liabilities, and has no fixed inescapable costs. It comprises core Tier 1 and other Tier 1 capital, which includes qualifying capital instruments such as non-cumulative perpetual preference shares and hybrid capital securities.
Tier 2 capital	A component of regulatory capital which includes forms of capital that do not meet the requirements for permanency and absence of inescapable fixed servicing costs that apply to Tier 1 Capital. It comprises qualifying subordinated loan capital, related non-controlling interests, allowable collective impairment allowances and unrealised gains arising on the fair valuation of equity instruments held as available-for-sale. Tier 2 capital also includes reserves arising from the revaluation of properties.
Tier 1 ratio	Tier 1 capital as a percentage of risk-weighted assets.
Tier 2 ratio	Tier 2 capital as a percentage of risk-weighted assets.
UK ALCO	UK Asset and Liability Committee.
Value at risk ("VaR")	A measure of the loss that could occur on risk positions as a result of adverse movements in market risk factors (e.g. rates, prices, volatilities) over a specified time horizon and to a given level of confidence.
Write-down	A reduction in the carrying value of an asset due to impairment or adverse fair value movements.

Other information

Country by Country Reporting ("CBCR")

The Capital Requirements (Country-by-Country Reporting) Regulations 2013 came into effect on 1 January 2014 and place certain reporting obligations on financial institutions that are within the scope of the European Union's Capital Requirements Directive (CRD IV). The purpose of the Regulations is to provide clarity on the source of the Group's income and the locations of its operations.

The vast majority of entities that are consolidated into the Group's financial statements are UK registered entities with the only substantive overseas element to the Group being a banking operation in Guernsey ("Clydesdale Bank International") that undertakes certain deposit activities. This branch was closed to new business on 14 January 2013 with the existing customer book now being run down.

The activities of Clydesdale Bank PLC are as described on page 4.

The total operating income and the average number of full time equivalent employees during the year to 30 September 2014 were:

Entity	Total operating income (£m)	Employees (Number)
Clydesdale Bank PLC	963	4,521
Clydesdale Bank International	(2)	5

The only other non UK registered entities of the Group are two Trustee companies that are part of the Group's securitisation vehicles (Lanark and Lannraig). Both of these entities (Lanark Trustees Limited and Lannraig Trustees Limited) are registered in Jersey. These entities play a part in the overall securitisation process by having the beneficial interest in certain mortgage assets assigned to them. Both entities have no assets or liabilities recognised in their financial statements with the securitisation activity taking place in other UK registered entities of the structures. These entities do not undertake any external economic activity and have no employees. The results of these entities as well as those of the entire Lanark and Lannraig securitisation structures are consolidated in the financial statements of the Group.

Website	www.cbonline.co.uk
Media	Press office 0845 603 5447 press.office@nab.co.uk
National Australia Bank	NAB Group results are available from www.nab.com.au