UK Asset Resolution Limited
Annual Report & Accounts
for the 15 months to 31 March 2014

Registered in England and Wales under company number 07301961

UK Asset Resolution

UKAR Group Overview

About UKAR

UK Asset Resolution Limited ('UKAR') is the holding company established on 1 October 2010 to bring together the government-owned businesses of Bradford & Bingley plc ('B&B') and NRAM plc ('NRAM') (formerly Northern Rock (Asset Management) plc). These businesses are both closed to new business and are in run-off. UKAR is wholly owned by Her Majesty's Treasury ('HM Treasury'), whose shareholding is managed by UK Financial Investments Limited ('UKFI'). The full governance structure is set out in a framework document ('the Framework Document') agreed between UKAR and HM Treasury (see page 16 for details).

In addition, on 8 October 2013 UKAR Corporate Services Limited ('UKARcs'), a subsidiary business of UKAR, became responsible for the administration of the government's Help to Buy: mortgage guarantee scheme on behalf of HM Treasury. The scheme is managed on a nil-gain nil-loss basis with all costs being fully reimbursed by HM Treasury.

Mission and Purpose

Our mission and purpose were established in 2010 and reaffirmed by the Board in 2013:

Mission

"To Maximise Value for the Taxpayer"

Vision

"Creating Success Together"

Strategic objectives

1. Reduce, protect and optimise the balance sheet.
2. Maximise cost effectiveness and efficiency through continuous improvement.
3. Be excellent in customer and debt management.
4. Be a great place to work.

Whilst treating all stakeholders fairly.

Values

- Straightforward
- Positive
- Caring
- Responsible
- Inspiring

Key Facts

Number of customers – 467,000

Value of customer loans – £61.2bn

Employees – 2,142

Locations – Crossflatts, West Yorkshire
– Doxford, Sunderland

Contents

Chairman's statement

This third set of consolidated results for UKAR are for a 15 month period as a result of the Group's accounting reference date changing from 31 December to 31 March in order to align to the reporting year-end of HM Treasury.

Our CEO, Richard Banks, gives a more detailed overview of our performance in the Strategic Report confirming that in 2013/14 we made excellent progress and exceeded the medium term targets for value creation and loan repayments agreed with our shareholder in 2011. Over the past 15 months, payments to the taxpayer, including repayments of loans, interest, fees and corporation tax totalled £6.2bn. Since establishment in October 2010 UKAR has repaid over £10bn of the government loans, reducing these from £48.7bn to £38.3bn.

Underlying profit before tax for the 15 months was £1,523.2m. When adjusted for comparable time periods this is 11% higher than the 12 month period of 2012 of £1,096.9m primarily due to a reduced loan impairment charge, as the result of continued improvements in the level of arrears and house prices.

The number of residential customers in arrears by more than 3 months continued to improve in 2013 and the first quarter of 2014 and reduced from 25,581 in December 2012 to 15,483, contributing to the loan impairment charge falling from £241m to £95m. Over 93% of our customers continue to be fully up to date with their loan payments and we are continuing our strategy of proactive contact with customers to help them manage their financial affairs.

In 2013 we replaced our costly and unreliable legacy IT infrastructure and completed the withdrawal from our operations in Gosforth, Newcastle. Colleagues now work from two main sites at Doxford in Sunderland and Crossflatts in West Yorkshire.

The remediation of historic regulatory defects has continued, principally relating to the mis-selling of Payment Protection Insurance ('PPI') and in respect of a segment of Northern Rock Consumer Credit Act ('CCA') regulated loans. Remediation has cost £116m in 2013/14 but we remain determined to correct the errors of the past and treat our customers fairly.

The Board

The UKAR Board comprises myself as Chairman, four independent Non-Executive Directors, two UKFI nominated Directors and one Executive Director. In September we welcomed Christopher Fox to the Board when UKFI appointed him as one of their representative Non-Executive Directors to manage HM Treasury's shareholdings in UKAR. Christopher replaced Jim O'Neil who left UKFI in the same month. We also said farewell to Phillip McLelland, our Finance Director, who left UKAR at the end of November for a role with Provident Financial plc and we wish him and Jim well in their new roles. We reduced the number of independent Non-Executive Directors by one at the end of 2013 when Louise Patten stepped down from the Board after 10 years. Louise has served the Board and our Remuneration Committee, which she chaired, exceptionally well and I would like to thank her for her contribution over the years.

At the end of the 15 months our internal review of the performance of the Board was positive and concluded that its performance continued to be satisfactory, demonstrating good collaborative team working. The various Board Committees also undertook annual reviews, with similar outcomes.

I would like to thank all Directors for their contribution to the effective running of UKAR in what has been a period of excellent progress.

Governance

High standards of corporate governance are fundamental to the way UKAR operates. The Board is committed to ensuring that we not only operate effectively, but that each Director is committed to the role and continues to make a valuable contribution to the business. You will find full details of the Board structure and biographies of each Director on pages 16 to 18.

Chairman's statement (continued)

Colleagues

Colleagues across UKAR have once again made tremendous efforts and shown resilience in coping with the change and complexity that arises as a result of bringing two businesses together. I want to thank all colleagues, those who are in daily contact with our customers and those in the support areas, for their commitment, loyalty and contribution to the success of UKAR.

Richard Banks and his management team have shown great leadership in managing the orderly wind down of the two mortgage books and maximising value for the taxpayer whilst maintaining high levels of colleague engagement, embedding good conduct and treating our customers fairly. Many complex issues have arisen over the 15 months and the team have applied themselves with great determination and professionalism to finding solutions to these.

Looking ahead

UKAR has been very successful since its formation in 2010 but we are conscious that new challenges will emerge as the wind down proceeds and the balance sheet shrinks. The Board keeps under review all options for realising value from the operational expertise that has been developed that are consistent with the objective of accelerating the repayment of government debt.

I thank everyone involved with UKAR for their efforts and look forward to continuing our progress in 2014/15.

Richard Pym

Chairman

2 June 2014

Strategic Report

Chief Executive Officer's introduction

Introduction

This strategic report brings together an overview of our business and our company, customer and people strategies, as well as a summary of our principal risks. We look at how we performed in the period and the progress since UKAR was formed.

Business model and objectives

UKAR is responsible for managing the orderly run-off of NRAM and B&B. We aim to maximise value for the taxpayer and have set ourselves a number of key goals, against which we have made notable achievements during 2013/14.

Financial performance

I am pleased to report that UKAR has surpassed all of the financial targets agreed with UKFI for 2013/14. In the 15 month period we paid HM Treasury £6.2bn (2012: £4.0bn) including £5.1bn (2012: £3.1bn) of principal on our loans from the government, reduced arrears by 39%, reduced our year-on-year costs by 9% and achieved £1,523.2m in underlying profits (2012: £1,096.9m).

A summary of UKAR's financial performance can be found on page 9, with more detail provided in the Financial Review on page 41.

Balance Sheet

Since UKAR was formed the UKAR companies have repaid £10.4bn of government funding, including £5.1bn in 2013/14. In addition, £7.4bn of other funding was repaid on maturity in the period. These repayments have been funded largely from a £7.5bn reduction in lending balances reflecting £5.8bn of secured residential redemptions, £0.1bn of unsecured redemptions, £0.2bn of commercial redemptions and £1.0bn of ongoing repayments. In addition, the £0.4bn NRAM standalone unsecured personal loan book was sold during the period.

As at 31 March 2014, lending balances stand at £61.2bn (December 2012: £68.7bn). In total, the Balance Sheet has reduced by £40.9bn from £115.8bn at formation to £74.9bn at 31 March 2014.

A summary of UKAR's progress since formation can be found on page 10.

Costs

Since UKAR was formed we have significantly reduced costs and increased operational flexibility. We have migrated systems onto common platforms, created common processes, rationalised the number of operating sites and created a single workforce and culture. Much of this work has been completed in 2013/14 with the closure of the Gosforth site and the transfer of our IT infrastructure to a new supplier.

Customer and debt management

UKAR aims for excellence in customer and debt management and during 2013/14 we continued to focus on proactively helping customers who are in financial difficulty now or who may be susceptible in the future. It is important that we take responsibility for good conduct and we continue to embed processes and controls that enable us to deliver fair and appropriate outcomes to our customers. Our approach is fully aligned with the Financial Conduct Authority's ('FCA's') principles, embedding good conduct and delivering fair and appropriate outcomes to our customers.

UKAR has almost 467,000 customers (2012: 614,000), with 529,000 mortgage accounts (2012: 586,000) and 119,000 unsecured personal loan accounts (2012: 228,000). In the main, these loans continue to perform well and over 93% are up to date. For those customers in financial difficulty we have proactively sought to support them and the total number of mortgage cases three or more months in arrears, including those in possession, reduced by 39% to 15,483 cases as at 31 March 2014 (December 2012: 25,581).

Currently 46% of UKAR residential mortgage accounts (excluding buy-to-let) held by 152,000 customers, are 'interest only', with 73% of these having more than ten years until maturity. We have now contacted over 31,000 customers reminding them of their obligations and discussing with them how they can make plans for the future.

Chief Executive Officer's introduction (continued)

Customer and debt management (continued)

Although we aim for excellence in customer and debt management, we are also aware that sometimes things go wrong. We continue to deal with several legacy issues inherited from Northern Rock and B&B. Our intent is to do the right thing for our customers, including redress if appropriate and we have provided £116m for such remediation in the 15 month period.

Further information on our customer strategy is on pages 11 and 12.

Help To Buy: mortgage guarantee scheme

In June 2013 the government announced that UKAR will provide administrative support to the mortgage guarantee scheme. The scheme launched on 8th October 2013 and is being administered by UKAR through a separate subsidiary, UKARcs. UKARcs is responsible for reviewing application documentation from lenders, monitoring activity in the scheme on behalf of HM Treasury, processing claims (claim eligibility, loss assessment and payments) and making any adjustments to claims as required by the scheme rules. The scheme is fully funded by HM Treasury and is being run on a nil-gain nil-loss basis by UKARcs.

Colleagues

We place a heavy emphasis on our people to manage the challenges we face in running a business in wind down and, therefore, being a 'Great Place to Work' is one of our four strategic objectives. Our internal survey results show high levels of colleague engagement demonstrating that we are succeeding in this objective (see our people strategy on pages 12 and 13).

Outlook

The signs are that the UK economy is continuing to recover, both in terms of growth and employment and in the housing and mortgage markets. House prices have increased strongly over the past 15 months, which, combined with continued low rates of interest, is good news for our customers and has driven increased redemption activity. However, despite the more positive conditions, many households continue to be under financial pressure. This, together with the prospect of interest rate rises and higher mortgage payments, will be a concern for many of our customers. In order to help ensure our customers can continue to afford their mortgage payments in the future, we are increasingly focusing on ways to help them plan ahead, to consider their financial situation and the long-term affordability of their mortgage.

Conclusion

UKAR has had a very successful 15 months delivering our financial objectives to the taxpayer whilst treating customers fairly. I would like to thank all my colleagues for their efforts over the past 15 months and for their continued commitment to UKAR. I also wish to thank the Board and Executive management team for their ongoing support.

Richard Banks

Chief Executive Officer

2 June 2014

Key highlights

Highlights of 2013/14

During the period we have made significant progress against all our key objectives and overall mission of maximising value for the taxpayer. Internally, UKAR measures its financial performance against the following four key performance indicators:

Financial Measure	15 months to March 2014	12 months to December 2012
Underlying Profit Before Tax	£1,523.2m	£1,096.9m
Government Loan Repayments	£5.1bn	£3.1bn
3m+ Residential Arrears	15,483	25,581
Ongoing Administrative Expenses	£244.5m	£207.3m

For the 15 month period to March 2014, underlying profit was £1,523.2m (12 months to December 2012: £1,096.9m). Underlying profit for the 12 months to March 2014 has increased by £185.5m to £1,259.1m (12 months to March 2013: £1,073.6m). The increase in profits was primarily due to a lower impairment charge, as the result of continued improvements in the level of arrears and increased House Price Inflation.

Government loan repayments of £5.1bn and other payments of £1.1bn (interest, fees and tax) were made to taxpayers for the 15 months. This brings total government loan repayments to £10.4bn since the formation of UKAR in October 2010 and the total payments to taxpayers to £13.2bn.

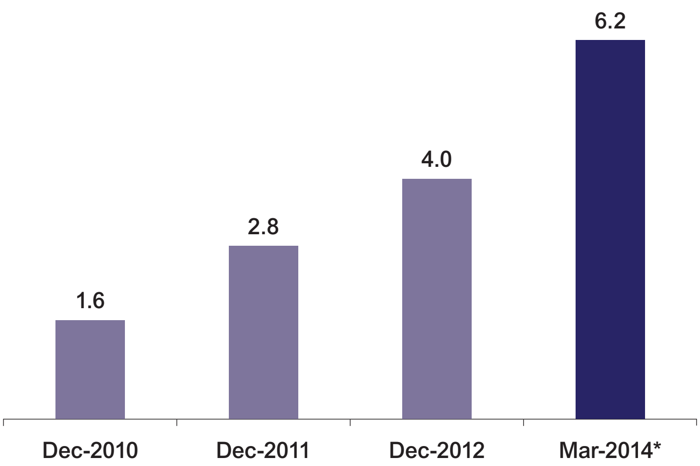
Absolute arrears levels for both B&B and NRAM continue to fall as a direct consequence of proactive arrears management coupled with the continued low interest rate environment. The total number of mortgage accounts three or more months in arrears, including those in possession, reduced by 39% from 25,581 at 31 December 2012 to 15,483 cases as at 31 March 2014.

Ongoing administrative expenses (i.e. excluding £1.8m UKARcs costs) for the 15 months were £244.5m (2012: £207.3m) and £188.0m for the 12 months to March 2014, which is 9% lower than the 12 months to March 2013 (£207.5m). Costs are expected to fall further in the coming year due to a full year of IT costs at the lower run rate and other cost reductions as the size of the balance sheet reduces.

In addition, we completed the £400m sale of the NRAM standalone unsecured personal loan book.

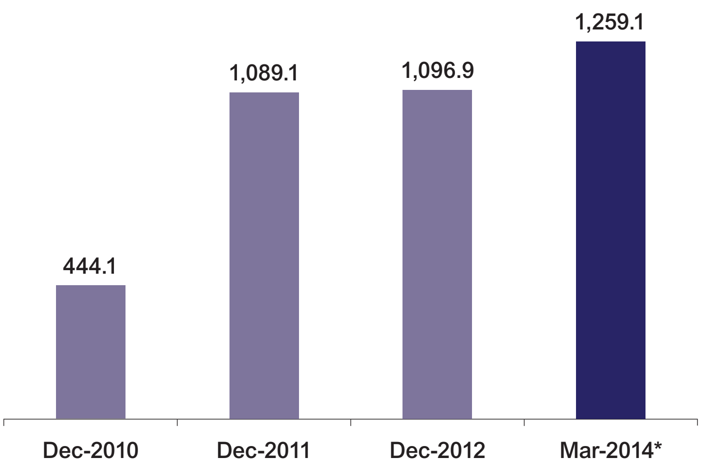
Please see pages 40 to 51 for a full review of the 2013/14 financial performance.

Total cash payments to HM Treasury (£bn)



* 15 months to March 2014

Underlying profit (£m)



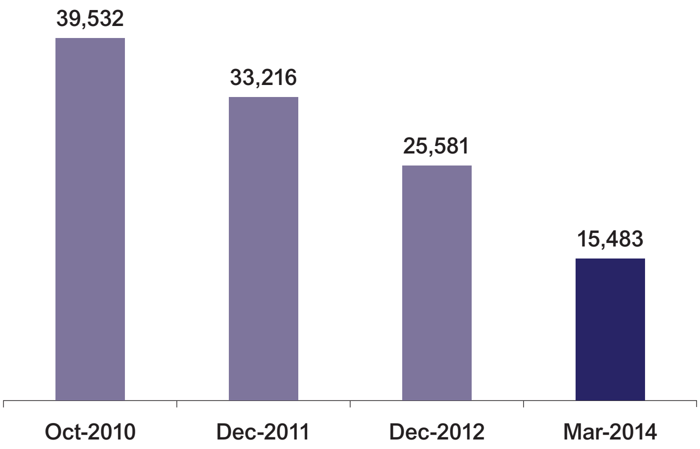
* 12 months to March 2014

Key highlights (continued)

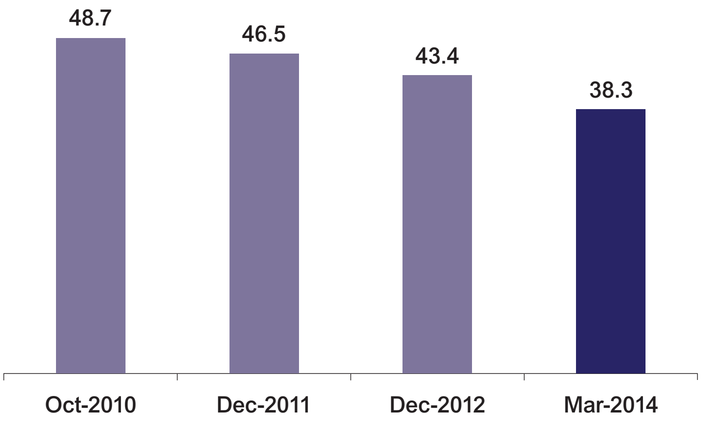
Highlights of 2013/14 (continued)

Since the formation of UKAR in October 2010 we have made significant progress towards our long term objectives by reducing arrears, repaying government loans, reducing the balance sheet and driving cost effectiveness.

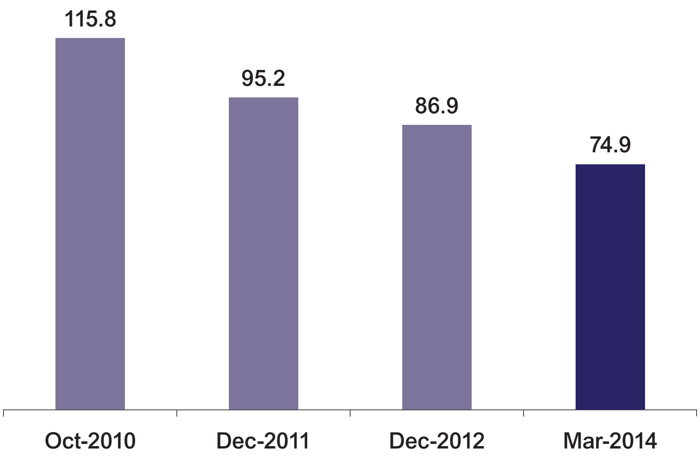
3m+ arrears down 61%



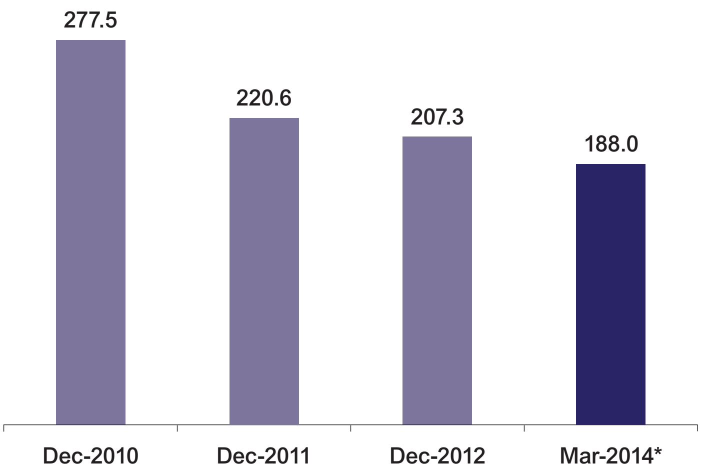
Repaid £10.4bn of government loans



Balance sheet assets (£bn) down 35%



Ongoing operating expenses (£m) down 32%



* 12 months to March 2014 excluding UKARcs costs of £1.8m

Strategy and operating environment

Company strategy

On the formation of UKAR in October 2010 it was anticipated that our strategy would involve three elements which have been implemented in parallel:

(1) Repair and prepare

'Repair and Prepare' focussed on the formation of UKAR, the definition of UKAR's mission and strategy and implementation of an efficient, integrated operating model. This has included the transfer of all our mortgages onto a single system, the migration to a new IT provider and the exit from the Gosforth site.

Under this phase we agreed the UKAR strategic objectives that have underpinned all that UKAR is doing. These objectives were as follows:

- To reduce, protect and optimise the Balance Sheet;
- To maximise cost effectiveness and efficiency though continuous improvement;
- To be excellent in customer and debt management; and
- To be a great place to work.

This stage of the process is now largely complete.

(2) Implement and improve

'Implement and Improve' is the increasing focus on maximising the value of the mortgage book through optimising redemptions and minimising losses. Here our proactive customer strategy is to engage with our customers, understand their circumstances and design appropriate strategies. During 2013/14 the focus has been on contacting our interest only customers with less than ten years remaining on their mortgage. Moving forward we intend to accelerate contact programmes for other cohorts of customers, for example those most susceptible to interest rate rises.

(3) Realise and release

'Realise and Release' focuses on extraction of value by selling parts of the book to accelerate the repayment of the government loans. An example of this was the sale of the NRAM standalone unsecured personal loan book during 2013/14.

We are now in much better shape than when UKAR took control of B&B and NRAM in October 2010. We have created an efficient and profitable mortgage service provider and debt collection business demonstrating better than industry performance. We have also partnered with leading IT suppliers to upgrade our systems. Therefore, as the economy continues to improve, the Board is looking to the future and continues to keep under review options for accelerating the repayment of government debt and realising value from the operational expertise that has been developed. Irrespective of this our continued focus is on the repayment of the government loan and the careful management of our customers, so that we maximise value for the taxpayer.

Customer strategy

Our colleague survey demonstrates clearly that our people are very committed to providing excellent customer service and are focused on ensuring we the do the right things for our customers. UKAR has almost 467,000 customers (2012: 614,000), with 529,000 mortgage accounts (2012: 586,000) and 119,000 unsecured personal loan accounts (2012: 228,000).

Support for customers experiencing payment difficulties

More than 93% of mortgage customers are up to date with their mortgage payments, however we do have a significant number of customers who are finding it difficult to meet their repayments. In these cases, we work closely with customers to offer a range of solutions to help them manage their circumstances. During the 15 months, 60,000 arrangements were successfully completed and approximately 2,000 account modifications were made (2012: 4,000) to assist customers with the repayments of their mortgage.

Research conducted by YouGov and the Money Advice Service shows that individuals who seek advice are twice as likely to have their debt become manageable within 12 months compared to those who do not. We work proactively with not-for-profit debt advice agencies who provide free assistance to help customers reorganise their finances and ensure, wherever possible, that they can continue as homeowners. We signpost their services to our customers, however, as a consequence of our proactive approach and the significant reduction of customers in arrears, the number of debt advice referrals has fallen in the last 15 months to 4,761 (2012: 6,073).

In some circumstances, however, the most appropriate course of action is for the customer to sell their property and we support this process, where suitable, through assisted voluntary sales. Repossession proceedings for customers in arrears are viewed as a last resort but in some situations this is inevitable and the best course of action to prevent further indebtedness. The number of properties taken into possession continues to slow, totalling 6,996 in the 15 months, an average of 466 per month (2012: 7,326; 611 per month).

Where a buy-to-let landlord is in arrears we endeavour to protect tenants by honouring the terms of all valid Assured Short Hold Tenancy agreements and instructing a Law of Property Act receiver to collect rent directly from the tenant, thereby enabling the tenant to stay in the property for the duration of any agreement.

Strategy and operating environment (continued)

Customer strategy (continued)

Proactive customer engagement

A key objective for UKAR is to work with customers to ensure we achieve the most appropriate outcome for their particular situation. In addition to our contact strategies for customers in financial difficulty, a further area of focus is to ensure our interest only customers have plans in place to repay their mortgage at the end of their term. We have been proactively contacting interest only customers with mortgage terms of ten years or less remaining. Of the 31,000 customers contacted, half have responded and shared their repayment plans with us. Many have also signed up to our Interest Only Review Programme so we can remain in contact with them in the future.

We are now developing a series of other contact programmes to cohorts of customers who may be more at risk when interest rates begin to rise, for example those customers who will still be repaying their mortgages in retirement. Our focus is on helping customers think about and plan their financial future.

Doing the right thing for our customers

Since the creation of UKAR we have been remediating a series of errors of process and procedure inherited from the legacy businesses. When we find these our intent is to do the right thing and ensure our customers have suffered no detriment. If they have then we will endeavour to recompense them. The most significant of these have been the mis-selling of Payment Protection Insurance (‘PPI’) and the issue of non-compliant CCA loan documentation to certain customers.

Although PPI complaints are slowing, new claims continue to be received, fuelled by the activities of Claims Management Companies (‘CMC’s’) who will charge customers a fee. Where a customer believes they have a claim they should contact us directly. Additional provisions of £71m have been set aside for the settlement of future PPI claims and other inherited issues. This brings total provisions for customer redress in the 15 month period to £116m.

People strategy

UKAR’s Vision is ‘Creating Success Together’ and we believe colleagues are the differentiating factor in delivering strong and sustained performance.

Being a Great Place to Work is one of our four strategic objectives. We believe it is important that colleagues feel valued, are proud of the contribution they make and are given the opportunity to grow and learn new skills. Colleagues who enjoy their work strive to do the best they can which increases productivity, gives better service to our customers and maximises value for the taxpayer.

Values

The values, behaviours and standards that underpin the way we do business were shaped by colleagues through a series of manager events, focus groups, surveys and interviews. We wanted to ensure that everyone had an opportunity to have their say in the creation of our values which are embedded from the approach we take to recruiting colleagues through to our performance framework, our training programmes and how we incentivise and thank colleagues for the work they do. It is not just ‘what’ is delivered, it is ‘how’ it is delivered and the behaviours that our colleagues demonstrate as part of their day-to-day work.

Engagement

We have developed an ‘engagement framework’ which encompasses all aspects of colleague life at UKAR and we track how we are doing against key areas by way of a twice yearly colleague engagement survey. Our most recent survey in February 2014 had an excellent response rate, with 83% of colleagues sharing their views. Our survey tracker score, based upon five key questions measuring UKAR as an employer, rose 4 points to a record high of 81%, which is above the benchmark figure provided by our survey business partner, People Insight.

Diversity

UKAR treats colleagues as individuals and we recognise the benefits of having a diverse workforce. Appointments and promotions are made according to the ability to meet the requirements of the job. UKAR’s workforce comprises 60% female to 40% male colleagues. On the Board we have one female (13%) and eight male (87%) directors. Two of the six members (33%) of the Executive Committee and 32% of the Senior Leadership Team are female compared to none and 21% respectively upon the formation of UKAR.

Learning & development

UKAR invests significantly in improving performance and increasing employability and we aim to provide an average of six days development per colleague each year. We also support a wide range of learning from process and operational training through to professional study. During the period we delivered 19,328 days of training and 86% of colleagues have undertaken development programmes to support their career.

In 2010 we introduced our Apprenticeship Scheme and we currently have 20 apprentices within the business and intend to recruit a further 20 in the coming year. Our Undergraduate scheme continued with four more internships in 2013 and we launched our Graduate scheme with three placements and plan to recruit seven more in 2014. We also support the government’s Centre of Excellence initiatives.

Well-being

UKAR supports colleagues through various ‘well-being’ programmes, offering membership of a private medical insurance scheme or the opportunity to contribute towards a healthcare cash plan and access to the Employee Assistance Programme.

We encourage colleagues to support our communities as detailed in the community section on page 13.

Strategy and operating environment (continued)

People strategy (continued)

Recognition

We have a popular recognition scheme enabling colleagues to show their appreciation to others by sending an e-card or by means of other on-the-spot awards. Colleagues who are an inspiration to others by living the UKAR values, going the extra mile, delivering superior performance or demonstrating exemplary behaviour can be nominated for quarterly and annual awards. We also celebrate the work of teams across UKAR by having a team of the quarter and team of the year scheme.

Community and environmental strategy

Community

We are committed to:

- Using the skills of the business to support education in our communities;
- Building the skills of our colleagues through community engagement; and
- Supporting colleagues with their own community and charity initiatives.

During 2013/14, UKAR supported Heart Research UK as our corporate charity and at each major site we also supported a local charity chosen by our colleagues. These were Yorkshire Air Ambulance in Crossflatts and Grace House Children's Hospice in Doxford. The total amount raised for these and other charities in 2013/14 was £49,939. In addition, UKAR matched employee fundraising to the total of £35,809 and payroll giving totalled £19,037.

UKAR's corporate charity in 2014/15 is MIND and our site charities are Martin House Children's Hospice in Crossflatts and Daft as a Brush Cancer Patient Care in Doxford.

Colleagues in UKAR are given the opportunity to volunteer to help our communities by working with Young Enterprise, a charity set up to work with schools to inspire young people with the confidence, ability and ambition to succeed in a challenging and changing economy.

Environment

We are committed to:

- Reducing environmental impact wherever possible;
- Increasing recycling programmes; and
- Creating awareness of environmental programmes and engaging colleagues in these activities.

We seek to improve our environmental performance through a range of initiatives and in 2013/14 we achieved the following:

Recycling	95.97% of waste recycled.
Landfill	4.03% of waste sent to landfill.
Carbon emissions *	Reduced by 2.7%.

* Carbon produced from utilities (Gas/Electric consumption).

Further details on our community and environmental strategy can be found at pages 56 and 57.

Risk overview

UKAR adopts an Enterprise-wide Risk Management Framework ('the Framework') which is designed to support the identification, assessment, management and control of the principal risks that threaten the achievement of UKAR's strategic and business objectives. The Framework sits alongside the Ten Year Business Plan, the Capital Statement and the Liquidity Statement in defining the high-level architecture of UKAR's business planning and risk management processes. The Framework itself is underpinned by UKAR's Risk Appetite Framework and a suite of high level risk policies which define the breadth of UKAR's exposure to inherent risks, and the management of these risks within appetite. The scope of the Framework extends to all principal risk types faced by UKAR. The table below illustrates the principal risk categories which could impact the delivery of the strategic objectives, key mitigating actions, key indicators and the 2014/15 focus.

Principal risk	Key mitigating actions	Key indicators	Focus 2014/15
Conduct risk The risk of UKAR treating its customers unfairly and delivering inappropriate outcomes leading to customer detriment or impacting market integrity.	• Conduct Risk Framework to ensure customers are central to the delivery of our objectives. • Conduct risk assessments are integral to all business change and customer initiatives. • Conduct Risk Dashboard tracked and actioned by relevant committees.	• Volume of upheld complaints. • Market Regulatory Indicators. • Internal quality assurance results. • Incentive scheme tracking.	• Appropriate customer outcomes. • Complaint Root Cause analysis and handling. • Cultural embedding.
Operational risk The risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.	• Quarterly Risk & Control Self Assessment (RCSA) process to identify and assess key operational risks. • Scenario analysis to determine the potential impact of high impact, low likelihood events. • Forward looking Key Risk Indicator monitoring to proactively identify shifts in risk exposure. • Loss event monitoring to identify control failures and appropriate corrective action.	• Comparison of scenario analysis and RCSA financial impacts against defined risk appetite. • Number and value of operational risk loss events. • People risk metrics (attrition and absence). • Systems risk metrics (availability and security incidents).	• Investment in core IT systems to limit systems outages and security breaches. • Tracking of operational loss events and subsequent control improvements. • Cyber risk exposure given continued concerns publicised by government agencies and the press. • Ongoing monitoring of people and process risks associated with a reducing business.
Credit risk The current or prospective risk to earnings or capital arising when a customer (residential or commercial) or counterparty defaults on its contractual obligations to the company.	• Credit Risk Policy, incorporating Board approved risk appetite to support the ongoing management of credit risk. • Forbearance Programme structured to support customers through periods of distress. • Dedicated Credit Risk Committee and robust processes and controls to identify credit risk exposures and action appropriate mitigation. • Euro and US dollar cash balances are held at a range of highly rated banks.	• Impairment Charge • Loan to Value • Arrears	• Manage the credit risk on the underlying mortgage book. • Interest Only Repayment Strategy. • End of Term Account Management. • Move to single credit reference data supplier including a refresh of customer income data held.
Strategic risk The current or prospective risk to earnings and / or fair value, given the B&B and the NRAM balance sheet structures, arising from changes in the business environment and from adverse business decisions, improper implementation of decisions or lack of responsiveness to changes in the business environment.	• Governance Structure. • Enterprise Wide Risk Management Framework. • Risk Appetite Framework. • Risk Policies. • Capital Assessment Framework.	• Material risks managed within defined risk appetite.	• On-going monitoring of strategic risks with the potential to significantly impact the delivery of strategic objectives. • Regulatory Change. • Potential impact of Scottish independence 'Yes' vote.
Liquidity risk The risk that either B&B and / or NRAM are unable to meet their obligations as they fall due.	• The defined appetite for liquidity risk is low. Sterling liquidity is held as cash balances at the Bank of England. • Stress & Scenario Testing is undertaken to ensure that B&B and NRAM will be able to meet their obligations in extreme conditions.	• Changes in the maturity profiles of assets and liabilities. • Level of liquidity.	• Manage liquidity to ensure UKAR has adequate levels of liquidity to meet its commitments at all times and maintain liquidity within levels agreed with HM Treasury facilities and the Liquidity Risk Policy.
Market risk The risk that changes in the level of interest rates, the rate of exchange between currencies or the price of securities or other financial contracts, including derivatives, will have an impact on the results of operations or the financial condition of B&B and / or NRAM.	• Market risk is managed and monitored within defined risk appetite and policy. • B&B and NRAM use derivative instruments to mitigate the market risk exposures. • Stress & Scenario testing is undertaken to ensure losses are acceptable even under extreme conditions.	• The sensitivity of interest income to changes in market rates. • Variations on the rate of repayment of fixed rate mortgages.	• Manage market risk within defined risk appetite.

Richard Banks
Chief Executive Officer, on behalf of the Board
2 June 2014

Directors' Report

Corporate governance

Introduction

UKAR is the holding company established on 1 October 2010 to bring together the government owned businesses of B&B and NRAM.

UKAR is 100% owned by the UK government which exercises control through UKFI. UKFI was set up on 3 November 2008 to manage the government's investments in Royal Bank of Scotland, Lloyds Banking Group, Northern Rock and Bradford & Bingley.

UKAR governs and controls NRAM and B&B, as their sole shareholder. Although managed under a common board and management structure, NRAM and B&B (the 'Principal Subsidiaries') remain separate legal entities and continue to operate as individual companies with their own individual brands and balance sheets.

This corporate governance section summarises the governance regime applicable to UKAR including its Principal Subsidiaries referred to above (the 'Group') at the date of this report.

UKAR Corporate Services Limited

In 2013, UKAR was appointed by HM Treasury to be the administrator of the Help to Buy: mortgage guarantee scheme on its behalf. The administration of the Scheme is kept separate from UKAR's core responsibilities through a separate company, UKARcs.

Governance structure

The governance structure for the Group is determined by a framework document ('the Framework Document') agreed between UKAR and its Shareholder, HM Treasury. The Framework Document has been updated periodically to reflect changing circumstances and the Group operates in accordance with the terms of the latest revision to the Framework Document, 'UK Asset Resolution Limited and UK Financial Investments Limited: Relationship Framework Document'. The Framework sets out how the relationship between the Group and UKFI, acting on behalf of HM Treasury, will work in practice. The terms of this agreement are reflected below and throughout this report.

The Framework Document is intended to ensure that the relationship between the companies in the Group, UKFI, HM Treasury (as Shareholder and the provider of financial support) and the FCA (as regulator), operates in the context of the over-arching objective of maximising value for the taxpayer, whilst paying due regard to the maintenance of financial stability and to acting in a way that promotes competition. The Framework Document requires the Group to set strategic aims and develop a business plan to achieve the overarching objectives.

Principles of the Framework Document

The relationship between the Group and UKFI operates according to the following principles under which UKFI:

- Appoints the Chairman of the Board and is entitled to appoint one or more Non-Executive Directors;
- Is required to consent to the appointment of other members of the Board proposed for appointment by the Nomination Committee and agrees the terms on which the Directors are appointed, remunerated and incentivised;
- Agrees with the Board the high level objectives of the business plan ('the Plan') and any revisions to it;
- Reviews with the Board from time to time the Group's strategic options;
- Requires that the Board is accountable to it for delivering the agreed Plan;
- Gives the Board the freedom to take the action necessary to deliver the Plan;
- Monitors the Group's performance to satisfy itself that the Plan is on track; and
- Is to be informed if the Group proposes to take certain significant actions and provide prior written consent before such action is taken.

Monitoring performance

UKFI monitors the Group's performance against the Plan by means of the following main mechanisms:

- Meetings between the Group and UKFI to review performance to date against the Plan; and
- Monthly (or, at UKFI's request, more frequent) financial and business performance monitoring to track the progress of the Plan and the Group's performance against agreed objectives on a timely, regular and appropriate basis.

In addition, UKFI has certain monitoring and information access rights and its approval must be obtained for certain material actions and transactions.

Our Board

UKAR, B&B and NRAM share a common Board of Directors. The individual profiles included in this section, therefore, set out the Directorships of all three companies.

Richard Pym – Non-Executive Chairman

Richard became Chairman of UKAR in July 2010 having been appointed Chairman of B&B in November 2008 and NRAM in January 2010. He also chairs the Nomination Committees of all three companies and the Transaction Approvals Committees of B&B and NRAM.

Richard is a Non-Executive Chairman of The Co-operative Bank plc, BrightHouse Group plc and Nordax Finans AB. He was Group Chief Executive of Alliance & Leicester plc until July 2007. Formerly, he was a Non-Executive Director of Old Mutual plc, Selfridges plc, The British Land Company plc and Chairman of Halfords Group plc. Richard is a Fellow of the Institute of Chartered Accountants in England and Wales.

Corporate governance (continued)

Our Board (continued)

Kent Atkinson – Senior Independent Director

Kent joined the Boards of UKAR and B&B in October 2010, and has been a Non-Executive Director of NRAM since January 2010. He is our Senior Independent Director, Chairman of the Audit Committees and a member of the Risk Committees of all three companies.

Kent was previously Group Finance Director of Lloyds TSB plc and subsequently a Non-Executive Director. He is a Non-Executive Director, Chairman of the Audit Committee and a member of the Risk Committee of the Bank of Ireland Group. Previously he was a Non-Executive Director and a member of the Audit Committee and Mergers & Acquisition Committee of Gemalto NV; the Senior Independent Director and Chairman of the Audit Committee of Coca-Cola HBC SA; a Non-Executive Director, Chairman of the Group Audit and Compliance Committee and a member of the Risk and Investment Committees of Standard Life plc; a Non-Executive Director, Chairman of the Audit Committee and a member of the Risk Committee of Northern Rock plc; the Senior Independent Director and Chairman of the Audit Committees of Cookson Group plc and Telent plc (previously Marconi Corporation plc), and a Non-Executive Director and a member of the Audit Committee of Millicom International Cellular S.A.

Richard Banks – Chief Executive Officer

Richard became Chief Executive Officer of UKAR in July 2010 and was appointed Chief Executive Officer of B&B and NRAM in October 2010. He is also a member of the Transaction Approvals Committee of B&B and NRAM.

Before joining the Board of B&B in May 2009, Richard's career has been in retail and commercial banking. He was previously a Director of Alliance & Leicester plc where he was Group Risk Director and before that Managing Director of Commercial Banking. Richard is an Associate of the Chartered Institute of Banking. He is also a Non-Executive Director of Shop Direct Financial Services Limited, ICICI Bank UK PLC and Liverpool Compact, which provides work experience for 14-19 year olds.

Michael Buckley – Non-Executive Director

Michael joined the Boards of UKAR and NRAM in October 2010 and has been a Non-Executive Director of B&B since July 2007. He is a member of the Audit, Risk and Nomination Committees of all three companies and the Transaction Approvals Committees of B&B and NRAM.

Michael is Non-Executive Chairman of DCC plc. He is also a senior advisor to a number of privately held Irish and US based companies and is an Adjunct Professor at the Department of Economics at NUI University College, Cork. He was Group Chief Executive of Allied Irish Banks plc from 2001 to 2005 having earlier served as Managing Director of AIB Capital Markets and AIB Poland. From April 2003 until April 2012 he was a Non-Executive Director of M&T Corporation in the USA. He was Managing Director of the NCB Group and a senior public servant in Ireland and the EU.

Sue Langley – Non-Executive Director

Sue joined the Boards of UKAR and B&B in October 2010, having joined the Board of NRAM in January 2010. She is Chairman of the Remuneration Committee and a member of the Nomination Committee of all three companies.

Sue is CEO of UK Financial Services – UKTI and a Non-Executive Director for the Home Office. Previous roles include Director of Market Operations and a member of the Executive Team for Lloyd's of London, Chairman of Lloyd's Japan and Director of Lloyd's Asia, Chief Operating Officer and a member of the Executive Team of the Hiscox Group and Board member for Hiscox Syndicates and Hiscox Insurance. She joined Hiscox from PricewaterhouseCoopers where she was a Principal Consultant working with a range of FTSE companies.

Keith Morgan – Non-Executive Director

Keith joined the Boards of UKAR and B&B in October 2010, having joined the Board of NRAM in January 2010. He is a member of the Risk and Remuneration Committees of all three companies and the Transaction Approvals Committee of B&B and NRAM.

Keith is CEO of the British Business Bank and a Director of British Business Bank Plc. He is also a Director of Capital for Enterprise Limited and Subsidiaries.

He was formerly a Director of UKFI and its Head of Wholly-Owned Investments, responsible for managing the government's shareholdings of UKAR, B&B and NRAM until August 2012. He was also a Non-Executive Director of Northern Rock plc until its sale to Virgin Money in January 2012. Keith joined UKFI from Banco Santander where he was a Director of Sovereign Bancorp in the U.S.A. focusing on the integration of Sovereign into Santander. He was previously Director of Strategy & Planning at Abbey National, where he was a member of the Executive Committee and was also Chairman of Santander's Asset Management and Credit Card businesses in the UK. Before joining Abbey in 2004, Keith spent 18 years at L.E.K. Consulting, where he was a partner specialising in financial services.

John Tattersall – Non-Executive Director

John joined the Boards of UKAR and NRAM in October 2010, having joined the Board of B&B in April 2010. He is Chairman of the Risk Committees and a member of the Audit and Remuneration Committees of all three companies.

John retired as a partner in PricewaterhouseCoopers LLP in 2009, where he had worked since 1975, latterly as leader of the firm's Financial Services Regulatory Practice and a senior client relationship partner. He started his career in the financial services sector with Kleinwort Benson Limited in 1973. Until 2009 he was Chairman of the Risk and Regulation Committee of the Financial Services Faculty of the Institute of Chartered Accountants in England and Wales, and a member of the faculty board. He is currently a Non-Executive Director of UBS Limited, R Raphael & Sons PLC (Raphael's Bank), CCLA Investment Management Limited and the South East Institute for Theological Education and Diocesan Trustees (Oxford) Limited. He is Chairman of the Oxford Diocesan Board of Finance, RC Bond Holdings Limited and Retail Charity Bonds Plc. He is also Chairman of the Gibraltar Financial Services Commission, Chairman of the court of the Royal Foundation of St Katharine, and a non-stipendiary priest in the Church of England. He acted as Consultant Editor and joint author of two books 'A Practitioner's Guide to the Basel Accord' and 'A Practitioner's Guide to FSA Regulation of Banking', and served as a member of the Independent Commission on Equitable Life payments.

Corporate governance (continued)

Our Board (continued)

Christopher Fox – Non-Executive Director

Christopher joined the Boards of UKAR, B&B and NRAM in September 2013 after being appointed by UKFI to manage HM Treasury's shareholdings in the Companies. He is a member of the Transaction Approvals Committee of B&B and NRAM.

Christopher has extensive experience of financial services, having provided capital markets and investment banking advice to a wide range of financial institutions around the world. He was most recently head of UK banks coverage for UBS Investment Bank. Christopher joined UBS in 1993 and is a qualified accountant. He has an MA from Cambridge University.

Balance of Executive and Non-Executive Directors

The Board comprises a Non Executive Chairman, four independent Non-Executive Directors, one Executive Director and two Shareholder Directors. The Non-Executive Directors have experience in a range of commercial or banking activities. The Board has determined that the Non-Executive Directors are independent because of the commonality of purpose between UKAR and the Principal Subsidiaries and a rigorous focus on the identification of any specific conflicts of interest.

Relationship between the Chairman and the Chief Executive Officer

A clear division of responsibility exists between the Chairman, who is responsible for running the Board and the CEO, who has responsibility for running the business. This division is set out in writing and has been approved by the Board.

Board appointments and changes during the financial period

Details of Board appointments and changes during 2013/14 are as follows:

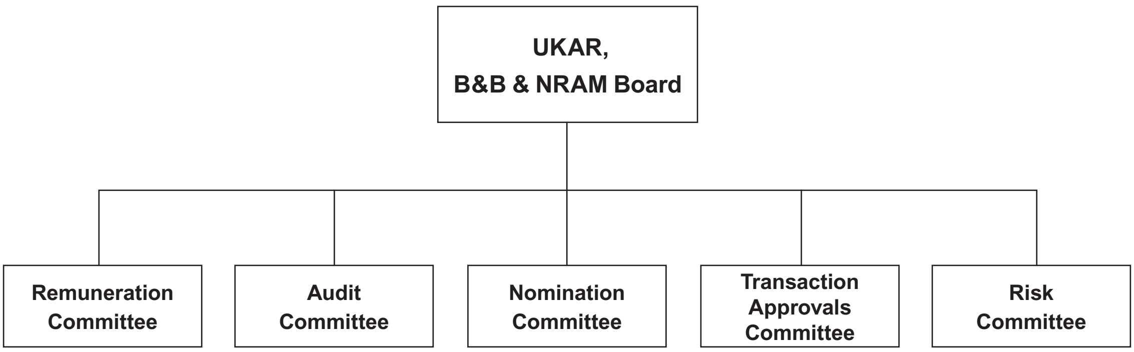
Richard Pym	Chairman for whole of 2013/14	Kent Atkinson	Senior Independent Director for whole of 2013/14
Richard Banks	Director for whole of 2013/14	Michael Buckley	Director for whole of 2013/14
Christopher Fox	Appointed 20 September 2013	Sue Langley	Director for whole of 2013/14
Phillip McLelland	Resigned 25 November 2013	Keith Morgan	Director for whole of 2013/14
Jim O'Neil	Resigned 20 September 2013	Louise Patten	Retired 31 December 2013
John Tattersall	Director for whole of 2013/14		

How the Board operates

Board structure and governance

In accordance with best practice outlined in the Code, the Board has delegated various powers and authorities to its Committees. They play a key role in ensuring the effectiveness of the corporate governance framework by supporting the Board and carrying out its functions.

The Board operates the following Committee structure:



The Principal Subsidiaries operate a Transaction Approvals Committee which is included in these accounts for a full understanding of the Group Committee Structure.

Corporate governance (continued)

How the Board operates (continued)

Board structure and governance (continued)

During 2013/14, the Chairman of each Committee was:

Committee	Chairman
Remuneration Committee	Sue Langley
Audit Committee	Kent Atkinson
Nomination Committee	Richard Pym
Transaction Approvals Committee	Richard Pym
Risk Committee	John Tattersall

Each of the Board Committees have a detailed terms of reference setting out their remit and authority. Details of the membership of each Committee are set out on the next page and the role and key activities in the individual Committee Chairman's reports. The Remuneration Committee Chairman's report is included in the Directors' Remuneration Report on page 22 and details of the role of the Remuneration Committee are provided on pages 22 and 23.

Board and Committee meetings

The Board and its Committees meet regularly. Board agendas are structured to allow adequate and sufficient time for discussions of the items on the agenda, particularly strategic issues.

The attendance of individual Board members at Board and Committee meetings during 2013/14, with the number of meetings each person was eligible to attend shown in brackets, is set out below.

Number of meetings held	Board 11	Audit 5	Nomination 2	Remuneration 7	Risk 5	Transaction Approvals * 3
Chairman						
Richard Pym	11 (11)		2 (2)			3 (3)
Senior Independent Director						
Kent Atkinson	10 (11)	5 (5)			5 (5)	
Independent Non-Executive Directors						
Michael Buckley	11 (11)	5 (5)	2 (2)		5 (5)	3 (3)
Sue Langley	10 (11)		2 (2)	7 (7)		
Louise Patten (retired 31.12.13)	9 (9)		2 (2)	6 (6)		
John Tattersall	11 (11)	5 (5)		1 (1)	5 (5)	
Non-Executive Directors						
Christopher Fox (appointed 20.09.13)	5 (5)					
Keith Morgan	10 (11)			7 (7)	5 (5)	3 (3)
Jim O' Neil (resigned 20.09.13)	6 (6)					
Executive Directors						
Richard Banks	11 (11)					3 (3)
Phillip McLelland (resigned 25.11.13)	8 (8)					2 (3)

* The Transaction Approvals Committee only relates to the Principal Subsidiaries. The Committee has not met since Christopher Fox was appointed.

During the period each of the Non-Executive Directors met the time commitment specified in their letters of appointment.

Board responsibilities

The Board's role is to provide leadership and oversight of the management of the Company in order to achieve its objectives. The Board is responsible for:

- Setting the Group's strategic aims and developing and recommending revisions to the Plan to deliver the over-arching objective of protecting and creating value for the taxpayer, paying due regard to the maintenance of financial stability and to acting in a way that promotes competition. Any proposed revisions to the Plan are subject to review and approval by UKFI;
- Delivering the Plan in accordance with the requirements of the Framework Document. In this respect, decisions on the day-to-day running of the Group, rest with the Board in accordance with the Directors' statutory, common law and fiduciary responsibilities. UKFI is committed to giving the Board the freedom necessary to deliver the agreed Plan and will not interfere in day-to-day operational and commercial matters; and
- Ensuring that the necessary financial and human resources are in place for the Group to deliver the agreed Plan, set the Group's values and standards and ensure that its obligations to HM Treasury as Shareholder are understood and met.

Corporate governance (continued)

How the Board operates (continued)

Board responsibilities (continued)

The Board has a written schedule of those matters reserved for its determination and those matters reserved for UKFI, in accordance with the Framework Document.

Key activities of the Board during 2013/14 included:
- Reviewing strategic options available to the Group, whilst ensuring that the overall objectives continue to be achieved;
- Considering and approving a refreshed Ten Year Plan;
- Receiving regular updates on finance, investment, risk and other key areas of the business to inform monitoring of progress against the Plan and future strategy; and
- Ensuring decision making at all levels reflects the fair treatment of customers.

Board appointments and composition

UKFI considers that the composition of the Board is a critical factor and seeks to secure an environment in which it shares a common view about Board composition and succession with the Chairman, including size, balance of experience and diversity. To achieve this and ensure that a common governance approach is applied, the Group operates under the following principles:
- The Chairman and either the Chairman of UKFI or a senior employee nominated by the Chairman of UKFI (the 'Nominated Officer'), will discuss and confirm Board composition and succession regularly in the light of performance and the requirements of the Plan;
- UKFI will be entitled to appoint to the Board one or more Non-Executive Directors nominated by UKFI (the 'Shareholder Directors'); Mr Fox and Mr Morgan are currently appointed as such Directors. The Group acknowledges that the Shareholder Directors intend to liaise with and report to representatives of UKFI from time to time in relation to the business of the Group and decisions made, or to be made, by the Board in order to assist with the exercise of their powers and duties as Directors;
- One or more senior representatives of UKFI will, if so requested by UKFI, attend meetings of the Board in an observer capacity;
- The Chairman will discuss with the Nominated Officer any impending changes to Board membership;
- The Chairman of the Nomination Committee will meet with the Nominated Officer as necessary to obtain UKFI's approval to any proposed Board changes before they become subject to the formal appointment/consent procedure. The Articles of Association require that at every Annual General Meeting each Director, other than the Shareholder Directors who are expressly exempt from this provision, shall retire from office and may offer themselves for re-appointment; the Shareholder Directors are exempt from this provision in respect of their appointments at the Principal Subsidiaries;
- Non-Executive Directors are appointed for a specified term, subject to re-appointment in accordance with the above procedures;
- The Chairman and the Non-Executive Directors each have a letter of appointment which sets out the terms and conditions of their Directorships, including fees payable and the expected time commitment;
- The Nomination Committee reviews the leadership needs of the Group, including succession planning for both Executive and Non-Executive Directors and, in particular, the key roles of Chairman and Chief Executive; and
- The Board will ensure that suitably rigorous appraisals are made of the effectiveness of the Chairman and the Board.

Board evaluation

The Board is committed to undertaking a formal and rigorous annual evaluation of its own performance and that of its Committees and individual Directors. During 2013, the Board and Committee evaluation exercise was conducted by the Chairman with assistance from the Company Secretary.

All Executive Directors, Non-Executive Directors and the Chairman participated in the annual appraisal to ensure that the operation of the Board and its Committees continued to be of the highest standard. The appraisal process consisted of questionnaires that canvassed Directors' views on a wide range of matters including:
- Effectiveness of the Board and how it works together as a unit;
- Role of the Committees and their interaction with the Board;
- Effectiveness of the Chairman;
- Board meeting process; and
- Composition of the Board.

The Company Secretary reported to the Chairman on the outcome of the evaluation exercise, which showed that the Board and its Committees are discharging their responsibilities effectively. Where the appraisal produced comments or recommendations to further improve effectiveness, these have been reviewed by the Board and, where appropriate, changes will be implemented during the course of 2014/15. The Chairman makes comment on the conclusions in his Chairman's Statement on page 5 of these accounts.

Evaluation of individual Non-Executive Directors has also been addressed directly by the Chairman.

Corporate governance (continued)

How the Board operates (continued)

Induction and training

The Group requires all newly appointed Directors to undergo a formal induction training programme appropriate to their skills and experience, to ensure that they:

- Are fully aware of and understand their role, duties and responsibilities as a Director; and
- Have a good understanding of the operation of the business, so as to contribute effectively.

The Group also requires Non-Executive Directors to undertake relevant ongoing training and development to improve their capabilities and thereby contribute more effectively to Board decision making.

A comprehensive thematic training programme is in place, which covers key areas of the business and topical issues, such as regulatory developments.

Board procedures

To ensure that the Group functions effectively, Directors have full and timely access to all information which may be relevant to the discharge of their duties and obligations. All Directors have access to the advice and services of the Company Secretary, who is responsible for ensuring that Board procedures and applicable rules are followed. Where necessary, Directors are able to take independent professional advice at the Group's expense.

Internal control and risk management

The Board is responsible for the Group's system of internal control and seeks regular assurance to satisfy itself that the system is functioning effectively in managing risks in the manner which it has approved. Such a system can only provide reasonable and not absolute, assurance against material misstatement or loss, as it is designed to manage, rather than eliminate, the risk of failure to achieve business objectives. Throughout the period ended 31 March 2014, the Group has operated a system of internal control, which includes an ongoing risk management process for identifying, evaluating and managing the principal risks faced by the Group. During the period, the Board has continued to review the effectiveness of the Group's system of financial and non-financial controls including operational and compliance controls, risk management and the Group's most material risks and mitigating actions.

In addition, as part of the process of preparing this statement, the Board has also performed its annual assessment of the effectiveness of risk management and internal controls. The Board of Directors is not aware of any material risk events or internal control failures that arose across the Group during 2013/14 that are not being addressed in accordance with the internal control procedures of the Group.

The Group is committed to developing and maintaining an appropriate risk management framework and culture with the aim of continuing to ensure that Management understand the key risks that the business faces. This is achieved through an organisational structure with clear reporting lines and governed by appropriate business monitoring mechanisms, codes of conduct and policy statements.

Under the risk management framework, the Group operates a risk management process, producing an enterprise-wide risk profile. This identifies the Group's principal risks, the probability of those risks occurring and their impact should they occur. Management regularly takes action to improve the design and operation of suitable controls, either as a result of its own initiative, or in response to reports from Internal Audit and other oversight review functions.

The risk management process is complemented by a formalised reporting and escalation process for control issues. Internal Audit has a key role in maintaining the control environment by providing independent assurance on the effectiveness of the Group's internal control systems. The Risk Committee and the Audit Committee oversee the risk management process, regularly consider the enterprise-wide risk profile and receive monitoring reports to update them on progress.

The system of risk management and internal control has been in place throughout 2013/14 and up to the date of approval of the Annual Report and Accounts.

In reviewing the effectiveness of this system, the Board takes into account the work of the Risk Committee which reviews the Group's principal risks and how these are being managed. The Risk Committee also considers reports from Compliance and from Management on the system of internal control, adherence to regulatory requirements and material control weaknesses, where these exist, together with actions taken to address them. The Audit Committee considers reports from Internal Audit and External Audit on the system of internal control and material control weaknesses, where these exist, together with actions taken to address them. The Chairmen of the Risk Committee and the Audit Committee report on the outcome of each meeting to the Board, where appropriate, and the Board also receives minutes of these Committee meetings.

Going concern

The Directors have assessed, in the light of current and anticipated economic conditions, the Company's and the Group's ability to continue as a going concern. As set out in note 1 to the Financial Statements and in the Annual Reports and Accounts of B&B and NRAM, HM Treasury has provided confirmation to the Directors of those two companies that it is HM Treasury's intention to fund those companies so as to maintain them as a going concern and has provided various on-demand facilities to each of those companies, to enable those companies to meet their debts as and when they fall due, for a period up to at least 1 January 2016. Accordingly, the Directors of B&B and NRAM are satisfied at the time of approval of these Financial Statements that the B&B and NRAM companies and groups have adequate resources to continue in business for the foreseeable future. The Directors of the Company confirm that, therefore, they are satisfied that the Company and the Group have adequate resources to continue in business for the foreseeable future and for this reason they continue to adopt the going concern basis in preparing the Financial Statements.

Directors' remuneration report

Sue Langley, Chairman of the Remuneration Committee, introduces the Directors' Remuneration Report and summarises the Committees' main areas of focus during 2013/14.

"As Chairman of the Remuneration Committee, I am pleased to present UKAR's report on Directors' Remuneration for 2013/14.

The work of the Committee during 2013/14 has covered a range of topics within our terms of reference, including monitoring of the reward strategy, oversight of performance review and bonus payments and alignment of remuneration with prudent risk management.

The committee works closely with UKFI on remuneration matters in line with the Shareholder Framework Agreement."

Chairman's overview of 2013/14

UKAR manages all colleagues, regardless of their position within the company, against the same set of reward principles which focus on fair and transparent remuneration.

Executive remuneration is aligned to UKAR's business strategy, aimed at delivering value for taxpayers. Base salaries are targeted at a mid-market level for companies of UKAR's size, to enable the business to retain talented individuals in key leadership roles. Variable remuneration is modest by comparison with market levels: annual bonuses are capped at 60% of base salary for excellent performance and the medium-term incentive plan has a maximum value of 20% of base salary per annum. Although UKAR is not subject to the variable pay cap introduced under the European Union Capital Requirements Directive it does comply with the cap. In addition, a large percentage of annual bonus is compulsorily deferred over a three year period and clawback provisions enable variable pay to be recouped in exceptional circumstances.

Performance conditions for annual bonus are directly linked to business goals including financial, operational and non-financial objectives. Financial objectives comprise: profitability, management of costs and repayment of government debt. Operational and non-financial criteria include customer service, management of arrears, people management and maintaining effective internal controls. The medium-term incentive scheme targets UKAR's performance over a three year period in repaying the government loan over and above the Ten Year Plan and/or delivering additional taxpayer value.

UKAR has performed strongly against all the performance criteria for 2013/14 and exceeded performance targets for the three years from 2010-2013 in respect of the medium-term incentive plan. For example, underlying profit before tax for 2013/14 was £1,523m and cumulative loan repayments to the government for the period 2011-2013 were £9.5bn. Strong performance against all the criteria is reflected in the performance-related remuneration levels detailed in this Remuneration Report.

Looking forward UKAR faces a number of challenges as the business starts to reduce in size. Our colleagues are fundamental to the success of our organisation and UKAR will continue to focus on ensuring it has the best people available to meets its needs. Consequently, the Remuneration Committee will continue to consider the approach to reward as the business evolves.

Although it is not required to do so UKAR continues to seek, as far as possible, to comply with the regulatory and governance requirements which apply to UK listed companies and the FCA's IFPRU Remuneration Code.

Given UKAR's extended financial period for 2013/14 additional figures have been provided to enable comparison with previous and future remuneration reports.

Role & membership of the Remuneration Committee

The Remuneration Committee membership and attendance at meetings is set out on page 19. Louise Patten retired from the Board and consequently her role on the Remuneration Committee on 31 December 2013. John Tattersall was appointed to the Remuneration Committee with effect from 1 January 2014.

Details of the skills and experience of Committee members can be found in the Directors' biographies on pages 16 to 18.

The Committee Chairman reports to the Board after each Committee meeting summarising the key matters discussed and the Board also receives the minutes of each meeting. The Remuneration Committee is responsible for:

- Making recommendations to the Board concerning Executive and other Code Staff remuneration arrangements.
- Recommending proposals in respect of related pay schemes.
- Overseeing any major changes in benefit structures.

The Chairman and Non-Executive Directors each have a letter of appointment which sets out the terms and conditions of their directorship, including fees payable.

Further details in relation to Board appointments is provided on page 20.

Directors' remuneration report (continued)

Role & membership of the Remuneration Commitee (continued)

Non-Executive Directors

The fees of the Chairman and Non-Executive Directors are set by the Remuneration Committee (Non Executives) consisting of Richard Banks and Christopher Fox.

As shown in the table below there has been no change to the majority of the fee levels for Non-Executive Directors in the reporting period. However, the Chairman, Richard Pym, voluntarily reduced his fee to £125,000 p.a. with effect from 1 July 2013.

Table 1 – Details surrounding fees for Non-Executive Directors

Element	Purpose and link to strategy	Operation	Maximum opportunity
Fees	To provide a competitive level of fees that reflect the skills, experience and time commitment required for the roles.	The ongoing effectiveness and appropriateness of the remuneration of the Chairman and the Non-Executive Directors is reviewed annually by the Executive Remuneration Committee and agreed by UKFI. All Non-Executive Directors take part in an annual evaluation process.	The fees for each Non Executive Director are provided below. Non-Executive Directors are not eligible to participate in any Group company's executive remuneration programme and receive no pension benefits.

Table 2 – Fees for the Chairman and Non-Executive Directors ('NED')

Per Annum	2013/14	2012	% Increase / Decrease
Chairman	£125,000*	£237,500	47% decrease
NED Base fee / Senior Independent Director	£47,500	£47,500	0%
Committee Chairman	£14,250	£14,250	0%
Committee Member	£4,750	£4,750	0%

*Reduced fee of £125,000 per annum effective from 1 July 2013.

Directors' remuneration policy

Policy overview

UKAR's Reward Policy applies to all colleagues across the organisation and is reviewed annually by the Remuneration Committee taking account of UKAR's business goals and public ownership. The policy is published and available to all colleagues internally.

The main purpose of the policy is to support the achievement of UKAR's overall business strategy by establishing an objective, consistent and fair reward system. This in turn provides a competitive yet cost-effective, salary, incentive and benefits package to all colleagues that reflects their role, competencies and the contribution they make, both now and in the future. The policy also seeks to support UKAR's unique circumstances and needs to be agile to respond to the changing economic and regulatory environment.

UKAR's reward policy aims to support the retention and attraction of high quality colleagues by differentiating reward for high performers. Reward is only one lever available to mitigate the risk of talented colleagues leaving the company and the reward policy is, therefore, aligned closely to the overarching HR strategy. This is becoming more important to UKAR's success given the contraction of the business and consequently the overall reward policy will be regularly reviewed.

UKAR recognises and consults with the Unite trade union and as part of the pay negotiations for all colleagues UKAR discusses its approach to pay for executives to ensure that the union are fully aware of the approach UKAR intends to take and have an opportunity to raise questions. In 2013/14, UKAR continued to apply a consistent salary review process across all of the company including executives and senior managers.

Directors' remuneration report (continued)

Directors' remuneration policy (continued)

The remuneration policy for directors

Table 3 – Key aspects of the remuneration policy for Executive Directors

Element	Purpose and link to strategy	Operation	Maximum opportunity
Base salary	To attract and retain key talent by ensuring an appropriate, competitive benefits package.	Roles are benchmarked externally. Salaries are reviewed by the Remuneration Committee and recommendations are submitted to the Board and UKFI, the shareholder representative, based upon the skills and experience they bring to the role.	The base salary for each Executive Director is confirmed later in the report. There is no prescribed maximum. However, the Remuneration Committee reviews the salary against the salary range each year before considering whether any increase is appropriate. They also consider the pay approach used for all UKAR colleagues. The approach to pay increases, including that for promotions / increased responsibility is in line with the approach taken for all colleagues.
Benefits	To provide a competitive package, aligned to market practice.	The benefit package for Executive Directors was agreed when UKAR was formed following external benchmarking. The package includes annual holiday entitlement, life assurance, car allowance, private medical insurance, income protection insurance, personal accident insurance and assistance with relocation, travel and accommodation where necessary. Individuals promoted to Executive Director from a below-Board role may retain entitlements under UKAR's Redundancy Policy.	Each benefit has its own maximum in line with the nature of the benefit and the policy that surrounds it.
Pension	To provide a competitive package, aligned to market practice.	Directors are either offered a pension allowance or employer contribution into UKAR's pension plan. The approach taken depends on the director's individual circumstances.	The pension allowance for the CEO is set at 30% of base salary. Other Executive Directors receive either a pension contribution of 15% of base salary or an equivalent cash allowance.
Short-term Incentive Plans ('STIP') (Annual Bonus)	To reward performance for delivery of key financial and operational targets.	UKAR's STIP is linked to achievement of the financial and operational targets in place for the relevant year (for 2013/14 this is a 15 month period), alongside personal performance. Given UKAR's status, all awards are made in cash as there is no option to award shares. From the 2014/15 year onwards, 60% will be paid initially with the remainder paid in equal instalments over the following three years. This reflects the FCA Remuneration code guidelines and is considered appropriate due to UKAR's business model. The Remuneration Committee approves personal objectives for the year for Executive Directors. Any potential awards, including deferrals, are subject to Remuneration Committee discretion and malus and clawback operates where appropriate. Should an event occur which the Remuneration Committee consider would materially alter achievement against targets, it has the discretion to change the personal objectives or targets. However, such change, in the opinion of the Committee, must not have the effect of making the performance objective or corporate assessments materially more onerous or easier to satisfy than it was immediately before the event in question.	Up to 60% of base annual salary in a 12 month period. *

Directors' remuneration report (continued)

Directors' remuneration policy (continued)

Table 3 – Key aspects of the remuneration policy for Executive Directors

Element	Purpose and link to strategy	Operation	Maximum opportunity
Medium-term Incentive Plan ('MTIP')	To reward performance for delivery of key metrics directly linked to UKAR's overarching strategy.	The MTIP measures performance over 3-year performance periods. MTIP performance periods run in sequence, rather than being a rolling annual grant programme with overlapping performance periods. Performance metrics are aligned to the repayment of loans made by the government and for delivering additional value for the taxpayer. Given UKAR's status, all awards are made in cash as there is no option to award shares. Under the 2011-2013 scheme the first payment of 20% of 2011 base salary was paid in March 2013. Another two payments both of 20% of 2011 base salary were paid in March 2014. All payments were made following achievement of the agreed targets. For the 2014/15 to 2016/17 MTIP cycle, vesting will take place following the end of the 3-year period, subject to the performance conditions. Any potential awards, including deferrals, are subject to Remuneration Committee discretion and malus and clawback operates where appropriate. Should an event occur which the Remuneration Committee consider would materially alter achievement against targets, it has the discretion to change the targets. However, such change, in the opinion of the Committee, must not have the effect of making the performance objective or corporate assessments materially more onerous or easier to satisfy than it was immediately before the event in question.	Up to 60% of base annual salary. The MTIP is not cumulative. The directors can only participate in one scheme at any time. Therefore, over the three year period of each scheme the average annualised payment is a maximum of 20% of base salary.

* Note – Given the Annual Report and Accounts are for the 15 months to 31 March 2014, a variety of different STIP payments are disclosed to cover different reporting periods.

Choice of performance measures and approach to target setting

UKAR has clear performance metrics understandable to every colleague in the business. The STIP scheme targets financial, operational and internal measures. Given the nature of its ownership and the focus on repaying government debt, the MTIP scheme is aligned to delivering additional government loan repayments and/or value for the taxpayer. Details of schemes are found in table 3.

Differences in remuneration policy for Executive Directors compared to other employees

The reward policy applies to all colleagues in the organisation and aims for objectivity, consistency and fairness. However, market practice means that to ensure UKAR remains competitive there are different benefits at various levels. Executive Directors' packages include higher holiday entitlement and employer pension contribution / allowance, increased car allowance, earlier eligibility for income protection insurance and eligibility for personal accident insurance. Executive Directors and the Executive Committee members ('ExCo') also have longer contractual notice periods.

A salary increase matrix applies to all colleagues including the Executive Directors with increases based upon an individual's position in their salary range and their personal performance.

Approach to recruitment and promotions

In the case of a new appointment to the Board the reward package is set in line with the structure agreed by the Remuneration Committee, as outlined above and also requires Board and UKFI approval.

The Remuneration Committee has the discretion to make additional awards to replace remuneration forfeited when a new Executive Director is appointed. Any awards would take account of the size of the award the individual was leaving behind, together with the vesting and performance conditions. The Committee has not made any such awards to date.

Service contracts & payments for loss of office

UKAR's policy is to employ Executive Directors on service agreements with 12 months employer notice periods. Wherever possible UKAR will seek to minimise any potential payments for loss of office. UKAR has not made any loss of office payments in this reporting period. Phillip McLelland resigned, therefore, his salary and benefits ceased in line with his contract termination date and he has no entitlement to any deferred incentive payments from previous years or payments due for the 2013/14 reporting period.

Directors' remuneration report (continued)

Directors' remuneration policy (continued)

Table 4 – Details of service contracts and loss of office payments policy

Provision	Detailed terms
Employer notice period	12 months
Termination payment	In the event of termination by the company, other than for misconduct, Executive Directors' contracts provide for 12 months' notice, or payment of base salary, pension and fringe benefits in respect of the unexpired portion of the notice period. 'Good leavers' , whose contracts have been terminated by the company, may also be eligible for: • STIP subject to assessment of the normal performance conditions and payable on the normal payment date, pro-rata by leave date; and • MTIP subject to the normal performance conditions and payment date, reduced pro-rata to the portion of the performance period that has expired. Individuals may also be eligible for statutory redundancy pay. Where an individual is appointed as an Executive Director through internal promotion, they may also retain eligibility for the company's redundancy policy which provides for a payment based on a number of weeks base salary per year of service. This does not apply to Richard Banks, as he was recruited from outside the organisation.

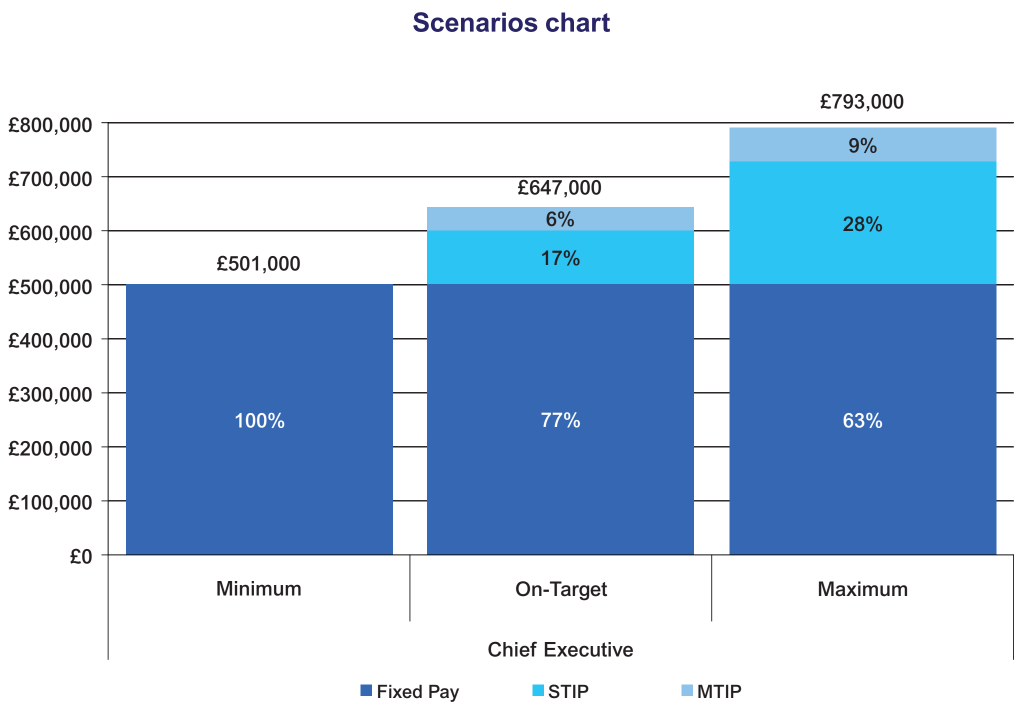
External non-executive director positions

Directors are permitted to take up external non-executive director positions at the Board's discretion, providing they do not conflict with their duties at UKAR. Where the appointment is not related to UKAR's business activity the Executive Director is permitted to retain any fees they receive.

Reward scenarios

The following chart shows how the make up of the executives' remuneration varies depending on performance.

Figure A: Executive Director total annual remuneration at different levels of performance



Assumptions:
Minimum = fixed pay only (salary + benefits + pension)
On-target = 50% vesting of the STIP, and MTIP awards (annualised)
Maximum = 100% vesting of the STIP, and MTIP awards (annualised)

Directors' remuneration report (continued)

Annual report on remuneration

This section of the report provides the detail behind the remuneration policy statements outlined earlier.

Remuneration for 2013/14

The tables below set out the earnings for both the Executive and Non-Executive Directors during the 2013/14 reporting year. As 2013/14 was a 15 month period, additional reporting periods are shown to enable like-for-like comparisons to be made.

Table 5 – Remuneration payments for Executive Directors (Audited)

	Richard Banks			
	January 2013 – March 2014	April 2013 – March 2014	January 2013 – December 2013	January 2012 – December 2012
Base Salary	£453,375	£364,500	£362,250	£348,975
Benefits (1)	£33,963	£27,149	£27,176	£27,362
Pension (2)	£136,013	£109,350	£108,675	£104,693
STIP Awarded (3)				
– STIP Non deferred	*£87,480*	*£69,984*	*£69,984*	*£36,972*
– STIP Deferred	*£131,220*	*£104,976*	*£104,976*	*£55,458*
MTIP Awarded (4) (5)	£138,720	£138,720	£138,720	£69,360
Total	**£980,771**	**£814,679**	**£811,781**	**£642,820**

	Phillip McLelland *			
	January 2013 – March 2014	April 2013 – March 2014	January 2013 – December 2013	January 2012 – December 2012
Base Salary	£250,916	£186,541	£250,916	£251,875
Benefits (1)	£9,942	£7,228	£9,880	£8,282
Pension (2)	£36,256	£26,600	£36,256	£37,781
STIP Awarded (3)				
– STIP Non deferred	-	-	-	*£39,140*
– STIP Deferred	-	-	-	*£58,710*
MTIP Awarded (4)	-	-	-	£50,000
Total	**£297,114**	**£220,369**	**£297,052**	**£445,788**

* Phillip McLelland left during the period and as such his payments are pro-rata. His base salary includes holiday pay due to accrued but untaken holiday.

1. This includes Private Medical Insurance and any allowances for housing or a car.
2. Richard Banks received a pension allowance. Phillip McLelland received employer pension contributions to the company scheme.
3. The STIP is deferred as described on page 31.
4. This was paid in line with scheme rules, as outlined in this report.
5. Richard Banks elected to defer his 2012 MTIP payment of £69,360, due for payment in March 2013, until his retirement from UKAR.

Directors' remuneration report (continued)

Annual report on remuneration (continued)

Table 6 – Remuneration payments for Non-Executive Directors (Audited)

	Fees[1]			
	January 2013 – March 2014	April 2013 – March 2014	January 2013 – December 2013	January 2012 – December 2012
Richard Pym	£206,563	£150,156	£175,313	£237,500
Kent Atkinson	£83,125	£66,500	£66,500	£69,125
Michael Buckley	£83,125	£66,500	£66,500	£67,041
Sue Langley [2]	£83,125	£66,500	£66,500	£69,125
Louise Patten	£57,000	£42,750	£57,000	£59,250
John Tattersall	£84,313	£67,688	£66,500	£69,125
Christopher Fox [3]	-	-	-	-
Keith Morgan [4]	£77,187	£61,750	£61,750	£20,583
Jim O'Neil [3]	-	-	-	-
Total	£674,438	£521,844	£560,063	£591,749

1. *Certain travel costs for board directors are considered taxable. The company considers that such travel is an essential requirement of directors duties and does not confer any personal benefit. Total tax paid to HMRC on behalf of directors was £12,305.71.*
2. *Until October 2013 Sue Langley's fees for her services were paid to Lloyds' of London.Therefore, January 2013 to March 2014 and January 2013 to December 2013 include £49,000, April 2013 to March 2014 include £33,250 and January 2012 to December 2012 include £69,125 paid to Lloyds of London.*
3. *Christopher Fox was appointed to the Board on 20 September 2013 as UKFI representative and replaced Jim O'Neil who resigned on the same date. As UKFI representative neither received any fees.*
4. *Keith Morgan is a UKFI appointed director but is not an employee of UKFI. As such he received fees.*

STIP for the period ending 31 March 2014

The individual targets used for the STIP scheme are based on key metrics and assessment of performance year-on-year. All elements are weighted equally and there is no recognition for overachievement, i.e. the targets are achieved or not achieved. In light of the achievement of all metrics, STIP for 2013/14 payments will be paid in full, dependent upon assessment of personal performance.

Table 7 – STIP Targets

	Measure	Actual	Weighting	Outcome
Financial	Underlying profit before tax	£1,523.2m	20%	Exceeded
	Costs	£244.5m	20%	Exceeded
	Government loan repayments	£5,124m	20%	Exceeded
Operational	Reduction in number of customers 3 months or more in arrears	15,483	20%	Exceeded
Non-Financial*	Balanced scorecard	Green	20%	Achieved

* These include measures of internal control, customer metrics and people management, which are evaluated on a Red, Amber, Green scale.

The individual objectives that then influence the performance rating for Richard Banks, which then determines the amount of incentive earned are detailed below. As Phillip McLelland resigned during the period and forfeited any right to incentive payments, his objectives are not included.

Table 8 – Richard Banks' 2013/14 Personal Objective Assessment

Objective Detail	Achievement
Lead the development of Balance Sheet Optimisation	Projects developed and implemented as approved by UKFI/HM Treasury in line with strategic objectives.
Lead the delivery of the change agenda	IT infrastructure transformation without major IT failures resulting and site consolidation completed.
Lead remediation agenda	Major remediation largely completed and a review of historic customer documentation also completed.
Lead colleagues to maintain the UKAR values and standards in line with principles of good governance and TCF, maintaining morale in a declining balance sheet.	Excellent business performance, high levels of colleague engagement and TCF standards maintained ensuring UKAR keeps the interests of customers and market integrity at the heart of the business.

The UKAR STIP comprises achievement of four financial objectives plus the balanced scorecard together with achievement of personal objectives which range from 'below expectations' at 0% to 'exceeds expectations' with a range of 40-60% for achieving five targets. Discretion is then applied in respect of the bonus ranges.

Directors' remuneration report (continued)

Annual report on remuneration (continued)

STIP for the period ending 31 March 2014 (continued)

Table 9 – STIP award matrix

Targets achieved	Exceeds expectations	Fully meets expectations	Developing in role	Partially meets expectations	Below expectations
5	60% – 40%	39.9% – 20.0%	19.9% – 5.0%	10.0% – 5.0%	0%
4	48% – 32%	31.9% – 16.0%	15.9% – 4.0%	8.0% – 4.0%	0%
3	36% – 24%	23.9% – 12.0%	11.9% – 3.0%	6.0% – 3.0%	0%
2	24% – 16%	15.9% – 8.0%	7.9% – 2.0%	4.0% – 2.0%	0%
1	12% – 8%	7.9% – 4.0%	3.9% – 1.0%	2.0% – 1.0%	0%

Richard Banks' annual performance was discussed at private sessions of the Remuneration Committee in March and May 2014 at which the majority of the Independent Directors and both UKFI representatives were present and subsequently with the Board. It was agreed that Richard Banks' had achieved all his personal objectives and that his leadership has driven the high performance of UKAR, and provided discipline and rigour to the activities of the business. It was agreed that his performance had 'exceeded expectations' which under the bonus scheme rules gives the Committee discretion in the range of 40%-60%, and the Board agreed with the recommendation to award him a bonus of 48%. This equates to £218,700 for the 15 month period.

Vesting of MTIP awards

UKAR operated an MTIP scheme which covered the period January 2011 to December 2013, with two payments paid in March 2014 linked to targets for the period 1 January 2011 to 31 December 2013. The targets for this scheme relate to driving additional shareholder value and/or early repayment of government loans.

The three year target was fully achieved. All awards are subject to clawback should a material adverse issue arise relating to personal and/or business performance which, in the opinion of the Remuneration Committee was not evident at the time that payment was made.

In 2013 Richard Banks volunteered to defer the first MTIP payment instalment under this scheme of £69,360 due to vest in March 2013 until his retirement or death-in-service. In March 2014 he received £69,360 in respect of achievement of 2013 targets, together with an additional match of £69,360 in respect of achievement of targets for the full three year period.

There have been no MTIP grants in the reporting period as the MTIP grant was made in 2011.

Given UKAR's status, all awards are made in cash as there is no option to award shares.

Total pension entitlements

Richard Banks receives a cash supplement of 30% of basic salary in lieu of UKAR pension benefit.

Phillip McLelland was a member of the UKAR Pension Plan, a Group Personal Pension Plan. The employer pension contributions that were paid to his Plan in the respective reporting periods until he left the employment of UKAR on 30 November 2013 are set out below.

January 2013 – March 2014	April 2013 – March 2014	January 2013 – December 2013	January 2012 – December 2012
£36,256	£26,600	£36,256	£37,781

None of the Executive Directors accrued any defined benefit pension during their tenure as a Director. Phillip McLelland was a member of the Bradford & Bingley Staff Pension Scheme in respect of service to 31 December 2009 prior to becoming a Director. At that date the scheme was closed to future accrual and from that date any salary increases ceased to impact the value of benefits.

During the reporting period, NRAM pension payments due to former Directors of the former Northern Rock plc, paid directly by NRAM and not connected to the Northern Rock Staff Pension Scheme were as follows (no similar payments were made by B&B during any of these periods):

January 2013 – March 2014	April 2013 – March 2014	January 2013 – December 2013	January 2012 – December 2012
£393,439	£316,584	£314,293	£303,760

Directors' remuneration report (continued)

Annual report on remuneration (continued)

Payments within the period to past directors for loss of office

There have been no payments made to any directors within the reporting period relating to loss of office. Phillip McLelland resigned as a director with effect from 30 November 2013 and in line with policy his salary and all benefits ceased with effect from this date. He also forfeited any entitlement to bonus payments under the year's incentive schemes and any deferred bonus payments.

Louise Patten stepped down as a Non-Executive Director with effect from 31 December 2013 and no payments were made for loss of office.

Percentage increase in the remuneration of the Chief Executive Officer

The table below shows a summary of year-on-year changes for a 12 month period for the Chief Executive Officer versus the rest of the colleague population. The change to fringe benefits is minimal with an increase in the cost of private medical insurance of £150 per annum for all colleagues with this benefit. The increase to Richard Banks' STIP is reflective of the fact that he volunteered to reduce his 2012 STIP by 35% given the discovery of the legacy CCA issue that required remediation in 2012. The increase in colleagues' bonus reflects the strong performance during the period.

Table 10 – Comparison of CEO remuneration change versus average employee's

	% change year-on-year*
Chief Executive	
– base salary	2.5%
– benefits	-
– STIPs	89%
Average per employee	
– base salary	4.2%
– benefits	-
– annual bonus	33%

* This information is based upon year-on-year comparison for colleagues who were in the business at both periods.

Performance

The table below shows a summary of Richard Banks' incentives that have been paid or vested since UKAR was formed, as compared to his total remuneration package.

Table 11 – Summary of CEO remuneration and incentives

	2011	2012	2013/14 (Apr 13 – Mar 14)	2013/14 (15 month)
Total remuneration	£596,697	£642,820	£814,679	£980,771
STIP (as % of maximum)	60%	43%	80%	80%
MTIP vesting (as % of maximum)	N/A	100%	100%	100%

Directors' remuneration report (continued)

Annual report on remuneration (continued)

Relative importance of the spend on pay

This section shows the percentage change in the cost of pay across the company, compared with statutory profit after tax.

Table 12 – Summary of colleague remuneration costs compared to statutory profit

	2012	2013/14*	% Change
Total remuneration costs for UKAR (salary, pension, bonus benefits)	£76.1m	£64.9m	(15%)
Profit after tax	£563.8m	£869.7m	54%

* Represents the 12 months to 31 March 2014.

External advisors

UKAR is advised by New Bridge Street ('NBS') who were appointed by the Remuneration Committee in 2011. The total fees paid to NBS in respect of its services to the Committee during the period were charged on a time spent basis and amounted to £33,454. NBS is a signatory to the Remuneration Consultants' Code of Conduct which requires it to provide objective and impartial advice.

External directorships

The table below outlines the external non-executive directorships that Richard Banks has held during the 2013/14 reporting period.

Phillip McLelland did not hold any external directorships whilst an Executive Director for UKAR.

Table 13 – Richard Banks' external directorships

Position	2012	2013/14 (15 month)
ICICI Bank UK	£60,000	£75,000
Shop Direct Financial Services Ltd	N/A	£11,600

Richard Banks was appointed a Non-Executive Director of Shop Direct Financial Services Ltd on 1 February 2014 and is stepping down from his directorship with ICICI Bank UK with effect from 30 June 2014.

How the policy will be applied in 2014 onwards

Reward will continue to play an important part in the delivery of UKAR's strategy, at executive level and across the organisation. This will become more important in the coming years as UKAR contracts and the attraction and retention of key staff becomes even more important.

2014/15 salary review

UKAR applies the same approach to salary uplifts for its Executive Directors as for the rest of the colleague population, with increases based upon a matrix of position against salary range and performance rating.

Richard Banks' current and previous salaries are as follows:

Table 14 – 2014 salaries for the Executive Director

Salary as at 1 January 2011	Salary as at 1 January 2012	Increase %	Salary as at 1 January 2013	Increase %	Salary as at 1 April 2014	Increase %
£340,000	£346,800	2.0%	£355,500	2.5%	£364,500	2.5%

Structure of STIP and MTIP

The maximum potential earnings under the STIP scheme for 2014/15 will be unchanged, with the financial and operational targets updated in line with UKAR's business plan. The MTIP for the 2014/15 to 2016/17 performance period will also continue to have the same maximum payment level as the previous MTIP.

The Remuneration Committee has reviewed the deferral and vesting structure for both STIP and MTIP, and brought it closer in line with market practice and FCA Remuneration Code requirements. MTIP payments for the 2014/15 – 2016/17 cycle will not vest until the three-year performance period is completed (under the previous MTIP, a third of the award vested after two years). In respect of the STIP, for performance from the next year which will run from 1 April 2014 to 31 March 2015, the percentage deferred will be 40% of the total award, rather than 60% that applied for prior years, in line with regulatory guidance. The combined effect of the change to the MTIP vesting and STIP deferral is that more than half of total variable remuneration is deferred, which is a higher deferral percentage than is required under the Remuneration Code for the size of variable remuneration at UKAR.

Directors' remuneration report (continued)

Annual report on remuneration (continued)

Performance targets for the STIP and MTIP awards to be granted in 2014 and beyond

UKAR's Balanced Scorecard has been adapted for 2014/15 to more closely align to the group's objectives of good conduct and appropriate customer outcomes being at the heart of what UKAR delivers. As a result of this change the financial and operational targets of profit, number of customers 3+ months in arrears, cost and government loan repayment will continue to determine the size of the bonus pot. However, the balanced scorecard will now reduce any potential payment by up to 40% if it is not green overall. The revised scorecard impacts annual bonus schemes across UKAR including that for Executive Directors.

The targets for both of these schemes have received Remuneration Committee, Board and UKFI approval.

For 2014/15 UKAR has reviewed its balanced scorecard to ensure that it continues to be aligned to customer outcomes. As a result of this change although the financial and operational targets of profit, number of customers 3+ months in arrears, cost and government loan repayment will continue to determine the size of the bonus pot the balanced scorecard will now reduce any potential payment by up to 40% if it is not green overall.

Approval

This Directors' Remuneration Report, including both the Policy and Annual Remuneration Report has been approved by the Board of Directors.

Signed on behalf of the Board of Directors.

Sue Langley

Chairman of the Remuneration Committee

Audit Committee Chairman's report

Kent Atkinson, Chairman of the Audit Committee, reports on how the Audit Committee discharged its responsibilities during 2013/2014.

"We have continued to ensure that there is strong management of UKAR's internal controls, working with the Risk Committee to maintain a coordinated approach. Establishing the appropriate level of provisions on the loan books is one of the most judgemental and high profile areas of the financial statements and represents a major element of our work. In addition, the challenge presented by the change in accounting reference date has been well managed through a clearly defined programme of activity."

Chairman's overview of 2013/14

The work of the Committee during 2013/14 has covered a variety of topics within our terms of reference, including:

- Oversight of the annual and interim Financial Statements, taking into account the change in year-end;
- Careful review of the level of impairment and customer redress provisions;
- Oversight in relation to the effectiveness of the systems of internal control;
- Review of the internal audit function, including approving its annual plan and monitoring its effectiveness; and
- Oversight of the effectiveness of external audit, including the approval of the year-end strategy and performance evaluation.

Audit Committee membership

The Audit Committee membership and attendance at meetings is set out on page 19.

Details of the skills and experience of Committee members can be found in the Directors' biographies on pages 16 to 18.

Audit Committee meetings were attended by members of ExCo, including the CEO, Finance & Investment Director and Risk Director, as well as representatives from other business functions from time to time.

The internal and external auditors attended each meeting and each held a separate private session with the Committee which was not attended by the Executive. The private sessions provided the opportunity for the Committee to discuss matters directly with the relevant audit teams.

The Committee Chairman reported to the Board after each Committee meeting, summarising the key matters discussed, and the Board has also received the minutes of each meeting.

Audit Committee responsibilities and activity in 2013/14

The Audit Committee is responsible for monitoring, reviewing and advising the Board on:

- All regulatory, prudential and accounting requirements that may affect the Group;
- The integrity of the Financial Statements and external reporting responsibilities;
- The effectiveness of the Group's systems of internal control and auditing plans;
- The Whistleblowing Policy;
- The objectivity and effectiveness of internal and external auditors; and
- The results of the external audit and any significant matters identified.

The key activities of the Audit Committee are summarised below:

Financial reporting and significant financial judgements

The Committee reviews the content of the interim and annual financial statements and advises the Board on whether, in the opinion of the Committee, taken as a whole, these are fair, balanced and understandable and provide the information necessary for the shareholder to assess the performance, business model and strategy.

During the period the Committee assessed the financial reporting processes, with assistance from management and the internal and external auditors. Management produce a comprehensive report providing details of judgements taken and other key reporting matters considered in preparing each set of results. The external auditors produce a similar report based on their audit findings. Due to the change in year-end, UKAR's reporting cycle included two sets of interim statements in addition to these accounts. During the 15 months the Committee considered the following significant issues / judgements in relation to the Group's financial statements and disclosures:

- **Loan Loss Provisioning** – despite significant improvements in the level of arrears and the economy, the provision remains highly material at £1.5bn and from necessity, is based on many judgemental assumptions. The Committee reviewed trends of default rates and losses to ensure that assumptions are reasonable. Focus was placed on the potentially higher risk areas of the loan books such as interest only, the equity release book and fraud provisions;
- **Provision for Customer Redress** – throughout the period the Committee have been kept informed of the approach to customer remediation, new developments and trends of PPI and other compensation claims. Based on this information, the Committee agreed that it was appropriate to further top-up PPI and other sundry redress provisions by £71m at the end of the period, bringing total provisions for the 15 month period to £116m;

Audit Committee Chairman's report (continued)

Audit Committee responsibilities and activity in 2013/14 (continued)

Financial reporting and significant financial judgements (continued)

- **Fair Value of Derivatives** – the number of derivatives held by UKAR has reduced significantly since formation as the inherited balance sheets are simplified. Methods continue to be reviewed against market best practice and the Audit Committee was satisfied that the bases adopted were appropriate;
- **Hedge Accounting** – over 97% of UKAR's total derivative books are in IAS39 hedge relationships at notional value. The Audit Committee reviewed the approach and were satisfied that it remains compliant with IFRS;
- **Going Concern** – following confirmation of HM Treasury's continued financial support for the Principal Subsidiaries and sight of the EU State Aid report, the Audit Committee determined that it continued to be appropriate to prepare the accounts on a going concern basis;
- **Contingent Liabilities** – the contingent liabilities note to the accounts was reviewed to ensure it reflected the latest position; and
- **Disclosures in the Annual Report and Accounts** – the Committee were comfortable that, taken as a whole, the Annual Report provided a fair, balanced and understandable reflection of UKAR's performance for the 15 month accounting period and the financial position as at 31 March 2014.

Internal audit

Deloitte LLP provide the internal audit services through an outsourced contract. Further details of the provision of the Internal Audit service can be found on page 53.

The Audit Committee fulfils its responsibility to monitor the objectiveness and effectiveness of internal audit through:

- Considering reports at each meeting from the Head of Internal Audit. These reports highlight existing and emerging matters of significance, areas of concern, planned actions, monitoring procedures and any other matters which are likely to impact on internal controls;
- Review and approval of the annual Internal Audit Plan, together with any changes required on a quarterly basis;
- Approval of the Terms of Reference for Internal Audit on an annual basis;
- Reviewing the adequacy and effectiveness of the activities carried out by the function; and
- The Head of Internal Audit attended all Audit Committee meetings during 2013/14 and has direct access to the Audit Committee and its Chairman.

The Audit Committee has satisfied itself that the Internal Audit function was effective and adequately resourced through the regular meetings held with, and reports provided by, the Head of Internal Audit.

Internal control

The Audit Committee reviews the effectiveness of the system of internal control annually in accordance with the UK Corporate Governance Code.

The Committee monitored progress in addressing the issues raised by Deloitte in their independent review of the underlying cause of the CCA issue.

The Committee reviewed reports on Whistleblowing and received assurance that the Policy is reinforced annually to all colleagues through mandatory training.

Further information on the approach to the Board's review of the Group's system of internal control is given within the Corporate Governance section at page 21.

External audit

The Committee places great importance on ensuring there are high standards of quality and effectiveness in the external audit process and is responsible for recommending the appointment, re-appointment and removal of the external auditors. It reviews the scope and results of the annual external audit and its cost effectiveness.

The external auditors may attend all meetings of the Committee and they have direct access to the Committee and its Chairman at all times.

The Audit Committee considered and approved the external audit plans and approach prior to the external auditors undertaking their audit work.

The external audit contract was last put out to tender in 2010 with PricewaterhouseCoopers LLP ('PwC') being appointed as external auditors from 28 April 2011 for a three year term, subsequently agreed to be extended up to 31 March 2014 due to the change in financial period. A full evaluation of PwC's performance was undertaken following the completion of all year-end work in 2013, which reported satisfaction with their performance since appointment, and was considered by the Audit Committee in October 2013. In January 2014, the Audit Committee agreed to extend PwC's contract for a further two years, until the year ended 31 March 2016.

Non audit services

The Audit Committee also develops and recommends to the Board a policy on the supply of non audit services by the internal or external auditors and reviews this annually, taking into account any relevant ethical guidance on the matter:

- The Policy clearly sets out the circumstances in which it is appropriate to employ any audit partner for additional work, the safeguards required and the mandate structure for approval;

Audit Committee Chairman's report (continued)

Audit Committee responsibilities and activity in 2013/14 (continued)

Non audit services (continued)

- The Finance & Investment Director must be aware of the hiring of auditors for non audit work;
- The Chairman of the Audit Committee must sign off work which will cost more than £25,000 and the auditors are asked to confirm that they are able to provide the services without compromising objectivity or independence;
- The auditors are required to demonstrate that accepting such a contract will not damage their independence or objectivity; and
- The Audit Committee reviews the audit and non audit fees paid to the internal and external auditors every six months and monitors the total spend with any auditors relative to the spend on audit work.

UKAR has used PwC and Deloitte for non audit related work but engagement is subject to the Non Audit Services Policy which aims to ensure that the objectivity and independence of both the external and outsourced internal auditors is not conflicted or compromised.

Priorities for 2014/15

For 2014/15, the key areas of focus for the Committee will be a continued oversight of the control environment, ensuring it continues to meet the needs of the business.

Kent Atkinson

Chairman, Audit Committee

Nomination Committee Chairman's report

Richard Pym, Chairman of the Nomination Committee, reports on how the Nomination Committee discharged its responsibilities during 2013/2014.

"The Nomination Committee continues to have an important role in ensuring the businesses have appropriate leadership and succession plans which reflect the unique nature of the business".

Chairman's overview of 2013/14

The work of the Committee during 2013/14 has covered a variety of topics within our terms of reference, including:

- Reorganisation of the Executive Team responsibilities following the resignation of Phillip McLelland, Finance Director, in November 2013;
- Ongoing review of Executive Development and Succession Planning;
- Review of the Constitution of the Board and its Committees; and
- Recommendation for reappointment of Directors at the AGM.

Nomination Committee membership

The Nomination Committee membership and attendance at meetings is set out on page 19. Louise Patten retired from the Board and consequently her role on the Nomination Committee on 31 December 2013.

Details of the skills and experience of Committee members can be found in the Directors' biographies on pages 16 to 18.

The Committee Chairman reported to the Board after each Committee meeting, summarising the key matters discussed, and the Board has also received the minutes of each meeting.

Nomination Committee responsibilities and activity in 2013/14

The responsibilities of the Committee include:

- reviewing the composition of the Board and preparing succession plans;
- identifying potential Executive and Non-Executive Directors;
- making recommendations to the Board concerning the appointment or re-appointment of Directors, having regard to the requirement for the Board to have the appropriate range of skills and experience; and
- reviewing the leadership needs of the business, the succession plans for key executive roles and approving the Board and Employee Diversity Policies.

The Nomination Committee fulfilled this remit through:

- reviewing the composition of the Board and its Committees and making recommendations to the Board which reflected the requirements of the business;
- recommending the renewal of Non Executive Director contracts to the Board where appropriate; and
- reviewing the leadership requirements of the organisation, including executive development and succession planning.

Diversity policy

The Board Diversity Policy endorses the principles of best practice and recognises the benefits of having a diverse board. The policy requires that in reviewing board composition, the Committee will consider the benefits of all aspects of diversity including skills, background, race, experience, gender and other qualities of directors. Due to the unique nature of the appointment process and the anticipated reduction in the size of the Board, a gender target is considered to be inappropriate.

Shareholder Directors

In accordance with the Framework Document UKFI is entitled to appoint one or more Non Executive Director and appointed Christopher Fox, UKFI's Head of Banking, as a Non Executive Director on 20 September 2013. In such circumstances the use of open advertising or an external search consultancy is inappropriate.

Priorities for 2014/15

In 2014/15 the Committee will continue to review Executive Development and succession planning to ensure that appropriate plans are in place and address any potential risks due to the nature of the business. The Committee will also make recommendations to the Board in relation to its composition and that of its Committees taking into account the strategic direction of the business.

Richard Pym

Chairman, Nomination Committee

Transaction Approvals Committee Chairman's report

Richard Pym, Chairman of the Transaction Approvals Committee, reports on how the Transaction Approvals Committee discharged its responsibilities during 2013/2014.

"The Transaction Approvals Committee has an important role in approving and overseeing the implementation of strategic transactions and ensuring they meet the overall objective of maximising the value for the taxpayer."

Chairman's overview of 2013/14

During 2013/14 the Transaction Approvals Committee has continued to oversee and approve the key stages of projects relating to the strategic transactions of B&B and NRAM.

Transaction Approvals Committee membership

The Transaction Approvals Committee membership and attendance at meetings is set out on page 19. Phillip McLelland resigned from the Board and consequently his role on the Transaction Approvals Committee on 25 November 2013. Christopher Fox joined the Transaction Approvals Committee with effect from 25 November 2013.

Details of the skills and experience of Committee members can be found in the Directors' biographies on pages 16 to 18.

The Committee Chairman reported to the Board after each Committee meeting, summarising the key matters discussed, and the Board has also received the minutes of each meeting.

Transaction Approvals Committee responsibilities and activity in 2013/14

The Committee is authorised to approve the implementation, including inter alia, terms, timing, pricing, documentation and appointment of advisors, of Strategic Transactions in accordance with any directions and limits set by the Board and with reference to the requirements of the Framework Document. The Committee meets as and when necessary depending on proposals for strategic transactions.

The Transaction Approvals Committee fulfilled this remit through updates on key strategic transactions and approval of the key stages of individual projects. This included approval of the sale of standalone unsecured loans from the NRAM book in July 2013.

Priorities for 2014/15

During 2014/15 the Transaction Approvals Committee will continue to oversee any strategic transactions and will work to ensure that the overarching objective of 'maximising the value to taxpayers' is achieved.

Richard Pym

Chairman, Transaction Approvals Committee

Risk Committee Chairman's report

John Tattersall, Chairman of the Risk Committee, reports on how the Risk Committee discharged its responsibilities during 2013/14.

"We continue to support the Board in ensuring that key risks are managed and monitored. In conjunction with the Audit Committee, we ensure that appropriate systems of internal control to mitigate those key risks are maintained. A key focus this period has been to ensure that conduct risk is embedded in everything we do and that will continue to be a priority."

Chairman's overview of 2013/14

The work of the Committee during 2013/14 has included the review of the principal risks each quarter, based on comprehensive reports from the Risk Director and Head of Compliance. The principal risks are:

- Conduct Risk;
- Operational Risk;
- Credit Risk;
- Strategic Risk;
- Liquidity Risk; and
- Market Risk.

In addition the Committee considered a variety of topics throughout the period, including:

- Overseeing the conduct risk approach;
- Monitoring the operational risk scenario testing;
- Considering the impact of emerging risks such as Scottish Independence and cyber risk;
- Maintaining an overview of the key compliance and regulatory issues;
- Monitoring progress on control improvements to address historical legacy issues; and
- Overseeing and monitoring the progress of the IT Transition Programme and organisation restructure.

Risk Committee membership

The Risk Committee membership and attendance at meetings is set out on page 19.

Details of the skills and experience of Committee members can be found in the Directors' biographies on pages 16 to 18.

Risk Committee meetings were attended by members of the Executive, including the CEO, Finance & Investment Director, Risk Director and Head of Compliance as well as representatives from other business functions from time to time. The Head of Internal Audit and the external auditors regularly attended the meetings.

The Committee Chairman reported to the Board after each Committee meeting, summarising the key matters discussed, and the Board has also received the minutes of each meeting.

Risk Committee responsibilities and activities in 2013/14

The main role of the Risk Committee is to advise the Board on the principal risks inherent in the business, risk governance and the effectiveness of the systems of control necessary to manage such risks and to present its findings to the Board. This responsibility requires the Risk Committee to:

- Keep under review the adequacy of the Group's risk management frameworks and systems of internal control, which include financial, operational and compliance risk management controls; and
- Foster a culture that emphasises and demonstrates the benefits of a risk-based approach to internal control and management of the Group.

The Risk Committee fulfilled this remit through:

- Oversight of the embedding of a supportive culture in relation to the management of risk;
- Making appropriate recommendations to the Board on all significant matters relating to the Group's risk appetite, strategy and policies;
- Monitoring the overall risk appetite within the Group and risk management performance, taking into account the current and prospective macroeconomic and financial environment, drawing on financial stability assessments such as those published by the Bank of England, FCA and other relevant authoritative sources;
- Assisting the Board in discharging its responsibilities for the setting of risk policies;
- Periodically reviewing the Group's material risk exposures in relation to risk appetite and capital adequacy;
- Ensuring public disclosure of information regarding the Group's risk management policies and key risk exposures is in accordance with statutory requirements and financial reporting standards;
- Considering reports from Compliance and Management on the system of internal control; and
- Overseeing UKAR's insurance programme and claims recoveries.

Further information on the role of the Risk Committee and its oversight of the risk management process is provided on page 53.

Risk Committee Chairman's report (continued)

Priorities for 2014/15

Against a backdrop of external economic challenges for UKAR customers and internal challenges associated with a business in run-off, a number of principal risks remain inherent, including strategic, conduct, operational and credit risk. These risks will continue to be monitored to ensure they remain within the Board approved risk appetite.

- **Conduct Risk** – ensuring appropriate customer outcomes and meeting regulatory expectations are at the heart of the business. We will continue to work hard to deal with customer complaints and review root cause analysis to improve our delivery of fair and appropriate customer outcomes. This will involve continuing to embed our cultural approach in front line operations and culturally within all our activities.
- **Operational Risk** – is particularly relevant since we are a reducing business and managing the people and process risks which this creates is a key priority. Our approach to risk means that regular monitoring and reporting of these risks will be visible at the relevant committees, ensuring that risk management supports the business in the next phase of the business strategy.

  Regulators and our business peers have expressed significant concern about the prevalence and impact of cyber security threats. The increasing importance of systems, the internet and telecommunications to complete business operations makes any threat to the security or availability of systems and information a risk to our success. During 2014/15 we will continue to monitor significant cyber security risks and assess the effectiveness of implemented controls to mitigate such risks.
- **Credit Risk** – given UKAR's customer profile, work continues to understand our customer's current financial position and in particular quantify the impact of interest rate rises. Our focus is on the various cohorts of customers who might be most impacted, for example, those in retirement, and ensuring that customers with interest only mortgage balances are able to repay their loans at the end of their term.
- **Strategic Risk** – the key strategic risks include those relating to the wider economic environment, the uncertain impact of a "yes" vote in favour of Scottish independence and the resolution of financial issues within the Eurozone. Other strategic risks include changing regulation, specifically the implementation and embedding of the new conduct risk regime.

UKAR principal risks are described in detail at pages 53 to 55.

John Tattersall

Chairman, Risk Committee

Key performance indicators – UKAR

In addition to the primary Financial Statements, we have adopted the following key performance indicators in managing business performance in the context of the Group's strategic priorities:

Strategic priorities	Financial measures	March 2014	Dec 2012	Commentary
Optimise the Balance Sheet	Total lending balances £bn Secured £bn Unsecured £bn	**61.2** **59.9** **1.3**	68.7 66.8 1.9	Lending balances reduced by 10.9% during the period due to £5.8bn of secured residential redemptions, £0.1bn of unsecured loan redemptions, £0.2bn of commercial loan redemptions and £1.0bn of other capital repayments. In addition, the £0.4bn NRAM standalone unsecured personal loan book was sold during the period.
	Residential mortgage redemption rate % Residential redemptions £bn	**7.1** **5.8**	6.3 4.6	Redemption rates have increased compared to 2012 reflecting increases in house prices and improved levels of remortgage activity across the market.
	Government loan repayments £bn Government loan balance £bn	**5.12** **38.3**	3.10 43.4	£2.0bn repaid against the B&B Working Capital Facility ('WCF') and £3.1bn on the NRAM government loan.
	Total cash payments to HM Treasury £bn	**6.22**	3.97	Total cash paid to HM Treasury during the period. This includes principal and interest repayments, guarantee fees and corporation tax paid. The main driver of the increase is the higher repayments of loan principal.
Minimise impairment and losses	Residential arrears balance: total residential mortgage balance % Residential payments overdue £m	**0.20** **121.2**	0.28 185.8	This represents the value of customers' missed payments as a proportion of the total balance of all residential mortgages and reflects that the level of debt owed on mortgages is falling at a quicker rate than the reduction in the book.
	Residential arrears 3 months and over and possessions as % of the book: – by value – by number of accounts Number of residential arrears 3 months and over and possessions cases	 **3.82** **2.93** **15,483**	 5.54 4.36 25,581	The reduction in arrears reflects both the improvement in collections performance and the continuing support provided to mortgage customers by low interest rates.
	Impairment provisions: Residential secured £m Cover % Unsecured £m Cover % Commercial/other £m Cover %	 **1,151.8** **1.90** **214.7** **14.35** **90.9** **12.73**	 1,411.1 2.09 403.8 17.56 100.0 11.34	The level of residential impairment Balance Sheet provision reduced by £259.3m. The provision reflects improved arrears performance and the benefit of improving house prices. Coverage has reduced on the unsecured book following the sale of the NRAM standalone personal unsecured loan book. Commercial coverage has increased as a result of updated property valuations.
Reduce costs	Total costs (excluding UKARcs) £m Ongoing costs (excluding UKARcs) £m* Ratio of costs to average interest-earning assets: – statutory % – ongoing %*	**244.5** **244.5** **0.26** **0.26**	267.0 207.3 0.32 0.25	The ongoing costs run rate, excluding UKARcs, has fallen reflecting the benefits of integrating the operations of the two businesses, the reducing customer base and the transfer of IT infrastructure to a new provider.
	12 months to March 2014 vs 12 months to March 2013	**March 2014**	March 2013	
	Total costs (excluding UKARcs) £m Ongoing costs (excluding UKARcs) £m* Ratio of costs to average interest-earning assets: – statutory % – ongoing %*	**188.0** **188.0** **0.25** **0.25**	267.2 207.5 0.33 0.25	

* Ongoing costs exclude certain items that are not expected to recur on an ongoing basis; an analysis of items excluded from ongoing costs is provided on page 44.

Financial review

Following the change of financial year-end to 31 March, these financial results are for the 15 month period to 31 March 2014. Therefore, to aid the comparison to prior year results (12 months to 31 December 2012) additional unaudited disclosures have been made in an appendix to this document. These outline the results for both the 12 months to 31 March 2014 and 12 months to 31 March 2013, plus the Balance Sheet position at 31 March 2013.

Performance

For the 15 month period to March 2014, underlying profit was £1,523.2m (12 months to December 2012: £1,096.9m). Underlying profit for the 12 months to March 2014 has increased by £185.5m to £1,259.1m (12 months to March 2013: £1,073.6m). The increase in profits was primarily due to a lower impairment charge, as the result of continued improvements in the level of arrears and increased HPI, and higher net operating income.

Underlying net operating income for the 15 month period was £1,846.9m (2012: £1,515.4m). For the 12 months to March 2014 underlying net operating income has increased by £40.5m to £1,486.3m (March 2013: £1,445.8m) due to lower funding costs, partly offset by lower income from the reducing Balance Sheet. Ongoing administrative expenses continue to fall. For the 12 months to March 2014 expenses were 9% lower than the previous year at £189.8m (March 2013: £207.5m). Administrative expenses for the 15 month period were £246.3m (2012: £207.3m). Impairment on loans to customers for the 15 months was £95.1m (2012: £241.4m) and £46.6m for the 12 months to March 2014, a reduction of £153.6m from March 2013 (£200.2m). Net impairment on investment securities was a £17.7m credit for the 15 months (2012: credit of £30.2m; March 2014: £9.2m; March 2013: £35.5m). The number of mortgage accounts 3 or more months in arrears including possessions reduced by 39% compared to December 2012.

The Board continue to believe it is appropriate to assess performance based on the underlying profits of the business, which excludes non-recurring costs, particularly those associated with the integration of B&B and NRAM and the remediation of inherited regulatory defects and certain gains such as the repurchase of our own liabilities at a discount. Also excluded are movements in fair value and hedge ineffectiveness relating to financial instruments which are expected to be held to maturity as opposed to being traded. The commentary on the results in this statement uses underlying profits and its components as the measure of performance. An analysis of the difference between the statutory profit and the underlying profit of UKAR is provided below.

Income Statement

For the 15 months ended 31 March / year ended 31 December	UKAR		B&B		NRAM	
	2014 £m	2012 £m	2014 £m	2012 £m	2014 £m	2012 £m
Net interest income	**1,830.6**	1,484.9	**511.9**	323.1	**1,318.7**	1,161.7
Underlying net non-interest income[1,2]	**16.3**	30.5	**30.2**	19.4	**(15.7)**	11.2
Underlying net operating income	**1,846.9**	1,515.4	**542.1**	342.5	**1,303.0**	1,172.9
Ongoing administrative expenses[1]	**(246.3)**	(207.3)	**(113.5)**	(93.4)	**(131.0)**	(113.9)
Impairment on loans to customers	**(95.1)**	(241.4)	**(78.8)**	(62.1)	**(16.3)**	(179.3)
Net impairment on investment securities[3]	**17.7**	30.2	**13.9**	51.1	**3.8**	(3.7)
Underlying profit before taxation	**1,523.2**	1,096.9	**363.7**	238.1	**1,159.5**	876.0
Unrealised fair value movements on financial instruments	**(29.6)**	(42.8)	**(26.7)**	(6.6)	**(2.9)**	(36.2)
Hedge ineffectiveness	**(27.6)**	(28.4)	**(6.3)**	(9.4)	**(21.3)**	(19.0)
Other net administrative expenses	**-**	(59.7)	**-**	(24.0)	**-**	(35.7)
Provision for customer redress	**(115.8)**	(419.0)	**(14.5)**	(12.0)	**(101.3)**	(407.0)
Gain on repurchase of own liabilities	**2.9**	143.5	**2.9**	27.6	**-**	115.9
Profit on sale of unsecured loans	**21.2**	-	**-**	-	**21.2**	-
Statutory profit before taxation	**1,374.3**	690.5	**319.1**	213.7	**1,055.2**	494.0

1. Underlying net non-interest income and ongoing administrative expenses include £1.8m in relation to UKARcs.
2. Underlying net non-interest income includes net fee and commission income, net gains on financial instruments designated at fair value, net realised gains less losses on investment securities and other operating income.
3. UKAR numbers include consolidation adjustments.

Financial review (continued)

Net interest income

For the 15 months ended 31 March / year ended 31 December	UKAR 2014 £m	UKAR 2012 £m	B&B 2014 £m	B&B 2012 £m	NRAM 2014 £m	NRAM 2012 £m
Interest receivable and similar income						
On secured loans	**2,714.9**	2,426.2	**1,005.4**	884.8	**1,709.5**	1,541.4
On other lending	**89.6**	111.2	**-**	-	**89.6**	111.2
On investment securities and deposits	**80.0**	86.6	**33.3**	31.5	**48.2**	56.9
Interest receivable and similar income	**2,884.5**	2,624.0	**1,038.7**	916.3	**1,847.3**	1,709.5
Interest expense and similar charges						
On amounts due to banks and HM Treasury	**(741.9)**	(676.2)	**(418.8)**	(426.1)	**(323.1)**	(250.1)
State guarantee fee**	**(46.9)**	(47.4)	**(46.9)**	(47.4)	**-**	-
On debt securities and other	**(265.1)**	(415.5)	**(61.1)**	(119.7)	**(205.5)**	(297.7)
Interest expense and similar charges	**(1,053.9)**	(1,139.1)	**(526.8)**	(593.2)	**(528.6)**	(547.8)
Net interest income	**1,830.6**	1,484.9	**511.9**	323.1	**1,318.7**	1,161.7
Average balances						
Interest-earning assets ('IEA')	**75,489**	84,117	**35,021**	36,968	**40,469**	47,280
Financed by:						
– Interest-bearing funding	**50,805**	59,769	**13,619**	15,643	**37,186**	44,262
– Interest-free funding*	**24,684**	24,348	**21,402**	21,325	**3,283**	3,018
Average rates %	**%**	%	**%**	%	**%**	%
Gross yield on IEA	**3.07**	3.12	**2.38**	2.48	**3.66**	3.62
Cost of interest-bearing funding	**(1.66)**	(1.83)	**(2.83)**	(3.49)	**(1.14)**	(1.24)
Interest spread	**1.41**	1.29	**(0.45)**	(1.01)	**2.52**	2.38
State guarantee fee**	**(0.05)**	(0.06)	**(0.11)**	(0.13)	**-**	-
Contribution of interest-free funding*	**0.59**	0.54	**1.73**	2.01	**0.09**	0.08
Net interest margin on average IEA	**1.95**	1.77	**1.17**	0.87	**2.61**	2.46
Annual average Bank Base Rate	**0.50**	0.50	**0.50**	0.50	**0.50**	0.50
Annual average 1-month LIBOR	**0.49**	0.62	**0.49**	0.62	**0.49**	0.62
Annual average 3-month LIBOR	**0.51**	0.83	**0.51**	0.83	**0.51**	0.83

* Interest-free funding is calculated as an average over the financial period, and includes the Statutory Debt and share capital and reserves.

** At the time of the nationalisation of B&B, HM Treasury provided a guarantee with regard to certain wholesale borrowings and derivative transactions existing at that time. The amount of this fee is dependent on balances outstanding and hence it is included within 'interest expense and similar charges.'

Net interest income for the 15 month period to March 2014 was £1,830.6m (2012: £1,484.9m) and £1,469.2m for the 12 months to March 2014 (March 2013: £1,441.0m). Across both books there was a reduction in income due to the decrease in average interest-earning assets over the 15 months of £8.6bn to £75.5bn (NRAM: £6.8bn, B&B: £1.9bn). In addition, 2012 only had eight months' impact of the NRAM government loan rate increase (increased by 0.75% in May 2012) which in isolation has a year on year impact of approximately £50m. However, both these impacts were offset by the improving funding mix on the B&B Balance Sheet as the Working Capital Facility ('WCF') was repaid.

Underlying net interest margin for the 15 months to March 2014 has increased to 1.95% at UKAR level from 1.77% in 2012.

On the B&B book the underlying net interest margin increased 0.30% to 1.17%, primarily due to reducing funding costs as the relatively expensive WCF is repaid. The WCF interest rate of Bank Base Rate + 500bps is in excess of the average yield on interest earning assets of 2.38%.

In NRAM, net interest margin increased to 2.61% from 2.46%, mainly due to reducing funding costs, partially offset by the higher cost of the government loan on which the interest rate payable was increased from Bank Base Rate + 25bps to Bank Base Rate + 100bps with effect from 4 May 2012.

Financial review (continued)

Underlying net non-interest income

Underlying net non-interest income was £16.3m in the 15 months (2012: £30.5m) and £17.1m in the 12 months to March 2014 (March 2013: £4.8m). Net fee and commission income was £17.9m in the 15 months (2012: £17.0m). Net fee and commission income was £0.9m higher in the 12 months to March 2014 at £14.8m than in the 12 months to March 2013 (£13.9m) due to higher redemption fee income.

Included in the first quarter of 2012 were one-off fair value gains on asset disposals of £17.5m, relating to a legacy NRAM asset previously held at nil value.

Net realised gains less losses on investment securities was a £12.5m loss in the 15 months to March 2014 due to the disposal or early maturity of a number of investment securities in both B&B and NRAM, as financial markets have returned to levels that enable legacy assets to be sold without diminishing taxpayer value.

Other operating income of £10.9m in the 15 months (2012: £10.9m) and £10.6m in the 12 months to March 2014 is roughly in line with the equivalent period to March 2013. However, 2013/14 includes profits from the sale and leaseback of the Doxford (Sunderland) properties (£7.3m) and income from managing the government's Help to Buy: mortgage guarantee scheme (£1.8m) and 2012/13 included property sales (£5.8m) and income for the use of systems and facilities by Northern Rock plc (£3.4m).

Net non-interest income

	UKAR		B&B		NRAM		UKARcs	
For the 15 months ended 31 March / year ended 31 December	**2014 £m**	2012 £m	**2014 £m**	2012 £m	**2014 £m**	2012 £m	**2014 £m**	2012 £m
Total net fee and commission income	**17.9**	17.0	**17.8**	14.4	**0.1**	2.7	**-**	-
Net gains on financial instruments designated at fair value	**-**	17.5	**-**	-	**-**	17.5	**-**	-
Net realised gains less losses on investment securities	**(12.5)**	(14.9)	**11.6**	1.4	**(24.1)**	(16.3)	**-**	-
Other operating income	**10.9**	10.9	**0.8**	3.6	**8.3**	7.3	**1.8**	-
Underlying net non-interest income	**16.3**	30.5	**30.2**	19.4	**(15.7)**	11.2	**1.8**	-
Unrealised fair value movements on financial instruments	**(29.6)**	(42.8)	**(26.7)**	(6.6)	**(2.9)**	(36.2)	**-**	-
Hedge ineffectiveness	**(27.6)**	(28.4)	**(6.3)**	(9.4)	**(21.3)**	(19.0)	**-**	-
Provision for customer redress	**(115.8)**	(419.0)	**(14.5)**	(12.0)	**(101.3)**	(407.0)	**-**	-
Statutory net non-interest income	**(156.7)**	(459.7)	**(17.3)**	(8.6)	**(141.2)**	(451.0)	**1.8**	-

Accounting volatility on derivative financial instruments

NRAM and B&B use derivative financial instruments for economic hedging purposes. Most of these are designated and accounted for as IAS 39 'Financial Instruments: Recognition and Measurement' compliant fair value or cash flow hedge relationships. Where effective hedge relationships can be established, the movement in the fair value of the derivative is offset in full or in part either by opposite movements in the fair value of the instrument being hedged or by being taken to reserves. Any ineffectiveness arising from different movements in fair value will offset over time.

Unrealised fair value movements were a net loss of £29.6m in the 15 month period (2012: loss of £42.8m) and £33.3m in the 12 months to March 2014 (March 2013: gain of £4.7m). These losses generally relate to derivatives that act as an economic hedge but were not treated as an accounting hedge under IAS 39.

Provision for customer redress

UKAR defines conduct risk as the risk of UKAR treating its customers unfairly and delivering inappropriate outcomes leading to customer detriment or impacting market integrity. Since the creation of UKAR we have been remediating a series of conduct issues inherited from the legacy businesses, including the mis-selling of Payment Protection Insurance ('PPI') by Northern Rock and the issue of non-compliant CCA loan documentation to certain customers.

During 2013/14 the overall level of PPI claims has reduced but the level of claims associated with the NRAM Unsecured loan book is higher than previously anticipated. As a result of this and some other areas where remediation is anticipated the PPI provisions has been increased by £29.0m.

In 2012 £271m was provided for remediating non-compliant CCA loans and 133,000 customers have now been contacted and their accounts corrected. At June 2013 we provided a further £47.0m primarily on a portfolio of accounts previously sold to a third party by Northern Rock plc prior to nationalisation, which were subject to the same problem. A separate charge of £17.9m has been made at the period end that mainly relates to additional redress required as a result of ongoing remediation exercises impacting CCA regulated loans.

In addition we have provided a further £21.9m in respect of provisions for other remediation activities during the period. This includes £15.0m for customers who have incorrectly been maintained on interest only products beyond their expectations, having originally switched from capital repayment plans for a temporary period.

Financial review (continued)

Ongoing administrative expenses

Costs for the 15 months include £1.8m for UKARcs relating to the provision of administrative support to the government's mortgage guarantee scheme. These costs were fully reimbursed by HM Treasury.

The Group has continued to focus on maximising cost effectiveness and efficiency through continuous improvement. We have completed the integration of the operations of the two businesses and the transfer of our IT infrastructure to HCL Technologies Limited ('HCL'), both contributing to reduced costs and increased operational flexibility. Ongoing administrative expenses for the 15 months were £246.3m (2012: £207.3m) and £189.8m for the 12 months to March 2014 (March 2013: £207.5m), which, when excluding the £1.8m UKARcs costs, is 9% lower. Costs are expected to fall further in the coming year due to a full year of IT costs at the lower run rate and other cost reductions as the size of the balance sheet reduces. The increase in depreciation in 2013/14 reflects the capital investment in integrating the two businesses.

Administrative expenses

	UKAR		B&B		NRAM		UKARcs	
For the 15 months ended 31 March / year ended 31 December	2014 £m	2012 £m	2014 £m	2012 £m	2014 £m	2012 £m	2014 £m	2012 £m
Wages and salaries	**71.3**	65.0	**30.5**	28.0	**40.4**	37.0	**0.5**	-
Social security costs	**7.4**	6.6	**3.2**	3.0	**4.2**	3.6	**-**	-
Defined benefit pension costs	**(0.8)**	0.6	**2.4**	0.9	**(3.2)**	(0.3)	**-**	-
Defined contribution pension costs	**4.2**	3.4	**1.6**	1.4	**2.6**	2.0	**-**	-
Other retirement benefit costs	**0.6**	0.5	**0.6**	0.5	**-**	-	**-**	-
Total staff costs	**82.7**	76.1	**38.3**	33.8	**44.0**	42.3	**0.5**	-
IT costs	**63.0**	56.0	**25.0**	25.9	**38.0**	30.1	**-**	-
Outsourced and professional services	**30.4**	25.5	**17.6**	13.4	**12.5**	12.1	**0.3**	-
Depreciation and amortisation	**19.4**	12.6	**8.0**	4.7	**11.2**	7.9	**0.2**	-
Other administrative expenses	**50.8**	37.1	**24.6**	15.6	**25.3**	21.5	**0.8**	-
Ongoing administrative expenses	**246.3**	207.3	**113.5**	93.4	**131.0**	113.9	**1.8**	-
Other net administrative expenses:								
– Transformation costs	**-**	51.4	**-**	24.0	**-**	27.4	**-**	-
– Accelerated depreciation	**-**	8.3	**-**	-	**-**	8.3	**-**	-
Total other net administrative expenses	**-**	59.7	**-**	24.0	**-**	35.7	**-**	-
Total administrative expenses	**246.3**	267.0	**113.5**	117.4	**131.0**	149.6	**1.8**	-

Other net administrative expenses

No 'other net administrative expenses' have been incurred in 2013/14. The £59.7m incurred in 2012 mainly related to investment in UKAR's IT platform through the transfer to the HCL and costs associated with the phased exit of the Gosforth site.

Financial review (continued)

Arrears and loan impairment: residential and unsecured loans

Total UKAR loan impairment provisions as at 31 March 2014 were £1,457.4m (2012: £1,914.9m) comprising residential mortgages £1,151.8m (2012: £1,411.1m), unsecured loans £214.7m (2012: £403.8m) and commercial property of £90.9m (2012: £100.0m).

Arrears and possessions

		UKAR			
At 31 March / 31 December		2014		2012	
		Residential	Unsecured	Residential	Unsecured
Arrears 3 months and over					
Number of cases	No.	**14,139**	**10,445**	23,376	31,140
Proportion of total accounts	%	**2.68**	**8.76**	3.99	13.67
Asset value	£m	**2,067.5**	**172.7**	3,341.1	410.1
Proportion of book	%	**3.48**	**13.47**	5.06	21.64
Total value of payments overdue	£m	**84.3**	**23.0**	132.3	96.9
Proportion of total book	%	**0.14**	**1.80**	0.20	5.11
Possessions					
Number of cases	No.	**1,344**	**-**	2,205	-
Proportion of total accounts	%	**0.25**	**-**	0.37	-
Asset value	£m	**199.0**	**-**	320.5	-
Proportion of book	%	**0.34**	**-**	0.48	-
Total value of payments overdue	£m	**14.0**	**-**	20.8	-
Proportion of total book	%	**0.02**	**-**	0.03	-
New possessions*	No.	**6,996**	**-**	7,326	-
Total arrears 3 months and over and possessions					
Number of cases	No.	**15,483**	**10,445**	25,581	31,140
Proportion of total accounts	%	**2.93**	**8.76**	4.36	13.67
Asset value	£m	**2,266.5**	**172.7**	3,661.6	410.1
Proportion of book	%	**3.82**	**13.47**	5.54	21.64
Total value of payments overdue	£m	**98.3**	**23.0**	153.1	96.9
Proportion of total book	%	**0.16**	**1.80**	0.23	5.11
Payments overdue					
Total value of payments overdue	£m	**121.2**	**23.8**	185.8	99.0
Proportion of total book	%	**0.20**	**1.86**	0.28	5.22
Loan impairment provision					
As % of total balances	%	**1.90**	**14.35**	2.09	17.56

* New possessions for the 15 months to 31 March 2014 and the 12 months to 31 December 2014.

Financial review (continued)

Arrears and possessions

At 31 March / 31 December		B&B 2014 Residential	B&B 2012 Residential	NRAM 2014 Residential	NRAM 2014 Unsecured	NRAM 2012 Residential	NRAM 2012 Unsecured
Arrears 3 months and over							
Number of cases	No.	**3,739**	5,197	**10,400**	**10,445**	18,179	31,140
Proportion of total accounts	%	**1.43**	1.85	**3.87**	**8.76**	5.95	13.67
Asset value	£m	**528.7**	760.7	**1,538.8**	**172.7**	2,580.3	410.1
Proportion of book	%	**1.78**	2.38	**5.20**	**13.47**	7.56	21.64
Total value of payments overdue	£m	**15.3**	23.1	**69.0**	**23.0**	109.2	96.9
Proportion of total book	%	**0.05**	0.07	**0.23**	**1.80**	0.32	5.11
Possessions							
Number of cases	No.	**435**	717	**909**	**-**	1,488	-
Proportion of total accounts	%	**0.17**	0.25	**0.34**	**-**	0.49	-
Asset value	£m	**63.8**	108.2	**135.2**	**-**	212.3	-
Proportion of book	%	**0.21**	0.34	**0.46**	**-**	0.62	-
Total value of payments overdue	£m	**3.2**	4.7	**10.8**	**-**	16.1	-
Proportion of total book	%	**0.01**	0.02	**0.04**	**-**	0.05	-
New possessions	No.	**1,987**	1,760	**5,009**	**-**	5,566	-
Total arrears 3 months and over and possessions							
Number of cases	No.	**4,174**	5,914	**11,309**	**10,445**	19,667	31,140
Proportion of total accounts	%	**1.60**	2.10	**4.21**	**8.76**	6.44	13.67
Asset value	£m	**592.5**	868.9	**1,674.0**	**172.7**	2,792.6	410.1
Proportion of book	%	**1.99**	2.72	**5.66**	**13.47**	8.18	21.64
Total value of payments overdue	£m	**18.5**	27.8	**79.8**	**23.0**	125.3	96.9
Proportion of total book	%	**0.06**	0.09	**0.27**	**1.80**	0.37	5.11
Payments overdue							
Total value of payments overdue	£m	**23.7**	34.6	**97.5**	**23.8**	151.1	99.0
Proportion of total book	%	**0.08**	0.11	**0.33**	**1.86**	0.44	5.22
Loan impairment provision							
As % of total balances	%	**1.99**	1.96	**1.82**	**16.75**	2.22	17.56

Arrears and loan impairment: residential loans

Strong arrears performance continues. UKAR has seen arrears in both companies fall notwithstanding the challenging economic conditions. At UKAR level, the number of mortgage accounts 3 or more months in arrears, including those in possession, has reduced by 39% since 31 December 2012.

UKAR adheres to the FCA's regulatory guidance regarding Treating Customers Fairly and continues to work closely with customers experiencing, or likely to experience, financial difficulty in maintaining their mortgage payments. UKAR offers a range of measures to support these customers depending upon their individual circumstances and ability to pay with the long term aim of sustaining their mortgage commitments and remaining in their homes. Possession continues to be a last resort.

The total number of cases 3 or more months in arrears, including those in possession, reduced by 39% from 25,581 at 31 December 2012 to 15,483 at 31 March 2014. The total value of debt owed by residential customers has reduced from £185.8m at 31 December 2012 to £121.2m at 31 March 2014 equivalent to 0.20% of mortgage balances (2012: 0.28%).

Provisions for residential loan impairment held on the Balance Sheet have reduced by £259.3m since 31 December 2012 to £1,151.8m (2012: £1,411.1m) reflecting the reduction in arrears cases and the benefit of improving house prices.

Financial review (continued)

Arrears and loan impairment: residential loans (continued)

Total UKAR fraud and professional negligence provisions have decreased by £50.3m since 31 December 2012 to £321.3m (2012: £371.6m) as a result of write-offs following the sale of properties and the impact of reducing the level of provisions across a number of portfolios as valuations benefit from improving house prices. Total UKAR fraud provisions represent coverage of 45% of suspected fraud and professional negligence cases (2012: 46%). Within the B&B book, fraud and professional negligence provisions have reduced since 31 December 2012 by £51.3m to £265.0m (2012: £316.3m). In the NRAM book, fraud and professional negligence provisions have remained flat at £56.3m (2012: £55.3m).

As a proportion of balances, the residential impairment provision was 1.90% (2012: 2.09%). The residential loan impairment charge was £52.8m for the 15 month period (2012: £187.0m) and £18.6m for the 12 months to March 2014 (March 2013: £165.9m). The reduction in the charge results from lower arrears volumes and the benefit of improving house prices.

The number of properties in possession for UKAR decreased from 2,205 at the end of 2012 to 1,344 at 31 March 2014. Within B&B, possession stock decreased from 717 cases at 31 December 2012 to 435 at 31 March 2014. In NRAM possession stock reduced to 909 cases from 1,488 at 31 December 2012. The rate at which properties have been taken into possession continues to slow. In total 6,996 properties were taken in possession in the 15 month period, an average of 466 per month (2012: 7,326, 611 per month).

In addition to residential property possessions, there are also a number of buy-to-let properties within B&B managed by Law of Property Act ('LPA') receivers. The LPA 'for sale' stock increased from 306 cases at 31 December 2012 to 369 at 31 March 2014.

During the 15 months, 7,857 cases, an average of 524 per month (2012: 7,826, 652 per month) were sold following possession and a further 367 cases (2012: 1,237) were sold which were under LPA management. Realised losses on properties sold following possession or sold by an LPA were £374.1m (2012: £458.8m), all of which had previously been fully provided for. Within these losses £53.2m were fraudulent and professional negligence cases (2012: £55.8m).

Arrears and loan impairment: unsecured loans

The standalone NRAM unsecured personal loan book was sold in July 2013 and hence is excluded from the arrears figures above. Comparative figures for December 2012 include these loans.

The number of unsecured loans 3 months or more in arrears was 10,445 cases (2012: 31,140). The charge for unsecured loan impairment for the 15 months was £36.4m (2012: £42.3m). The charge for the 12 months to March 2014 was £21.2m, £5.4m lower than March 2013 (£26.6m). Asset coverage was 14.3% at 31 March 2014 (2012: 17.6%).

The provision for unsecured loans was £214.7m (2012: £403.8m). Realised losses in the 15 months were £82.2m (2012: £155.4m) all of which had previously been fully provided for.

Arrears and loan impairment: commercial loan book

The provision for the commercial book has decreased to £90.9m from £100.0m at 31 December 2012, with coverage at 12.7% (2012: 11.3%). We continually review the level of provisions against each individual loan based on current and future property valuations, future rental income projections, tenant quality and general market conditions.

Net impairment release on investment securities

UKAR continues to review securities held on the Balance Sheet and believes the risk of further impairment is not significant. During the financial period we have identified a number of assets in both B&B and NRAM where events have occurred that caused us to reverse impairments previously charged. These have resulted in a net credit to impairment in the 15 months of £17.7m (2012: £30.2m net credit) and £9.2m in the 12 months to March 2014 (March 2013: £35.5m).

Gain on repurchase of own liabilities

In the 15 months to March 2014 we repurchased £5.3m of our subordinated debt yielding gains of £2.9m. In 2012 we reported gains of £143.5m following the repurchase of some of our securitised notes.

Taxation

The total charge for tax per the Income Statement for the 15 months ended 31 March 2014 was £308.3m (2012: £126.7m). Given the statutory profit before taxation of £1,374.3m (2012: £690.5m) this equates to an effective tax rate of 22.4% (2012: 18.3%).

Financial review (continued)

Balance Sheet

Balance Sheet summary

At 31 March / 31 December	UKAR 2014 £m	UKAR 2012 £m	B&B 2014 £m	B&B 2012 £m	NRAM 2014 £m	NRAM 2012 £m
Loans to customers:						
– residential mortgages	**59,344.6**	66,056.3	**29,758.0**	31,911.3	**29,586.6**	34,145.0
– commercial and other secured loans	**623.0**	781.9	**454.8**	556.5	**168.2**	225.4
– unsecured lending	**1,281.9**	1,895.4	**-**	-	**1,281.9**	1,895.4
Wholesale assets	**8,598.2**	11,778.9	**3,051.5**	3,717.2	**5,663.3**	8,192.8
Fair value adjustments on portfolio hedging	**308.8**	493.8	**223.0**	341.4	**85.8**	152.5
Derivative financial instruments	**4,616.2**	5,720.2	**1,569.6**	1,800.3	**3,046.6**	3,919.8
Other assets	**167.3**	159.7	**97.7**	134.9	**89.2**	79.2
Total assets	**74,940.0**	86,886.2	**35,154.6**	38,461.6	**39,921.6**	48,610.1
Statutory Debt and HM Treasury loans	**38,350.5**	43,487.3	**23,415.3**	25,424.2	**14,935.2**	18,063.1
Wholesale funding	**29,005.2**	36,415.0	**8,212.9**	9,559.1	**20,912.5**	26,991.3
Derivative financial instruments	**446.0**	783.7	**331.9**	502.2	**114.1**	281.5
Other liabilities	**582.0**	575.9	**220.4**	265.4	**378.3**	363.9
Other capital instruments	**215.3**	359.2	**159.1**	146.2	**56.2**	213.0
Equity	**6,341.0**	5,265.1	**2,815.0**	2,564.5	**3,525.3**	2,697.3
Total equity and liabilities	**74,940.0**	86,886.2	**35,154.6**	38,461.6	**39,921.6**	48,610.1

The Balance Sheet has decreased by £12.0bn to £74.9bn from £86.9bn since December 2012.

Lending balances have reduced by £7.5bn (10.9%) to £61.2bn during the 15 month period to March 2014 due to £5.8bn of secured residential redemptions, £0.1bn of unsecured loan redemptions, £0.2bn of commercial loan redemptions and £1.0bn of other capital repayments. In addition, the £0.4bn NRAM standalone unsecured personal loan book was sold during the period.

Liabilities

Statutory Debt and HM Treasury loans (excluding accrued interest) have reduced by £5.1bn to £38.3bn (2012: £43.5bn) due to repayments of principal in the period (NRAM: £3.1bn, B&B: £2.0bn). UKAR did not draw down any facility during the period. In addition, £7.4bn of other external wholesale funding was repaid in the period.

Cash repayments

At the end of 2012, UKAR had £27.8bn of funding from HM Treasury, plus a further £15.7bn owed to the Financial Services Compensation Scheme ('FSCS'). Repayment of this debt remains a primary objective of UKAR. In the 15 months a further £5.1bn (2012: £3.1bn) of HM Treasury debt was repaid. In addition, £1.1bn of other cash flows were generated for HM Treasury in the form of State guarantee fees, interest and taxes. The Board considers the total of all these cash flows paid to HM Treasury to be an important measure. Total cash payments in 2013/14 to HM Treasury were £6.2bn (2012: £4.0bn).

Of the £5.1bn loan repayments made during the period, £790m was generated from the disposal of Treasury assets and the sale of NRAM unsecured personal loan book (NRAM: £749m; B&B: £41m).

Financial review (continued)

Capital

UKAR operates under a MIPRU regulatory status. Strictly the regulated companies within the Group are required to hold capital in excess of 1% of total Balance Sheet assets plus any undrawn commitments. However, the Board believes it should hold capital above 1% reflecting the increased risk in the business compared to a standard MIPRU firm. As at 31 March 2014 capital in B&B plc represented 6.6% of B&B Company assets and NRAM plc capital represented 8.8% of NRAM Company assets.

The Group's capital is provided by its shareholders (currently HM Treasury) and the holders of subordinated notes and subordinated liabilities.

The regulated Group companies met their capital requirements in full throughout the period and have received no additional capital from HM Treasury.

Capital resources – B&B plc

At 31 March / 31 December	2014 £m	2012 £m
Share capital and reserves	**2,740.2**	2,382.6
Available-for-sale reserve adjustments	**(25.8)**	(17.1)
Cash flow hedge reserve adjustments	**(56.9)**	(86.8)
Net pension deficit adjustment	**-**	(103.3)
Less: deductions	**(515.1)**	(521.3)
Tier 1 capital	**2,142.4**	1,654.1
Capital instruments	**81.8**	83.6
Total capital	**2,224.2**	1,737.7

Capital resources – NRAM plc

At 31 March / 31 December	2014 £m	2012 £m
Share capital and reserves	**3,337.2**	2,461.3
Available-for-sale reserve adjustments	**29.9**	73.7
Cash flow hedge reserve adjustments	**(156.8)**	(192.2)
Pension scheme asset	**(65.3)**	(43.0)
Reserve capital instruments	**101.4**	101.4
Tier one notes	**40.9**	41.9
Withheld coupons	**71.8**	53.8
Less: deductions	**(1.0)**	(1.1)
Tier 1 capital	**3,358.1**	2,495.8
Subordinated notes	**23.4**	23.4
Subordinated liabilities	**-**	150.7
Total capital	**3,381.5**	2,669.9

B&B plc total capital resources of £2,224.2m are £486.5m higher than 2012, due to profits generated in the 15 month period and reduced pension adjustments. In 2012, B&B's Tier 1 capital was adjusted to reflect future payments which B&B had committed to make to address the deficit on the defined benefit pension scheme (31 December 2012: £103.3m). At 31 March 2014, as permitted by the FCA's capital rules, B&B has elected to make no such adjustment but to leave the pension deficit as per the statutory accounts.

NRAM plc total capital resources of £3,381.5m are £711.6m higher than 2012, due to profits generated in the 15 month period offset by the maturity of the £150.7m subordinated loan provided by HM Treasury.

Since 2009, NRAM has been withholding coupons on all its subordinated instruments where it is legally permitted to do so. Where such instruments are categorised as equity rather than as debt, (ie reserve capital instruments and subordinated notes), they are shown as non-shareholders' funds. Under accounting standards, as these form part of equity, it is not permitted to accrue for these withheld coupons. Previous Annual Reports and Interims Reports have not quantified the amount of withheld coupons, however, the non-shareholders' funds are now presented inclusive of the withheld coupons. There is no impact on total equity, merely a reclassification between the components of equity.

Key performance indicators – B&B

In addition to the primary Financial Statements, we have adopted the following key performance indicators in managing business performance in the context of its strategic priorities.

Strategic priorities	Financial measures	2014	2012	Commentary
Optimise the Balance Sheet	Lending balances secured £bn	**30.2**	32.5	Lending balances reduced by 6.9% during the period due to £1.9bn of residential redemptions and £0.4bn of other capital repayments.
	Residential mortgage redemption rate % Residential redemptions £bn	**4.7** **1.9**	4.0 1.3	Redemptions have increased compared to 2012 reflecting increases in house prices and improved levels of remortgage activity across the market.
	Government loan repayments £bn Government loan balance £bn	**2.00** **23.4**	1.43 25.4	No drawdowns were made in the period from the WCF arranged with HM Treasury. The balance of £5.0bn, excluding accrued interest, is within the £11.5bn maximum facility level currently agreed with HM Treasury. Repayments of £2.0bn were made in the period against the WCF. No payments were made against the Statutory Debt and the balance remains at £18.4bn at 31 March 2014.
	Total cash payments to HM Treasury £bn	**2.50**	1.93	Total cash paid to HM Treasury during the period. This includes principal and interest repayments, State guarantee fees and corporation tax paid. The main driver of the increase is the higher principal repayment.
Minimise impairment and losses	Residential arrears balance: total residential mortgage balance % Residential payments overdue £m	**0.08** **23.7**	0.11 34.6	This represents the value of customers' missed payments as a proportion of the total balance of all residential mortgages and the reduction to 0.08% reflects that the level of overdue debt owed on mortgages is falling faster than the book.
	Residential arrears 3 months and over and possessions as % of the book: – by value – by number of accounts Number of residential arrears 3 months and over and possessions cases	 **1.99** **1.60** **4,174**	 2.72 2.10 5,914	The reduction in arrears reflects both the improvement in collections performance and the continuing support provided to mortgage customers by low interest rates.
	Impairment provisions: Residential £m Cover % Commercial £m Cover %	 **602.8** **1.99** **63.0** **12.17**	 637.6 1.96 50.3 8.29	The level of the residential impairment Balance Sheet provision reduced by £34.8m and the level of cover stayed broadly flat at 1.99%. The level of the commercial impairment provision increased by £12.7m and the level of cover increased by 3.88% mainly due to revised valuations.
Reduce costs	Total costs £m Ongoing costs £m* Ratio of costs to average interest-earning assets: – statutory % – ongoing %*	**113.5** **113.5** **0.26** **0.26**	117.4 93.4 0.32 0.25	The ongoing costs run rate has fallen reflecting the benefits of integration of the operations of the two businesses, the reducing customer base and the transfer of IT infrastructure to a new provider.
	12 months to March 2014 vs 12 months to March 2013	**March 2014**	March 2013	
	Total costs (excluding UKARcs) £m Ongoing costs (excluding UKARcs) £m* Ratio of costs to average interest-earning assets: – statutory % – ongoing %*	**86.2** **86.2** **0.25** **0.25**	119.8 95.8 0.33 0.26	

* Ongoing costs exclude certain items that are not expected to recur on an ongoing basis; an analysis of items excluded from ongoing costs is provided on page 44.

Key performance indicators – NRAM

In addition to the primary Financial Statements, we have adopted the following key performance indicators in managing business performance in the context of its strategic priorities.

Strategic priorities	Financial measures	2014	2012	Commentary
Optimise the Balance Sheet	Total lending balances £bn Secured £bn Unsecured £bn	**31.0** **29.8** **1.3**	36.3 34.4 1.9	Lending balances reduced by 14.4% during the period due to £4.0bn of residential redemptions, £0.1bn of unsecured loan redemptions and £0.8bn of other capital repayments. In addition, the £0.4bn NRAM standalone unsecured personal loan book was sold during the period.
	Residential mortgage redemption rate % Residential redemptions £bn	**9.3** **4.0**	8.4 3.2	Redemption rates have increased compared to 2012 reflecting increases in house prices and improved levels of remortgage activity across the market.
	Government loan repayments £bn Government loan balance £bn	**3.1** **14.9**	1.7 18.0	During the period, £3.1bn was repaid against the NRAM government loan.
	Total cash payments to HM Treasury £bn	**3.73**	2.05	Total cash paid to HM Treasury during the period. This includes principal and interest repayments, State guarantee fees and corporation tax paid. The main drivers of the increase is higher principal repayments on the government loan and maturity of the HM Treasury subordinated loan.
Minimise impairment and losses	Residential arrears balance : total residential mortgage balance % Residential payments overdue £m	**0.33** **97.5**	0.44 151.1	This represents the value of customers' missed payments as a proportion of the total balance of all residential mortgages and the reduction to 0.33% reflects that the level of overdue debt owed on mortgages is falling faster than the book.
	Residential arrears 3 months and over and possessions as % of the book: – by value – by number of accounts Number of residential arrears 3 months and over and possessions cases	 **5.66** **4.21** **11,309**	 8.18 6.44 19,667	The reduction in arrears reflects both the improvement in collections performance and the continuing support provided to mortgage customers by low interest rates.
	Impairment provisions: Residential secured £m Cover % Unsecured £m Cover % Commercial £m Cover %	 **549.0** **1.82** **214.7** **14.35** **27.9** **14.23**	 773.5 2.22 403.8 17.56 49.7 18.07	The level of the residential impairment Balance Sheet provision reduced by £224.5m and the level of cover decreased from 2.22% to 1.82% due to the improved arrears performance and improving house prices.
Reduce costs	Total costs £m Ongoing costs £m* Ratio of costs to average interest-earning assets: – statutory % – ongoing %*	**131.0** **131.0** **0.26** **0.26**	149.6 113.9 0.32 0.24	The ongoing costs run rate has fallen reflecting the benefits of integration of the operations of the two businesses, the reducing customer base and the transfer of IT infrastructure to a new provider.
	12 months to March 2014 vs 12 months to March 2013 Total costs (excluding UKARcs) £m Ongoing costs (excluding UKARcs) £m* Ratio of costs to average interest-earning assets: – statutory % – ongoing %*	**March 2014** **101.8** **101.8** **0.26** **0.26**	March 2013 147.4 111.7 0.32 0.24	

* Ongoing costs exclude certain items that are not expected to recur on an ongoing basis; an analysis of items excluded from ongoing costs is provided on page 44.

Risk management and control

Pages 52 to 55 form an integral part of the audited Financial Statements

Introduction

In accordance with the requirements of the Framework Document which is referred to on page 16, the Group's approach to risk management is built on formal governance processes and relies on individual responsibility and collective oversight, informed by comprehensive reporting.

The following sections describe the Group's approach to risk management, including the risk governance structure and principal risk categories under management. Other than the risks described here, there are other factors which could also affect the Group's results, including economic factors. Therefore, the categories of risk described below should not be considered to represent all of the potential risks and uncertainties which could impact the Group's performance.

Risk governance

The responsibility for the strategy and approach to risk governance and management lies with the Board. The Board is responsible for determining risk strategy, setting risk appetite and reviewing the effectiveness of risk and control processes in support of the Group's strategy. The Board is also responsible for establishing a clearly defined risk management structure with distinct roles and responsibilities. Under that structure, Internal Audit provides 'third line of defence' challenge and review of the management of risks and the adequacy and effectiveness of controls within the business. Management committees and the Risk Function provide 'second line of defence' oversight, challenge and review. Line managers have 'first line of defence' responsibility for the identification, measurement and management of the risks within their business areas.

The management of the risk framework, including oversight and challenge to the business on the effectiveness of their risk management activity and reporting of strategic, operational, conduct and financial Risk, is performed by specialist teams in the Risk Function. Second line of defence monitoring of the risk management framework is also performed by the Risk Function.

Management Committees

The management committees, under the authority delegated by the Board are described below:

Executive Committee ('ExCo')

ExCo is an advisory committee which supports the CEO in managing the business to achieve its strategic objectives. ExCo will normally meet three times each month with a specific focus to each meeting of either a) Conduct and Customers, b) Change, or c) Board reporting.

The following are sub-committees of ExCo:
- Investment Advisory Committee ('IAC')
- Remediation Steering Committee ('RSC')
- Executive Risk Committee ('ERC')

Other management committees include: Health & Safety Committee, Treating Customers Fairly Management Committee and the Customer Steering Group.

Investment Advisory Committee

The IAC supports, advises and makes recommendations to ExCo on the development and subsequent execution of proactive strategies that balance reduction of the UKAR Balance Sheet with the maximisation of taxpayer value.

Remediation Steering Committee

The RSC supports ExCo in effectively executing its obligations of ensuring fair and timely remediation to customers in circumstances where customer redress is appropriate. This includes providing oversight and challenge of the delivery of customer remediation or redress activities across the Group.

Executive Risk Committee

The ERC is a management sub-committee of ExCo with a reporting line to the Risk Committee ('RC'). The primary objective of the ERC is to provide technical oversight of key financial and operational risks and governance issues, including the review of the adequacy of risk mitigating actions, costs and capital effectiveness. The Committee supports, advises and makes recommendations to ExCo and the RC.

The following are sub-committees of the ERC:
- Asset & Liability Committee ('ALCO')
- Operational Risk Committee ('ORC')
- Credit Risk Committee ('CRC')
- Fraud & Professional Negligence Committee ('FPNC')

Asset & Liability Committee

The primary objectives of ALCO are to support and advise the ERC on the appropriate risk appetite and analyse and report exposures to market, liquidity, wholesale credit and capital risk.

Risk management and control (continued)

Pages 52 to 55 form an integral part of the audited Financial Statements

Operational Risk Committee

Principally, ORC supports the ERC in its oversight of the Principal Subsidiaries' adherence to Operational Risk Framework elements including Operational Risk, Financial Crime, Information Security and Business Continuity Management policies and procedures. The Committee provides challenge to the business on the content, accuracy and reliability of operational risk information and reports.

Credit Risk Committee

The CRC's primary purpose is to review credit policies, procedures and credit related proposals that have a financial impact on the business and to ensure the proposals balance the risk and reward ratio in line with the Credit Risk Appetite set by the Board.

Fraud & Professional Negligence Committee

The FPNC determines and oversees the implementation of the strategy to mitigate the impacts of fraud and/or professional negligence and ensures that recoveries are maximised. The FPNC supports risk oversight of key fraud and professional negligence matters through reporting into the ERC.

Risk management oversight

The Risk Function provides oversight and independent challenge to the management of Risk across the Group. The Function comprises a team of risk management specialists with responsibility for the embedding and oversight of operational, conduct, financial and strategic risk management, plus analysis and reporting of risk matters to the Board and the Board advisory and management committees. Key functional responsibilities include:

- Development of the Enterprise Wide Risk Management Framework ('EWRMF') and policies for the identification, assessment and mitigation of financial, strategic and operational risks;
- Provision of support to the Group business line management in the implementation of the EWRMF;
- Aggregate analyses and review of risk concentrations and sensitivities across the Principal Subsidiaries;
- Act as a point of reference for risk and control matters, providing advice to management, sharing best practice and carrying out special reviews as directed by the Board, RC, ExCo and sub committees of ExCo; and
- Provision of independent assessment of, and challenge to, the business areas' risk management and profiles to ensure that they are maintained in a robust manner.

Compliance

The role of Compliance is to:

- Provide assurance to the Board and ExCo, through the RC, that control processes are in operation to manage all regulatory and conduct risks across the Group;
- Contribute to the continuous improvement of regulatory compliance through provision of advice to the Group; and
- Oversee and co-ordinate liaison with the FCA on a day to day basis to promote open and co-operative relationships.

Internal audit

Internal audit activities are outsourced and are provided by Deloitte LLP. Deloitte services include the provision of a seconded Head of Internal Audit. This person is approved for the position by the FCA and the Audit Committee. However, the oversight of the Internal Audit function remains with the Group. The Head of Internal Audit reports to the Chairman of the Audit Committee and to the CEO.

The primary role of Internal Audit is to help the Board and Executive management to protect the assets, reputation and sustainability of the Group. The main objective of the Internal Audit department is to provide reliable, valued and timely assessment to the Board, Audit Committee and Executive management on the effectiveness of the system of internal controls in mitigating current and evolving key risks and in so doing, assist the organisation in enhancing the effectiveness of its approach to risk management.

Business and support activities of the Group are included in the scope of Internal Audit's responsibility and are subject to regular and appropriate internal audit review in accordance with Internal Audit's risk based Audit Plan.

Additional detail is contained in the Audit Committee Chairman's report on page 34.

Risk categorisation

The Group categorises Risk under the following headings:

(i) Credit risk

Credit risk is the potential for financial loss caused by a retail or commercial customer, or wholesale counterparty, failing to meet their obligations to the Principal Subsidiaries as they become due. As the Principal Subsidiaries are no longer making any new retail loans, the absolute level of retail credit risk is expected to decline as the current assets mature and wholesale credit risk will decline in line with the maturity profile of financial instruments and investments. Credit risk is the largest risk the Principal Subsidiaries face and the monitoring of the recoverability of loans and amounts due from counterparties is inherent across most of the Principal Subsidiaries' activities.

Risk management and control (continued)

Pages 52 to 55 form an integral part of the audited Financial Statements

(i) Credit risk (continued)

The Principal Subsidiaries employ credit behavioural scoring and fraud detection techniques to support loss minimising strategies. As no new lending is now being undertaken, the focus of credit risk activities is on:

- A proactive approach to the identification and control of loan impairment in the Residential and Commercial Credit Risk and Credit Control areas;
- Fraud and professional negligence investigation; and
- The use of credit behavioural scoring and other techniques to monitor the risk profile of the existing book.

Adverse changes in the credit quality of borrowers or a general deterioration in UK economic conditions could affect the recoverability and value of the Principal Subsidiaries' assets and, therefore, the financial performance of each subsidiary.

As credit risk is the main source of loss for the Principal Subsidiaries, a credit risk framework has been established as part of the overall governance framework to measure, mitigate and manage credit risk within risk appetite. To a lesser degree, the Group is exposed to other forms of credit risk such as those arising from settlement activities where the risk is a consequence of a transaction, rather than a driver of it.

The extent to which the impact of credit risk on the Group's Balance Sheet is mitigated is shown by the following table of provisions for mark-downs on impaired assets:

At 31 March / 31 December	Balance Sheet value 2014 £m	Provision 2014 £m	Balance Sheet value 2012 £m	Provision 2012 £m
Loans secured on residential property	**59,345**	**1,152**	66,056	1,411
Other secured loans	**623**	**91**	782	100
Unsecured personal loans	**1,282**	**215**	1,895	404
Wholesale assets	**8,598**	**444**	11,779	667

The Principal Subsidiaries' ability to influence the structure of their credit risk profiles, in the absence of asset sales, is largely restricted to the degree of control which they have over risk strategy, loan redemptions and credit collections activity. With the composition of the loan portfolio largely fixed in the short to medium term, the Principal Subsidiaries' credit risk profiles are now determined by the credit quality of the existing portfolio. Changes in credit quality will arise from changes in the underlying economic environment, assumptions about the future trends in the economy, changes in the specific characteristics of individual loans and the credit risk strategies developed to add value to the book whilst mitigating credit risk.

It is Group policy to monitor the profile of the Principal Subsidiaries' lending exposure on a quarterly basis. Changes in the risk profile are reported as part of the subsidiaries' stress tests. The stress tests forecast losses, impairment and capital requirements at a portfolio and product level over a 10 year horizon given a range of economic scenarios.

The Board receives a monthly update on changes in the key drivers of the lending credit risk profile, with more detailed information on the factors underlying these key drivers being reported monthly to the ERC.

Credit related policies and limits are developed and maintained within Credit Risk and are reviewed and approved annually by the Board, or when significant changes to policies are recommended. The ERC ensures that any exposure to credit risk remains within overall risk appetite levels as agreed by the Board.

Authorised credit risk limits for wholesale money market counterparties reflect their credit rating as well as size, depth and quality of their capital base. Wholesale Credit related policies and limits are developed and maintained by Wholesale Risk and are approved by the Board at least annually, or when material changes to policies are recommended.

The Principal Subsidiaries each hold a structured finance portfolio that primarily consists of investments in asset backed securities ('ABS'). The credit risk is determined by the quality of the underlying securitised assets. No new structured finance investments are permitted apart from the purchase of those issued by the Group's own secured funding vehicles.

(ii) Market risk

Market risk is the potential for change in Group income or Group net worth arising from movements in interest rates, foreign exchange rates or other market prices. Effective identification and management of market risk is essential for maintaining stable net interest income. The Principal Subsidiaries do not trade or make markets in any areas and market risk arises only as a legacy of past business and supporting core activities.

Interest rate risk is principally managed via interest rate swaps and foreign exchange risk by foreign exchange contracts.

The Board's appetite for Market Risk is set out in the Board approved Market Risk Policy. Responsibility for staying within risk appetite is delegated to the Finance & Investment Director and exposures are reported daily by Finance to senior management and monthly by Wholesale Risk to ALCO. ALCO is responsible for ensuring that the Finance & Investment Director implements market risk strategies consistent with the Board's risk appetite.

Risk management and control (continued)

Pages 52 to 55 form an integral part of the audited Financial Statements

(iii) Liquidity risk

Liquidity risk is the risk of being unable to pay liabilities as they fall due and arises from both the mismatch in asset, liability, derivative, and collateral cashflows and from unforeseen changes to these.

The Board's appetite for Liquidity Risk is low and is managed to ensure it has an adequate level of liquidity to meet its commitments at all times and maintained within agreed HM Treasury facilities, with minimum liquidity levels set out in the Board-approved Liquidity Risk Policy. Responsibility for managing liquidity risk is delegated to the Finance & Investment Director. Stress tests are used to assess the adequacy of liquidity both daily and monthly by Finance and Wholesale Risk and reported monthly to ALCO. ALCO is responsible for ensuring that the strategies of the Finance & Investment Director maintain liquidity risk within the Board's Risk Appetite.

Sterling liquidity is held as cash balances at the Bank of England. Euro and US dollar cash balances are held at a range of highly rated banks.

(iv) Conduct risk

Conduct risk is defined as the 'risk of UKAR treating its customers unfairly and delivering inappropriate outcomes leading to customer detriment or impacting market integrity'.

A new material risk category of conduct risk with a Conduct Risk Framework (CRF) was established during 2013. The CRF forms part of UKAR's existing Enterprise Wide Risk Management Framework (EWRMF). Through the EWRMF the approach to conduct risk will be led by Senior Management and the Board. It ensures a joined-up and consistent approach to the management of conduct risk and has been integrated into business strategy, management and decision making.

The CRF sets out the approach to the effective assessment, management and monitoring of conduct risk in accordance with our stated conduct risk appetite. UKAR has a zero risk appetite for systemic conduct risk that could lead to unfair customer outcomes or pose a risk to market integrity. Conduct risk is an integral part of the way UKAR does business, specifically, the interests of customers and market integrity are at the heart of UKAR's strategy, business and culture. With clear and visible leadership from the Board everyone takes responsibility for good conduct throughout our business model with established controls to deliver fair and appropriate outcomes to our customers. Our market conduct ensures that UKAR has no impact on market integrity. To support this annual mandatory conduct risk training has been introduced for all colleagues.

(v) Operational risk

Operational risk is defined as 'the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events'.

The Operational Risk Framework includes a balance of policies, appropriate procedures and internal controls to enable effective identification, assessment, monitoring and reporting of key operational risks. The framework is overseen and reported on by the operational risk function. The key objectives of the framework are as follows:

Risk and control self assessment

Provision of a consistent framework for the identification, assessment, monitoring and reporting of significant risks and key controls across the Group. Where controls are assessed as ineffective in design or operation, a defined Corrective Action Plan process is in place to develop, track and implement control improvements.

Operational risk event reporting

Provision of a consistent framework for the identification, investigation, assessment and reporting of operational risk events (losses, gains and near misses) across the Group. Root cause analysis performed as part of operational risk event reporting enhances the control environment by directing control improvement effort where there is a risk of event recurrence.

Operational risk weighted financial impact analysis and scenario analysis

The Group undertakes operational risk weighted financial impact analysis and scenario analysis to calculate the financial impact of both expected and unexpected operational risk events. This analysis facilitates a comparison between operational risk, financial exposure and the operational risk capital allocation derived under the Group's capital adequacy assessment process.

(vi) Strategic risk

Strategic risk is defined as the current or prospective risk to earnings and/or fair value, given the B&B Group and the NRAM Group Balance Sheet structure, arising from changes in the business environment and from adverse business decisions, improper implementation of decisions or lack of responsiveness to changes in the business environment.

UKAR considers the primary strategic risks to be macroeconomic environment, market pressures, structural asset/liability mix, political, regulatory and legal risk, infrastructure risk and project risk.

UKAR's focus is on continuous assessment and measurement of movement in strategic risk status in order to ensure continuous monitoring of potential impacts on the 10 Year Plan, annual business and operating plans, and UKAR's overarching strategic objectives. Thus, close oversight of movements in strategic risk (proximity, financial impact, probability) is maintained via monthly reporting to ExCo and the Board. Where appropriate, and taking in to account the mainly external nature of strategic risk, risk management strategies can then be defined to mitigate the impact of a risk event arising.

Corporate social responsibility report

UKAR aims to conduct its business in a socially responsible manner in respect of our customers, the workplace, the communities we operate in and the environment.

Customers

The Group has almost 467,000 customers, making us one of the largest mortgage service providers in the UK.

We are committed to:
- Ensuring that simplicity, integrity and truth applies to everything we do;
- Supporting vulnerable customers; and
- Supporting customers in financial difficulty.

Workplace

UKAR's employment practices reflect international and national standards covering areas such as minimum working age, working hours, health and safety and discrimination.

UKAR aims to recruit high calibre employees from all sections of the community, ensuring that no employee or job applicant receives less favourable treatment on grounds which are not related to the job. We adopt best practice policies and procedures which form a key part of our induction programmes together with the standards of behaviour we should all abide by and expect from each other.

A comprehensive training and development programme for colleagues throughout UKAR provides colleagues with the skills and specialist development opportunities to achieve their potential in order to help them do their job today and for any future roles they may undertake. Since UKAR was formed, 184 colleagues have achieved an external qualification through the support of the UKAR training academy. In 2010 we introduced our Apprenticeship Scheme and we currently have 20 apprentices within the business and intend to recruit a further 20 this year. Our Undergraduate scheme continued with four more internships in 2013 and we launched our Graduate scheme with three placements and plan to recruit seven more in 2014. We also support the government's Centre of Excellence initiatives.

UKAR believes that promoting both a diverse culture and diverse working practices will help retain and engage talent, maintain motivation and improve the wellbeing of all colleagues in the workplace. We build a working environment based on trust and openness and encourage effective and efficient communication throughout the organisation.

Colleague engagement is important to us and that is why 'Being a Great Place to Work' is one of our four strategic objectives. It is important to us that colleagues feel valued, are proud of the contribution they make and are given the opportunity to grow and learn new skills. We use a variety of channels for communicating with our colleagues including our intranet site, monthly team meetings, regular open surgeries with our CEO and members of ExCo and a quarterly magazine which is developed with the support of an editorial panel drawn from colleagues throughout the business. We have a very popular recognition scheme based around our core values and new ideas are encouraged via a suggestion scheme. We publish weekly 'blogs' from ExCo members to highlight the efforts we are making to encourage a 'One Team' culture both within and between different sites and departments. We believe that colleagues who enjoy working at UKAR strive to do the best they can and act in a professional way which will ensure that our customers receive the best possible outcomes and the organisation maximises value for the taxpayer.

We have a good relationship with the Unite union and colleagues also represent the business on the Health & Safety Committee. We are flexible in the way we approach the personal circumstances of colleagues, preventing discrimination for example on family grounds and ensuring the workplace needs of those with families are addressed. We report our sickness and stress absence data to the Board on a monthly basis and throughout 2013/14 we remained below the national benchmark for sickness and stress. In particular we monitor stress related absence and investigations to date have shown no particular trends arising from particular business areas or site locations.

Community

We are committed to:
- Using the skills of the business to support education in our communities;
- Building the skills of our colleagues through community engagement; and
- Supporting colleagues with their own community and charity initiatives.

During 2013/14, UKAR supported Heart Research UK as our corporate charity.

At each major site we also supported a local charity chosen by our colleagues. These were Yorkshire Air Ambulance in Crossflatts and Grace House Children's Hospice in Doxford. The following amounts were raised for these charities in 2013/14:
- Heart Research UK £17,966
- Yorkshire Air Ambulance £15,008
- Grace House Children's Hospice £11,322

£5,643 was also raised for other charities in 2013/14.

In addition, UKAR supports other charitable fundraising activities by adding up to £250 to funds raised per employee and by matching employee donations to charity through a payroll giving programme. During 2013/14, in total, UKAR matched employee fundraising to the total of £35,809 and payroll giving totalled £19,037.

Corporate social responsibility report (continued)

Community (continued)

UKAR works with Young Enterprise to give colleagues the opportunity to have a positive impact on young people in the local communities by volunteering to deliver their programmes in local schools.

Young Enterprise is a charity set up to work with schools to inspire young people with the confidence, ability and ambition to succeed in a challenging and changing economy.

During 2013/14, 543 employees took part in volunteering events.

Environment

We are committed to:

- Reducing environmental impact wherever possible;
- Increasing recycling programmes; and
- Creating awareness of environmental programmes and engaging colleagues in these activities.

We seek to improve our environmental performance through a range of initiatives and in 2013/14 we achieved the following:

Recycling	95.97% of waste recycled.
Landfill	4.03% of waste sent to landfill.
Carbon emissions*	Reduced by 2.7%.

Wherever possible surplus furniture and equipment is donated to charitable organisations or is recycled in other ways.

Corporate Social Responsibility in 2014/15

In 2014/15 our Community Investment Approach will focus on using the skills of the business to support youth education in our communities and address health as a social issue which affects our business and the communities we operate in.

UKAR's corporate charity in 2014/15 is MIND. We will also support the following local charities:

Crossflatts	Martin House Children's Hospice
Doxford	Daft as a Brush Cancer Patient Care

* Carbon produced from utilities (Gas/Electric consumption).

Other matters

Review of business, future developments and uncertainties

A review of the business, future developments and uncertainties is set out in the Strategic Report on pages 6 to 14.

Principal risks

Principal risks of the UKAR Group are covered on pages 52 to 55.

Dividends

The Directors do not propose the payment of any dividend in respect of the period ended 31 March 2014.

Major shareholders

As at the date of this Report, all shares in UKAR are held by HM Treasury and all shares in B&B and NRAM are held by UKAR.

Change of name

On 16th May 2014, the company formerly known as Northern Rock (Asset Management) plc changed its name to NRAM plc.

Employee involvement

The People Strategy of UKAR is detailed at pages 12 and 13.

The Group is committed to employment policies which follow best practice, based on equal opportunities for all employees, irrespective of sex, race, colour, disability or marital status. The Group gives full and fair consideration to applications for employment from disabled persons, having regard to their particular aptitudes and abilities. Appropriate arrangements are made for the continued employment and training, career development and promotion of disabled persons employed by the Group. If members of staff become disabled the Group continues employment, either in the same or an alternative position, with appropriate retraining being given if necessary.

Directors’ indemnities

The Articles of Association provide the power to indemnify any Director against liabilities incurred as a result of their office.

UKAR has also provided each Director with a Deed of Indemnity, which constituted ‘qualifying third party indemnity provision’ in accordance with the provisions of the Companies Act 2006. The Deeds were in force during the whole of the financial period ended 31 March 2014 and remains in force as at the date of approval of the Director’s Report. The Deeds were also in force for the benefit of Directors who resigned during the period.

The Deeds indemnify the Directors to the fullest extent permitted by law against all losses suffered or incurred in respect of acts and omissions arising as a result of holding office. The indemnities also extend to the reimbursement of each Director with the costs of defending all claims, actions and proceedings including regulatory investigation arising out of or connected with the exercise of, or failure to exercise, any of the Director’s powers, duties or responsibilities as an officer, director, trustee, agent or employee of the Group and any of its subsidiaries. Reimbursement is subject to the Director’s obligation to repay the Company in accordance with the provisions of the Companies Act 2006. The payment obligations of the Company under each Deed of Indemnity are backed by a specific guarantee in favour of the Director entered into between each Director and HM Treasury.

UKAR has also arranged Directors’ and Officers’ Insurance on behalf of the Directors in accordance with the provisions of the Companies Act 2006.

Annual General Meeting (‘AGM’)

It is proposed that the AGM of the Company will be held on 1 July 2014.

Independent Auditors

A resolution to re-appoint PricewaterhouseCoopers LLP as the Group’s auditors will be put to the Shareholder at the forthcoming AGM.

Disclosure of information to the Auditors

As at the date of this report, each person who is a Director confirms that:

- So far as each Director is aware there is no relevant audit information of which the Company’s auditors are unaware; and
- Each Director has taken such steps as he or she ought to have taken as a Director in order to make him or herself aware of any relevant audit information and to establish that the Company’s auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 (2) of the Companies Act 2006.

Statement of Directors' and Accounting Officer's responsibilities in respect of the Directors' Report and the Financial Statements

The Directors are responsible for preparing the Annual Report, the Directors' Remuneration Report and the Financial Statements in accordance with applicable law and regulations. Company law requires the Directors to prepare financial statements for each financial period. Under that law the Directors have prepared the Group and Parent Company Financial Statements in accordance with International Financial Reporting Standards ('IFRS') as adopted by the European Union. 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 the Company and of the profit or loss of the Group for that period. In preparing these Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRS as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the Financial Statements; and
- prepare the Financial Statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the Financial Statements and the Directors' Remuneration Report comply with the Companies Act 2006 and, as regards the Group Financial Statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the Company's website and legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the Directors confirms that, to the best of each person's knowledge and belief:

- the Financial Statements, prepared in accordance with IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group and Company; and
- the Directors' Report contained in the Annual Report includes a fair review of the development and performance of the business and the position of the Company and Group, together with a description of the principal risks and uncertainties that they face.
- The Annual Report and Accounts, taken as a whole, is fair, balanced and understandable, providing the information necessary for shareholders to assess the Group's performance, business model and strategy.

This report has been approved by the Board of Directors and is signed by the Chief Executive Officer on behalf of the Board of Directors.

The Accounting Officer of HM Treasury has designated UKAR's Chief Executive Officer as the Accounting Officer of UKAR. The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which the Accounting Officer is answerable, for keeping proper records and for safeguarding UKFI's assets, are set out in 'Managing Public Money', published by HM Treasury.

In preparing the Financial Statements, the Accounting Officer is required to comply with the requirements of the Government Financial Reporting Manual and in particular to:

- observe the Accounts Direction issued by HM Treasury, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards as set out in the Government Financial Reporting Manual have been followed, and disclose and explain any material departures in the Financial Statements; and
- prepare the Financial Statements on a going concern basis.

Richard Banks

Chief Executive Officer, on behalf of the Board

2 June 2014

Independent Auditors' report to the Members of UK Asset Resolution Limited

Report on the Financial Statements

Our opinion

In our opinion, the Financial Statements, defined below:
- give a true and fair view of the state of the Group's affairs as at 31 March 2014 and of its profit and cash flows for the 15 month period then ended;
- have been properly prepared in accordance with International Financial Reporting Standards ('IFRS') as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Financial Statements, Article 4 of the IAS Regulation.

This opinion is to be read in the context of what we say in the remainder of this report.

What we have audited

The Group Financial Statements (the 'Financial Statements'), which are prepared by UK Asset Resolution Limited (the 'Parent Company'), comprise:
- the Consolidated Balance Sheet as at 31 March 2014;
- the Consolidated Income Statement and Consolidated Statement of Comprehensive Income for the period then ended;
- the Consolidated Cash Flow Statement for the period then ended;
- the Consolidated Statement of Changes in Equity for the period then ended; and
- the notes to the Financial Statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in their preparation is applicable law and IFRS as adopted by the European Union.

Certain disclosures required by the financial reporting framework have been presented elsewhere in the Annual Report and Accounts (the 'Annual Report'), rather than in the notes to the Financial Statements. These are cross-referenced from the Financial Statements and are identified as audited.

What an audit of financial statements involves

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ('ISAs (UK & Ireland)'). An audit involves obtaining evidence about the amounts and disclosures in the Financial Statements sufficient to give reasonable assurance that the Financial Statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:
- whether the accounting policies are appropriate to the Group's 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.

Overview of our audit approach

Materiality

We set certain thresholds for materiality. These helped us to determine the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the Financial Statements as a whole.

Based on our professional judgement, we determined overall materiality for the Financial Statements as a whole to be £113 million which represents 0.15% of the total assets of the Group. In arriving at this judgement we had regard to the total assets of the Group given that the key element of the Financial Statements is loans to customers. These represent a significant proportion of the total assets, and given the nature of the Group's activities in servicing mortgage loans there are a number of Key Performance Indicator's ('KPI's') around asset management.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £2.5 million as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Overview of the scope of our audit

The Group comprises Bradford & Bingley plc and its subsidiaries ('B&B'), NRAM plc and its subsidiaries ('NRAM') and UKAR Corporate Services Limited (UKARcs). For the purpose of our audit, we identified two significant components, being B&B and NRAM.

We performed an audit of the complete financial information of both these components as both have statutory audit requirements.

This, together with additional procedures performed on balances arising as a result of the Group's consolidation process gave us the evidence we needed for our opinion on the Financial Statements as a whole.

Independent Auditors' report to the Members of UK Asset Resolution Limited (continued)

Report on the Financial Statements (continued)

Overview of our audit approach (continued)

Areas of particular audit focus

In preparing the Financial Statements, the Directors made a number of subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. We primarily focused our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the Financial Statements.

In our audit, we tested and examined information, using sampling and other auditing techniques, to the extent we considered necessary to provide a reasonable basis for us to draw conclusions. We obtained audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

We considered the following areas to be those that required particular focus in the current period. This is not a complete list of all risks or areas of focus identified by our audit. We discussed these areas of focus with the Audit Committee.

Area of focus	How the scope of our audit addressed the area of focus
Loan loss impairment We focused on this area because the Directors make complex and subjective judgements over both the timing of the recognition of impairments and the estimation of the extent of the impairment. This includes making judgements in respect of the assumptions that underpin the impairment models, such as probability of default, property forced sales discounts and expectations of movements in future house prices (see note 2 to the financial statements).	We assessed the design and implementation of controls, and tested the operating effectiveness of key controls over loan impairment calculations. Where impairment was calculated on a collective modelled basis, we evaluated and tested the controls around the impairment models used by management including reconciliations to source systems, access and change controls, and the controls around reviews of the outputs. In addition, we tested the integrity of the provisioning model, including the completeness and accuracy of the data inputs. We focussed on the principal assumptions underlying the calculations and considered whether all relevant risks were reflected, and where not, whether model overlays appropriately reflected those risks. We have challenged management on the reasonableness of each key assumption applied in the model including comparing the assumptions to observable evidence. We challenged management by using our industry knowledge and experience and through comparisons to industry data. Testing has then been performed to ensure that the assumptions have been implemented correctly in the model. Where impairment was individually calculated, we tested a sample of loans and advances to ascertain whether the impairment event had been identified in a timely manner and whether the provision is reasonable given the specific details of the impaired mortgage account. This included assessment of loans not impaired to gain comfort over the completeness of the provision.
Customer redress provisions The Group has made provisions that require significant judgements to be made by management, due to uncertainties in relation to the amount of current and potential future claims from customers for products and business mis-sold to customers in the past (see note 27 to the financial statements).	We focused on identifying products and business with exposure, particularly in relation to Payment Protection Insurance redress (PPI) and Consumer Credit Act redress (CCA), but we also assessed potential exposures from emerging industry issues. For all provisions made, we assessed the current assumptions underpinning the calculations, including future claims volumes and settlement amounts. We have discussed the provisions with internal legal counsel and read associated legal correspondence from external counsel and legal advisors. Given the judgemental nature of the uncertainties that exist over the likelihood and value of future customer claims and the sensitivity of these provisions to changes in underlying assumptions, we have performed sensitivity analysis on the forecasts. Where management have concluded that a provision is not required in respect of potential customer redress, we have challenged management's basis for this judgement and critically assessed the evidence available to support the position taken. We have also critically assessed the disclosures made in the Financial Statements in respect of provisions and contingent liabilities and assessed those made in the Financial Review for consistency with the Financial Statements.
Management override of controls ISAs (UK & Ireland) state that the risk of management override of controls is a significant risk on all audit engagements.	We assessed the design and implementation of controls and tested the operating effectiveness of company-wide key controls. We considered whether there was evidence of bias by the Director's or management in the significant accounting estimates and judgements relevant to the Financial Statements. We also identified higher risk journal entries in the general ledger which included those with a material impact on the income statement, round sum postings and postings at unusual times. We assessed their appropriateness through substantiation to relevant supporting evidence. We also incorporated unpredictability into our audit approach.
Fraud in revenue recognition ISAs (UK & Ireland) presume there is a risk of fraud in revenue recognition because of the pressure management may feel to achieve planned results. We focused on the occurrence of retail and treasury interest and the risk of manual adjustments to system generated interest income calculations.	We tested the design and implementation of, and tested the operating effectiveness of, controls over the whether revenue had occurred. We performed substantive audit procedures over revenue recognition (including using computer assisted audit techniques), to recalculate interest income from loans to customers.

Independent Auditors' report to the Members of UK Asset Resolution Limited (continued)

Opinion on other matter prescribed by the Companies Act 2006

In our opinion, the information given in the Strategic Report and the Directors' Report for the financial period for which the Financial Statements are prepared is consistent with the Financial Statements.

Other matters on which we are required to report by exception

Adequacy of information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion, we have not received all the information and explanations we require for our audit. We have no exceptions to report arising from this responsibility.

Directors' remuneration

Under the Companies Act 2006 we are required to report if, in our opinion, certain disclosures of Directors' remuneration specified by law have not been made. We have no exceptions to report arising from this responsibility.

Responsibilities for the Financial Statements and the audit

Our responsibilities and those of the Directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 59, 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 ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Parent Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Other matter

We have reported separately on the Parent Company Financial Statements of UK Asset Resolution Limited for the 15 month period ended 31 March 2014 and on the information in the Directors' Remuneration Report that is described as having been audited.

Craig Gentle (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors

London

2 June 2014

a) The maintenance and integrity of the UK Asset Resolution Limited website is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the Financial Statements since they were initially presented on the website.
b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The Accounts

Notes to the Financial Statements

UKAR Limited Company Accounts

Notes to the Company Financial Statements

Appendix A

Consolidated Income Statement

	Note	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Interest receivable and similar income	3	**2,884.5**	2,624.0
Interest expense and similar charges	3	**(1,053.9)**	(1,139.1)
Net interest income	3	**1,830.6**	1,484.9
Fee and commission income		**33.0**	29.3
Fee and commission expense		**(15.1)**	(12.3)
Net fee and commission income		**17.9**	17.0
Net gains on financial instruments designated at fair value	4	**-**	17.5
Net realised gains less losses on investment securities	5	**(12.5)**	(14.9)
Unrealised fair value movements on financial instruments	6	**(29.6)**	(42.8)
Hedge ineffectiveness	6	**(27.6)**	(28.4)
Provision for customer redress	26	**(115.8)**	(419.0)
Other operating income		**10.9**	10.9
Non-interest income		**(156.7)**	(459.7)
Net operating income		**1,673.9**	1,025.2
Administrative expenses:			
– ongoing	7	**(246.3)**	(207.3)
– other net expenses	7	**-**	(59.7)
Impairment on loans to customers	14	**(95.1)**	(241.4)
Net impairment release on investment securities	11	**17.7**	30.2
Profit on sale of unsecured loans	13	**21.2**	-
Gain on repurchase of own liabilities	8	**2.9**	143.5
Profit before taxation		**1,374.3**	690.5
Taxation	9	**(308.3)**	(126.7)
Profit for the financial period		**1,066.0**	563.8

The notes on pages 70 to 123 form an integral part of these Financial Statements.

The results above arise from continuing activities.

Consolidated Statement of Comprehensive Income

For the 15 months to 31 March 2014	Gross of tax £m	Tax £m	Net of tax £m
Profit for the financial period	**1,374.3**	**(308.3)**	**1,066.0***
Other comprehensive income/(expense)			
Items that may be reclassified subsequently to profit or loss:			
Available-for-sale instruments:			
– net gains recognised in available-for-sale reserve during the period	**66.7**	**(15.2)**	**51.5**
– amounts transferred from available-for-sale reserve and recognised in profit during the period	**(1.9)**	**0.4**	**(1.5)**
Cash flow hedges:			
– net losses recognised in cash flow hedge reserve during the period	**(435.8)**	**165.4**	**(270.4)**
– amounts transferred from cash flow hedge reserve and recognised in profit during the period	**349.8**	**(135.5)**	**214.3**
	(21.2)	**15.1**	**(6.1)**
Items that will not be reclassified subsequently to profit or loss:			
Retirement benefit remeasurements	**4.5**	**(1.7)**	**2.8**
	4.5	**(1.7)**	**2.8**
Total other comprehensive (expense)/income	**(16.7)**	**13.4**	**(3.3)**
Total comprehensive income/(expense) for the financial period	**1,357.6**	**(294.9)**	**1,062.7***

For the 12 months to 31 December 2012	Gross of tax £m	Tax £m	Net of tax £m
Profit for the financial year	690.5	(126.7)	563.8*
Other comprehensive income/(expense)			
Items that may be reclassified subsequently to profit or loss:			
Available-for-sale instruments:			
– net gains recognised in available-for-sale reserve during the year	73.0	(17.8)	55.2
– amounts transferred from available-for-sale reserve and recognised in profit during the year	(2.2)	0.5	(1.7)
Cash flow hedges:			
– net gains recognised in cash flow hedge reserve during the year	(1,236.9)	647.1	(589.8)
– amounts transferred from cash flow hedge reserve and recognised in profit during the year	1,322.0	(692.5)	629.5
	155.9	(62.7)	93.2
Items that will not be reclassified subsequently to profit or loss:			
Retirement benefit remeasurements	(87.2)	19.6	(67.6)
	(87.2)	19.6	(67.6)
Total other comprehensive income/(expense)	68.7	(43.1)	25.6
Total comprehensive income/(expense) for the financial year	759.2	(169.8)	589.4*

* Of which £18.0m (2012: £14.1m) is attributable to the holders of the non-shareholders' funds, as detailed in note 31.

Consolidated Balance Sheet

	Note	At 31 March 2014 £m	At 31 December 2012 £m
Assets			
Balances with the Bank of England	10	**5,020.3**	5,599.8
Cash at bank and in hand	12	**2,503.2**	4,129.2
Investment securities	11	**1,074.7**	2,049.9
Loans to customers	13	**61,249.5**	68,733.6
Fair value adjustments on portfolio hedging	13	**308.8**	493.8
Derivative financial instruments	35 (d)	**4,616.2**	5,720.2
Other assets	17	**37.4**	40.7
Retirement benefit assets	18 (b)	**65.3**	43.0
Property, plant and equipment	20	**21.9**	28.7
Intangible assets	21	**42.7**	47.3
Total assets		**74,940.0**	86,886.2
Liabilities			
Amounts due to banks	22	**3,119.2**	4,794.9
Statutory Debt and HM Treasury loans	23	**38,350.5**	43,487.3
Derivative financial instruments	35 (d)	**446.0**	783.7
Debt securities in issue	24	**25,886.0**	31,620.1
Other liabilities	25	**159.8**	169.8
Current tax liabilities		**183.4**	64.1
Deferred tax liabilities	16	**50.8**	43.9
Retirement benefit obligations	18 (a)	**20.3**	70.5
Provisions	26	**167.7**	227.6
Capital instruments	27	**215.3**	359.2
Total liabilities		**68,599.0**	81,621.1
Equity			
Issued capital and reserves attributable to equity holder of the parent:			
– share capital	28	**1.2**	1.2
– reserves	29	**1,313.2**	1,319.3
– retained earnings *		**4,830.0**	3,766.0
Share capital and reserves		**6,144.4**	5,086.5
Non-shareholders' funds *	31	**196.6**	178.6
Total equity		**6,341.0**	5,265.1
Total equity and liabilities		**74,940.0**	86,886.2

* Non-shareholders' funds and retained earnings as at 31 December 2012 have been re-presented compared to the amounts presented in the 2012 Annual Report and Accounts, as detailed on page 68.

The notes on pages 70 to 123 form an integral part of these Financial Statements.

The Financial Statements on pages 65 to 123 were approved by the Board of Directors on 2 June 2014 and signed on its behalf by:

Richard Banks
Chief Executive Officer

Richard Pym
Chairman

UK Asset Resolution Limited is registered in England and Wales under company number 07301961.

Consolidated Statement of Changes in Equity

For the 15 months to 31 March 2014	Share capital £m	Available-for-sale reserve £m	Cash flow hedge reserve £m	Merger reserve £m	Retained earnings* £m	Total share capital and reserves £m	Non-shareholders' funds* £m	Total equity £m
At 1 January 2013	**1.2**	**(53.4)**	**250.1**	**1,122.6**	**3,766.0**	**5,086.5**	**178.6**	**5,265.1**
Other comprehensive income / (expense):								
– net movement in available-for-sale reserve	-	64.8	-	-	-	64.8	-	64.8
– net movement in cash flow hedge reserve	-	-	(86.0)	-	-	(86.0)	-	(86.0)
– retirement benefit remeasurements	-	-	-	-	4.5	4.5	-	4.5
– tax effects of the above	-	(14.8)	29.9	-	(1.7)	13.4	-	13.4
Total other comprehensive income / (expense)	-	50.0	(56.1)	-	2.8	(3.3)	-	(3.3)
Profit for the financial period	-	-	-	-	1,048.0	1,048.0	18.0	1,066.0
Total comprehensive income / (expense)	-	50.0	(56.1)	-	1,050.8	1,044.7	18.0	1,062.7
Release of time-expired provision for unclaimed shares (see note 30)	-	-	-	-	13.2	13.2	-	13.2
At 31 March 2014	**1.2**	**(3.4)**	**194.0**	**1,122.6**	**4,830.0**	**6,144.4**	**196.6**	**6,341.0**

For the 12 months to 31 December 2012	Share capital £m	Available-for-sale reserve £m	Cash flow hedge reserve £m	Merger reserve £m	Retained earnings* £m	Total share capital and reserves £m	Non-shareholders' funds* £m	Total equity £m
At 1 January 2012	1.2	(106.9)	210.4	1,122.6	3,283.7	4,511.0	165.4	4,676.4
Other comprehensive income / (expense):								
– net movement in available-for-sale reserve	-	70.8	-	-	-	70.8	-	70.8
– net movement in cash flow hedge reserve	-	-	85.1	-	-	85.1	-	85.1
– retirement benefit remeasurements	-	-	-	-	(87.2)	(87.2)	-	(87.2)
– tax effects of the above	-	(17.3)	(45.4)	-	19.6	(43.1)	-	(43.1)
Total other comprehensive income / (expense)	-	53.5	39.7	-	(67.6)	25.6	-	25.6
Profit for the financial year	-	-	-	-	549.7	549.7	14.1	563.8
Total comprehensive income	-	53.5	39.7	-	482.1	575.3	14.1	589.4
Gain on repurchase of equity (see note 8)	-	-	-	-	0.2	0.2	(0.9)	(0.7)
At 31 December 2012	1.2	(53.4)	250.1	1,122.6	3,766.0	5,086.5	178.6	5,265.1

* Non-shareholders' funds and retained earnings as at 1 January 2012 and 31 December 2012 have been re-presented compared to the amounts presented in the 2012 Annual Report and Accounts in order to present, as part of non-shareholders' funds, the cumulative amount of coupons which have been withheld on reserve capital instruments and subordinated notes. As a result, non-shareholders' funds are now presented as being £53.8m higher and retained earnings £53.8m lower as at 31 December 2012 than were presented in the 2012 Annual Report and Accounts (2011: £39.7m). Further detail is provided in note 31.

Consolidated Cash Flow Statement

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Cash flows from operating activities:		
Profit before taxation for the financial period	**1,374.3**	690.5
Adjustments to reconcile profit to cash generated from operating activities:		
– profit on sale of unsecured loans	**(21.2)**	-
– provision for customer redress	**115.8**	419.0
– depreciation and amortisation	**19.4**	20.5
– net (gain)/loss on sale of property, plant and equipment	**(7.3)**	0.4
– impairment on loans to customers	**95.1**	241.4
– net impairment release on investment securities	**(17.7)**	(30.2)
– gain on repurchase of own liabilities	**(2.9)**	(143.5)
– fair value adjustments on financial instruments	**(64.1)**	(178.1)
– other non-cash movements	**254.2**	(809.6)
Cash flows from operating activities before changes in operating assets and liabilities	**1,745.6**	210.4
Net (increase)/decrease in operating assets:		
– cash at bank with original maturity of three months or more	**6.0**	-
– loans to customers	**7,099.8**	5,622.0
– sale of secured and unsecured loans	**308.7**	465.0
– derivative financial instruments receivable	**1,103.9**	1,649.0
– other assets	**41.2**	(36.9)
Net increase/(decrease) in operating liabilities:		
– amounts due to banks	**(1,675.7)**	719.9
– derivative financial instruments payable	**(337.7)**	(181.7)
– debt securities in issue	**(5,652.3)**	(4,749.2)
– other liabilities	**(86.8)**	89.0
– provisions	**(186.4)**	(210.9)
Income tax paid	**(168.7)**	(175.8)
Net cash generated from operating activities	**2,197.6**	3,400.8
Cash flows from investing activities:		
– purchase of property, plant and equipment and intangible assets	**(10.7)**	(24.5)
– proceeds from sale of property, plant and equipment and investment property	**10.0**	40.8
– purchase of investment securities	**-**	(74.3)
– proceeds from sale and redemption of investment securities	**881.1**	959.4
Net cash generated from investing activities	**880.4**	901.4
Cash flows used in financing activities:		
– repayment of HM Treasury loans	**(5,274.8)**	(3,098.8)
– repurchase of own liabilities and equity	**(3.2)**	(394.7)
Net cash used in financing activities	**(5,278.0)**	(3,493.5)
Net (decrease)/increase in cash and cash equivalents	**(2,200.0)**	808.7
Cash and cash equivalents at beginning of period	**9,721.1**	8,912.4
Cash and cash equivalents at end of period	**7,521.1**	9,721.1
Represented by cash and assets with original maturity of three months or less within:		
– balances with the Bank of England	**5,018.1**	5,597.4
– cash at bank and in hand	**2,503.0**	4,122.7
– investment securities	**-**	1.0
Total cash and cash equivalents at end of period	**7,521.1**	9,721.1

1. Principal accounting policies

UK Asset Resolution Limited ('UKAR' or 'the Company') is a private limited company incorporated on 1 July 2010 and domiciled in the United Kingdom. UKAR acquired Bradford & Bingley plc ('B&B') and NRAM plc ('NRAM') (formerly Northern Rock (Asset Management) plc) by a share-for-share exchange on 1 October 2010. These consolidated Financial Statements are prepared under the 'predecessor accounting' method, which presents the UKAR consolidated results as if the UKAR Group ('the Group') had always been in existence in its present form. In addition, the Company owns 100% of the share capital of UKAR Corporate Services Limited ('UKARcs'), which was incorporated on 20 June 2013 (see note E). The Financial Statements of the UKAR Company are presented on pages 126 to 130 and form an integral part of these Financial Statements. The Company's accounting reference date has been changed from 31 December to 31 March to align to the year end of the Company's ultimate parent, HM Treasury, therefore these consolidated Financial Statements cover the 15 months ended 31 March 2014. To aid year-on-year comparisons, Appendix A on pages 131 to 132 sets out unaudited Consolidated Income Statements for the Group for the 12 months ended 31 March 2014, the 12 months ended 31 March 2013 and an unaudited Consolidated Balance Sheet for the Group as at 31 March 2013. This unaudited information has been prepared using accounting bases and policies which are consistent with those used in the audited Financial Statements.

These Financial Statements were authorised for issue by the Directors on 2 June 2014 and will be put to the shareholder for approval at UKAR's Annual General Meeting to be held on 1 July 2014.

(a) Statement of compliance

Both the UKAR Company Financial Statements and the Group (comprising UKAR and its subsidiaries) Financial Statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards ('IFRS') as adopted by the EU. In publishing the UKAR Company Financial Statements, here together with the Group Financial Statements, the UKAR Company has taken advantage of the exemption in s408 of the Companies Act 2006 not to present its individual Income Statement and related notes.

For these 2014 Financial Statements, including the 2012 comparative financial information where applicable, the Group and Company have adopted for the first time the following statements:

- IFRS 10 'Consolidated Financial Statements', IFRS 11 'Joint Arrangements' and IFRS 12 'Disclosure of Interests in Other Entities', along with the 2011 revisions to IAS 27 'Separate Financial Statements' and IAS 28 'Investments in Associates'. These statements amend the criteria for consolidation of subsidiaries, but had no impact on the Financial Statements other than expanded disclosure. The Group and Company have not taken the option for EU companies to defer adoption to 2015.
- IFRS 13 'Fair Value Measurement' and the associated amendments to IFRS 7 'Financial Instruments: Disclosures'. IFRS 13 sets out principles for measurement of the fair value of financial assets and liabilities but does not change which items are carried at fair value. In order to comply with IFRS 13 the Group and Company have made minor changes to methods for calculating fair values; there was no material impact on the Group's or Company's Income Statement, Statement of Comprehensive Income, Balance Sheet or Cash Flow Statement for 2013-14 or 2012, and in accordance with IFRS 13 no restatement has been made of 2012. The methodology for calculating the fair value of loans to customers (disclosed in note 35(a)) has been revised, and the fair value disclosed in respect of 2012 has been changed from that disclosed in the 2012 Annual Report and Accounts. IFRS 13 and the amended IFRS 7 also introduced additional disclosure requirements.
- The December 2011 amendments to IFRS 7 'Financial Instruments: Disclosures' and IAS 32 'Financial Instruments: Presentation' relating to the offsetting of financial assets and financial liabilities. These amendments had no material impact on the Group or Company.
- The June 2011 amendments to IAS 1 'Presentation of Financial Statements' relating to 'Presentation of Items of Other Comprehensive Income'. As a result, the Statement of Comprehensive Income now shows which elements of other comprehensive income may subsequently be reclassified to profit or loss.
- The June 2011 amendments to IAS 19 'Employee Benefits'. This has been applied in calculating the costs of the defined benefit schemes and in the calculation of defined benefit scheme assets and obligations. The impact on the Financial Statements is not considered material.
- The Annual Improvements to IFRSs 2009-2011 Cycle, issued in May 2012. These changes had no material impact on the Group or Company.

For these 2014 Financial Statements the Group and Company have not adopted the following statements; the Group and Company are assessing the impacts of these statements on their Financial Statements:

- IFRS 9 'Financial Instruments', sections of which have been issued as part of the International Accounting Standard Board's ('IASB's') project to replace IAS 39 'Financial Instruments: Recognition and Measurement'. This statement has not yet been adopted for use in the EU and the Group continues to monitor developments.
- The June 2013 amendments to IAS 39 relating to ' Novation of Derivatives and Continuation of Hedge Accounting' which will be mandatory for the Group and Company Financial Statements for the year to 31 March 2015. This restricts the circumstances in which a novation of a derivative contract may be treated as a continuation of an existing hedge relationship.
- The Annual Improvements to IFRSs 2010-2012 Cycle issued in December 2013. These changes are mandatory for the Group and Company Financial Statements for the year to 31 March 2015.
- The Annual Improvements to IFRSs 2011-2013 Cycle issued in December 2013. These changes are mandatory for the Group and Company Financial Statements for the year to 31 March 2015.

All other new standards, amendments to standards and interpretations are not considered relevant to and have no impact upon the Financial Statements of the Group or UKAR Company.

1. Principal accounting policies (continued)

(b) Basis of preparation

The Financial Statements have been prepared on a going concern basis and using the historical cost convention except:

(i) the following assets and liabilities are carried at their fair value:
- derivative financial instruments;
- financial instruments categorised under IAS 39 as 'available-for-sale'; and
- investment property; and

(ii) where fair value hedge accounting has been applied, the carrying value of hedged items has been adjusted to take account of the fair value of the risk which has been hedged.

The validity of the going concern basis of accounting is dependent upon the funding position of the UKAR Company, B&B and NRAM. At the date of approval of these Financial Statements the Group is reliant upon the financing facilities and also upon the guarantee arrangements provided to B&B and NRAM by HM Treasury. Withdrawal of the financing facilities or the guarantee arrangements would have a significant impact on the Group's operations and its ability to continue as a going concern, in which case adjustments may have to be made to reduce the carrying value of assets to recoverable amounts and to provide for further liabilities that might arise. At the signing date of these Financial Statements HM Treasury has confirmed its intentions to continue to provide funding until at least 1 January 2016. It has also committed to convert up to £1.6bn of its loan to NRAM to meet regulatory capital requirements if so required.

The Directors consider that the accounting policies set out in this note are the most appropriate to the Group's and the UKAR Company's circumstances, have been consistently applied to both the Group and the Company in dealing with items which are considered material and are supported by reasonable and prudent estimates and judgements.

The accounting policies have been applied to all periods presented in these Financial Statements and are consistent with the accounting policies used by the B&B Group and the NRAM Group in preparing their Interim Financial Reports for the nine months ended 30 September 2013.

B&B and NRAM are regulated by the Financial Conduct Authority ('FCA') as mortgage administration companies and the Directors believe that those companies have appropriate and adequate levels of capital to support these activities subject to the continuing support of HM Treasury.

The Financial Statements have been prepared in accordance with EU-adopted IFRS, IFRIC interpretations issued by the IFRS Interpretations Committee and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. A summary of accounting policies is set out below. The preparation of the Financial Statements in conformity with these accounting policies and generally accepted accounting principles requires the use of estimates and assumptions that affect the reported values of assets and liabilities at the date of the Financial Statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amounts, events or actions, actual results ultimately may differ from those estimates (see note 2).

The Directors consider the business to comprise one operating and geographical segment due to the similarity of risks faced within its UK-based residential, commercial and unsecured portfolios.

(c) Basis of consolidation

The UKAR Group's Financial Statements are prepared in accordance with IFRS 10 'Consolidated Financial Statements' and incorporate on a fully consolidated line-by-line basis the Financial Statements of the UKAR Company and those entities (including special purpose structures) which are controlled by UKAR (its subsidiaries); the Group Financial Statements primarily comprise the transactions and balances of the B&B Group and the NRAM Group. The UKAR Company's acquisition of the entire issued share capital of B&B and NRAM in a share-for-share exchange has been accounted for under 'predecessor accounting'. The difference between the UKAR Company's carrying value of investments and merger reserves, and the share capital and non-distributable reserves of the B&B Group and the NRAM Group, has been accounted for in the UKAR Group as a 'merger reserve'.

An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Where subsidiaries have been acquired during a period, their results are consolidated into the UKAR Group's Financial Statements from the date control is transferred to UKAR. Where subsidiaries have been disposed of, their results are consolidated to the date of disposal. On the acquisition of a business, fair values are attributed to the assets, liabilities and contingent liabilities acquired. Any difference between the consideration given and the fair value of the net assets acquired is capitalised as goodwill, which is subject to impairment testing in accordance with IAS 36 'Impairment of Assets'. Where necessary, the Group Financial Statements include adjustments to bring the financial statements of subsidiaries into alignment with the accounting policies used by the Group. All intra-group transactions and balances are eliminated on consolidation.

The UKAR Group has securitised various residential mortgage loans, generally by sale or transfer to Special Purpose Vehicles (SPV's), which in turn have issued securities to investors. The SPVs are consolidated line-by-line into the UKAR Group Financial Statements if they are, in substance, controlled by UKAR; all of the Group's SPVs are fully consolidated.

1. Principal accounting policies (continued)

(d) Interest income and expense

For all interest-bearing financial instruments except derivatives, interest income and expense are recognised in the Income Statement on an Effective Interest Rate ('EIR') basis.

The EIR method calculates the amortised cost of a financial asset or financial liability and spreads interest income or interest expense on a level yield basis over the expected life of the instrument or an appropriate shorter period. The calculation includes all directly attributable incremental fees and costs, premia on acquisition of mortgage portfolios and all other premia and discounts as well as interest. In respect of loans to customers, the elements other than interest are spread over the period to which the product reprices to a Standard or Product Variable Rate. The EIR is the rate which, at the inception of the instrument, exactly discounts expected future cash flows over the appropriate period to the initial carrying amount. When calculating the EIR, future cash flows are estimated, considering all contractual terms of the instrument (for example prepayment options) but potential future credit losses are not considered.

Interest on derivatives is included in interest income where the derivative is hedging interest income and interest expense where the derivative is hedging interest expense.

When a financial asset or a group of similar financial assets is written down as a result of an impairment loss, interest income continues to be recognised by applying the applicable EIR to the reduced balance.

(e) Fee and commission income

Where Value Added Tax ('VAT') is charged, income is stated net of VAT.

Commission receivable from the renewal of third party regulated financial services products was recognised as income within 'fee and commission income' when the renewal policy went 'on risk', net of any provision for repayment in the event of early termination by the customer. If the commission is receivable on deferred terms, a deemed interest element of the commission is separated and recognised on an EIR basis over the deferred payment period.

Fees charged to existing borrowers, including arrears and redemption fees, are recognised in fee and commission income as they arise.

(f) Bonuses payable

An accrual is made for all bonuses which have been earned by the Balance Sheet date even though these may not subsequently be payable due to clawback or the employee leaving the Group.

(g) Financial instruments

In accordance with IAS 39 each financial asset is classified at initial recognition into one of four categories:

(i) Financial assets at fair value through profit or loss;

(ii) Held-to-maturity;

(iii) Loans and receivables; or

(iv) Available-for-sale;

and each financial liability into one of two categories:

(v) Financial liabilities at fair value through profit or loss; or

(vi) Other liabilities.

Where the Directors believed it appropriate to do so, financial assets have been reclassified out of the 'available-for-sale' category to 'loans and receivables' in accordance with the revisions to IAS 39 issued by the IASB in October 2008. Such reclassifications are permitted only under certain restricted circumstances, including that there is no active market for the asset. The asset is reclassified using its fair value at the point of transfer and from that point on is accounted for on an EIR basis. The difference between the carrying value at the point of reclassification and the expected value at the redemption date is recognised in profit or loss on an EIR basis over the expected life of the asset and the asset's carrying value accretes to the redemption amount over that period, except where the asset has become impaired. The balance in the available-for-sale reserve which related to the asset is amortised to profit or loss over the expected life of the asset; in the Income Statement the amortisation of the difference between value at reclassification and at redemption and the amortisation out of the available-for-sale reserve exactly offset each other.

Measurement of financial instruments is either at amortised cost (categories (ii), (iii) and (vi) above) or at fair value (categories (i), (iv) and (v) above), depending on the category of financial instrument.

Amortised cost is the amount measured at initial recognition adjusted for subsequent principal and other payments, less cumulative amortisation calculated using the EIR method; the amortisation is taken to interest income or expense depending on whether the instrument is an asset or a liability. For assets, the amortised cost balance is reduced where appropriate by an allowance for amounts which are considered to be impaired or uncollectible.

1. Principal accounting policies (continued)

(g) Financial instruments (continued)

IFRS 13 'Fair Value Measurement' defines 'fair value' 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'. Where an active market is considered to exist, fair values are based on quoted prices or lead manager prices. For instruments which do not have active markets, fair value is calculated using discounted cash flows and applying independently sourced market parameters including interest rates and currency rates. Interest income and interest expense on instruments carried at fair value are included in the Income Statement in 'interest receivable and similar income' or 'interest expense and similar charges'. Movements in fair value are recognised in the 'unrealised fair value movements on financial instruments' line in the Income Statement except in the case of instruments categorised as 'available-for-sale', in which case the fair value movements are taken to the 'available-for-sale' reserve. On sale or derecognition of an available-for-sale instrument the accumulated fair value movements are transferred from the 'available-for-sale' reserve to the 'net realised gains less losses on investment securities' line of the Income Statement.

(h) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount is reported in the Balance Sheet only where there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

(i) Derivative financial instruments and hedge accounting

All of the Group's derivative contracts are used for commercial management of exposures to interest rate risks, foreign currency risks and risks arising from forecast transactions.

For many of the Group's derivative contracts, hedge accounting is applied. However, in some cases natural offsets apply.

Each derivative is carried at fair value on the Balance Sheet; as an asset when the fair value is positive and as a liability when the fair value is negative. The fair value of a derivative includes any interest accrued on that derivative. Changes in the fair value of derivatives are charged to the Income Statement; however, by applying the hedge accounting rules set out in IAS 39, the changes in fair value of derivatives which are used to hedge particular risks can either be mitigated in the Income Statement (fair value hedge accounting) or recognised in other comprehensive income (cash flow hedge accounting). The Group has adopted cash flow hedge accounting and fair value hedge accounting.

(i) Cash flow hedge accounting

A cash flow hedge is used to hedge exposures to variability in cash flows such as variable rate financial assets and liabilities. The effective portion of changes in the derivative fair value is recognised in other comprehensive income and recycled to the Income Statement in the periods when the hedged item will affect profit and loss. The fair value gain or loss relating to the ineffective portion is recognised immediately in the Income Statement.

(ii) Fair value hedge accounting

A fair value hedge is used to hedge exposures to variability in the fair value of financial assets and liabilities such as fixed rate loans. Changes in 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 Group uses fair value hedge accounting on one-to-one relationship and portfolio hedging bases as described below.

Where hedge accounting is not applied, changes in fair values are recognised immediately in the Income Statement.

(iii) One-to-one fair value hedges

Where one or more specific derivative financial instruments hedge the changes in fair value of a specific asset or liability, provided that the hedge arrangement meets the requirements of IAS 39 to be classed as 'highly effective', the associated hedged item is carried on the Balance Sheet at fair value in respect of the hedged risk. Fair value gains and losses are recognised in the Income Statement, mitigating the fair value movements on the associated derivative financial instruments. The Income Statement immediately recognises any hedge accounting 'ineffectiveness'; that is any difference between the fair value movement on the hedging instrument and that on the hedged item.

(iv) Portfolio fair value hedges

Where a group of derivative financial instruments hedges the interest rate exposure of a group of assets or liabilities and the hedge meets the requirements of IAS 39 to be classed as 'highly effective', the hedge relationship is accounted for in the same way as a one-to-one fair value hedge except that the Balance Sheet carrying value of the hedged items is not adjusted; instead, the difference between the carrying value and the fair value in respect of the hedged risk is carried on the Balance Sheet in 'fair value adjustments on portfolio hedging'.

(v) Hedge effectiveness

At the inception of each hedging arrangement the relationship between the hedging instruments and the hedged items is documented, as well as the risk management objective and strategy. Also documented is an assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in the hedging arrangement are 'highly effective' in offsetting changes in fair values or cash flows of the hedged items. Under IAS 39 a hedge is deemed to be 'highly effective' if effectiveness is forecast to fall, and is actually found to fall, within the 80% to 125% range. Any hedge relationship falling outside these limits is deemed to be ineffective and hedge accounting is discontinued.

(vi) Termination of hedges

Where a hedge relationship is terminated or deemed not to be highly effective (other than as a result of the hedged item being derecognised from the Balance Sheet due to sale or other reason), the adjustment relating to the terminated hedge relationship is amortised to the Income Statement over the period that the hedged item affects profit and loss.

1. Principal accounting policies (continued)

(i) Derivative financial instruments and hedge accounting (continued)

(vii) Embedded derivatives

Certain financial instruments have derivative features embedded within them. Where the economic characteristics and risks of the embedded derivative are not closely related to those of the host instrument and where changes in fair value of the host instrument are not reflected in the Income Statement, the embedded derivative is separated from the host and carried on the Balance Sheet at fair value with gains and losses on the embedded derivative being recognised in the Income Statement. In accordance with IFRIC 9 'Reassessment of Embedded Derivatives' the decision as to whether to separate and value an embedded derivative is reassessed when and only when the terms of the host contract are significantly modified.

(j) Sale and repurchase agreements

Securities sold subject to repurchase agreements ('repos') continue to be reported as they were originally classified within the Group's Balance Sheet as the risks and rewards associated with that asset remain with the Group. The counterparty liability is included in 'amounts due to banks' or 'other deposits'. Securities purchased under agreements to resell ('reverse repos') are recorded as 'cash at bank and in hand'. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the EIR method.

(k) Impairment losses

Financial assets which are not held at fair value through profit or loss are reviewed for indications of possible impairment throughout the year and at each published Balance Sheet date. An impairment loss is recognised if, and only if, there is objective evidence that a loss event (or events) has occurred after initial recognition and before the Balance Sheet date and has a reliably measurable impact on the estimated future cash flows of the financial asset or group of financial assets. Losses that are incurred as a result of events occurring after the Balance Sheet date are not recognised.

(i) Financial assets held at amortised cost

For each asset, an assessment is made as to whether an impairment provision should be made on either an individual or a collective basis. Assets where an individual impairment assessment is made include all loans in possession or held for sale with a Law of Property Act ('LPA') receiver and others which management consider to be individually impaired, for example where a fraud has been uncovered. The carrying value of the asset at the Balance Sheet date is reduced by applying an impairment allowance to the net present value of the expected future cash flows associated with the asset, calculated at the asset's original EIR. These cash flows include, where appropriate, estimated amounts recoverable by possession and sale of a secured property taking into account a discount on property value to reflect a forced sale.

All assets that have been assessed as having no individual impairment are then collectively assessed for impairment, grouped by assets with similar characteristics. Assessment is made of impairment arising due to events which are believed to have occurred by the Balance Sheet date but have not yet been reported, taking into account the economic climate in the market. This collective impairment is reflected by reducing the carrying value by applying an impairment allowance.

Impairment of assets is charged in the Income Statement in the 'impairment on loans to customers' and 'net impairment on investment securities' lines.

For impaired loans to customers, interest is accrued for accounting purposes on the loan amount after any impairment adjustments in accordance with IAS 39, using the original EIR of the loan. However, for the purposes of the amount legally due from the borrower, interest continues to accrue on the full outstanding balance and it is this full balance plus full interest which is pursued for collection.

A loan to a customer is written off and any associated impairment allowance released when, and only when, the property is sold, the account is redeemed, or in respect of unsecured loans where the collections process indicates a loan is not recoverable. Any subsequent proceeds are recognised on a cash basis and offset against 'impairment on loans to customers' in the Income Statement. An investment security is written off and any associated impairment allowance released when there is strong evidence to suggest nothing will be recovered.

Where a property has been taken into possession or an LPA receiver has been appointed to collect rental income on the property, the loan continues to be carried within 'loans to customers'.

(ii) Available-for-sale financial assets

Investment securities classified as available-for-sale are carried at fair value which appropriately reflects any impairment. Impairment is recognised when the investment security exhibits objective evidence of impairment or is uncollectible. Such evidence may include:

- Significant financial difficulty;
- Payment defaults;
- Renegotiation of terms due to borrower difficulty;
- Sustained fall in credit rating or creditworthiness;
- Significant restructuring;
- Disappearance of an active market;
- Significant and sustained fall in market price; or
- Observable data indicating measurable decrease in the estimated future cash flows from a group of financial assets, although the decrease cannot yet be identified within individual assets in the group.

1. Principal accounting policies (continued)

(k) Impairment losses (continued)

Movements in the fair value which are a reflection of impairment of the long term value of the investment security are charged to 'net impairment on investment securities' in the Income Statement. Investment impairment losses recognised against investment securities are reversed through 'net impairment on investment securities' in the Income Statement if the improvement relates to an event occurring after the initial impairment was recognised. An investment security is written off and any associated impairment allowance released when there is strong evidence to suggest nothing will be recovered.

If there is a sustained increase in the fair value of an investment security where an impairment loss has previously been recognised but no improvement can be attributed to a subsequent credit event, then the increase in value may be treated as a revaluation and recognised through other comprehensive income in the available-for-sale reserve.

(l) Recognition and derecognition of financial instruments

Purchases and sales of mortgage portfolios are accounted for on the completion date. All other purchases and sales of financial assets are accounted for on the date of commitment to buy or sell (the 'trade date').

A financial asset is derecognised (ie removed from the Balance Sheet) only when substantially all of the risks and rewards associated with that asset have been transferred to another party.

A financial liability is derecognised only when the contractual obligation is discharged, cancelled or has expired.

(m) Debt and equity securities in issue

Issued securities, including capital instruments, are classified as liabilities where the contractual arrangements result in the issuing company having an obligation to deliver either cash or another financial asset to the security holder, or to exchange financial instruments under conditions that are potentially unfavourable to the company. Issued securities are classified as equity where they meet the definition of equity and confer a residual interest in the company's assets on the holder of the securities. Issued securities include ordinary and preference share capital. Preference shares are classified as equity instruments where dividend payments and redemptions are discretionary.

On initial recognition, debt issued is measured at its fair value net of directly attributable issue and transaction costs. Subsequent measurement is at amortised cost using the EIR method to amortise attributable issue and transaction costs, premia and discounts over the life of the instrument. These costs are charged along with interest on the debt to 'interest expense and similar charges'. Unamortised amounts are added to or deducted from the carrying value of the instrument.

Equity instruments (including share capital) are initially recognised at net proceeds after deducting transaction costs and any related income tax.

(n) Foreign currencies

The presentation and functional currency of the Company and the presentational currency of the Group is pounds sterling.

Transactions which are not denominated in pounds sterling are translated into sterling at the spot rate of exchange on the date of the transaction or the contracted rate. Monetary assets and liabilities which are not denominated in pounds sterling are translated into pounds sterling at the closing rate of exchange at the Balance Sheet date.

Foreign exchange gains and losses resulting from the restatement and settlement of such transactions are recognised in the Income Statement.

(o) Intangible assets

Intangible assets comprise capitalised computer software systems and licences. Purchased computer software licences are capitalised as intangible assets where it is probable that future benefits will flow to the Group. Thereafter they are carried at cost less accumulated amortisation. Amortisation is provided on a straight line basis over their useful economic lives which may be up to five years. Those which have a life expectancy at the outset of less than two years are not capitalised but instead their costs are charged to the Income Statement as they arise.

Costs that are directly associated with developing identifiable computer software systems are capitalised if the criteria in IAS 38 'Intangible Assets' are satisfied; the main criteria are that the successful completion of the development project is reasonably certain and that the software is expected to generate future economic benefits. Each item of capitalised developed computer software is carried at cost less accumulated amortisation; amortisation is provided on a straight line basis over its estimated useful life. Costs that do not qualify for capitalisation or are associated with maintaining software are charged to the Income Statement as they arise.

Intangible assets in the course of construction are not amortised until they have been completed. The costs of financing intangible assets in the course of construction are not included in the costs of the assets. Intangible assets in the course of construction are included in the impairment test referred to below where appropriate.

All items of intangible assets are reviewed at each published Balance Sheet date for any indication of impairment. If there is indication of impairment, the carrying value is reviewed. If any impairment is identified, the asset is written down to the impaired value, being the higher of value in use and estimated net proceeds of sale with the impairment being charged immediately to the Income Statement. In addition, the estimated useful lives are also reassessed annually and if they are judged to have changed then the rate of amortisation charged in periods after the date of the change reflects the revised estimates.

1. Principal accounting policies (continued)

(p) Cash and cash equivalents

Cash and cash equivalents comprise balances which are highly liquid and have an original maturity of three months or less.

(q) Taxation

(i) Current tax

The charge for taxation is based on the result for the period and takes into account taxation deferred or accelerated arising from temporary differences between the carrying amounts of certain items for taxation and for accounting purposes. Tax relating to items which are taken directly to reserves is also taken directly to reserves.

(ii) Deferred tax

Deferred tax is calculated using the liability method on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Financial Statements. Deferred tax is determined using tax rates and laws that have been enacted or substantively enacted by the Balance Sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled. The principal temporary differences arise from depreciation of property, plant and equipment, revaluation of certain financial assets and liabilities including derivative contracts, provisions for pensions and other post-retirement benefits, tax losses carried forward and changes in accounting basis on adoption of IFRS.

Deferred tax assets are recognised when it is probable that future taxable profits will be available against which these temporary differences can be utilised.

Deferred tax is provided on temporary differences arising from investments in subsidiaries and associates, except 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 related to fair value remeasurement of available-for-sale investments and cash flow hedges which are recognised in other comprehensive income, is also recognised in other comprehensive income and subsequently, in the consolidated Income Statement together with the associated gain or loss.

(r) Retirement benefits

The Group operates a number of retirement benefit plans for its current and former employees including defined contribution pension plans, defined benefit pension plans and post-retirement healthcare benefits. The costs of these plans are charged to the 'administrative expenses' line of the Income Statement and other comprehensive income in accordance with IAS 19 'Employee Benefits'. During the period, the Group has adopted the revisions to IAS 19 which were issued in June 2011 and adopted for use in the EU in June 2012. The main effect on the Group of these revisions to IAS 19 is that, instead of an expected rate of return being applied to defined benefit plan assets, the discount rate previously applied to defined benefit plan obligations is instead applied to the net surplus or deficit on the plan.

A defined contribution pension plan is an arrangement where the employer pays specified contributions into a fund. The contributions are charged to the Income Statement when employees render the related services, which is generally in the period of contribution.

A defined benefit pension plan is an arrangement that defines an amount of pension benefit that an employee will receive during retirement, usually dependent on one or more factors such as age, years of service and salary. As at 31 March 2014 and 31 December 2012 the B&B defined benefit pension scheme was in deficit. The NRAM defined benefit pension scheme was in surplus on an accounting basis but in deficit on a trustee's funding basis. As these are separate schemes, a surplus on one scheme cannot be offset against a deficit on the other.

Full actuarial valuations of the Group's defined benefit sections of the pension schemes are undertaken every three years, with interim reviews in the intervening years; these valuations are updated at each published balance sheet date by qualified independent actuaries. For the purpose of these updates, scheme assets are included at their fair value and scheme liabilities are measured on an actuarial basis using the projected unit credit method. Details of the actuarial assumptions made are provided in note 18. The resulting net surplus or deficit on each scheme is included in full in the Balance Sheet. Retirement benefit remeasurements are charged to retained earnings in full in the period in which they occur and pass through other comprehensive income rather than the Income Statement. The Income Statement includes, for each scheme, the current service cost of providing pension benefits, the expected return on the scheme's assets net of administration costs and the interest cost on the scheme's liabilities. The current service cost is nil as the schemes are closed to future service accruals.

In B&B, post-retirement healthcare benefits are accounted for in the same way as defined benefit pension benefits, with the present value of the defined benefit obligation being carried as a liability on the Balance Sheet. NRAM does not provide post-retirement healthcare benefits.

(s) Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and provision for impairment as appropriate. Additions and subsequent expenditure are included in the asset's carrying value or are recognised as a separate asset only when they improve the expected future economic benefits to be derived from the asset. All other expenditure is regarded as repairs and maintenance and is charged to the Income Statement in the period in which it is incurred. Depreciation is provided so as to write off the cost less the estimated residual value of each significant component of each item of property, plant and equipment over that component's estimated useful life, as follows:

- Freehold land is not depreciated
- Freehold and leasehold buildings 6.7% pa on a straight line basis
- Motor vehicles 25% pa on a reducing balance basis
- Computer equipment 20% – 33% pa on a straight line basis
- Fixtures and fittings 20% pa on a straight line basis
- Other plant and equipment and major alterations to buildings 10% pa on a straight line basis or over the remaining life of the building if shorter.

1. Principal accounting policies (continued)

(s) Property, plant and equipment (continued)

All items of property, plant and equipment are reviewed at each published Balance Sheet date for any indication of impairment. If there is indication of impairment, the carrying value is reviewed. If any impairment is identified the asset is written down to the higher of value in use and estimated net proceeds of sale, with the impairment being charged immediately in the Income Statement. In addition, the estimated useful lives and estimated residual values are also reassessed annually and if they are judged to have changed then the rate of depreciation charged in periods after the date of the change reflects the revised estimates.

Where a property ceases to be occupied by a Group company and it is not intended to re-occupy the property or to sell it in the ordinary course of business, the property is reclassified as an investment property and is carried at fair value. Any shortfall between the carrying amount of the property and its fair value at the date of reclassification is charged to the Income Statement. Any surplus between the carrying amount of the property and its fair value at the date of reclassification is credited directly to other comprehensive income except to the extent that the increase reverses a previous impairment loss for that property, in which case the increase is recognised in the Income Statement.

Assets in the course of construction are not depreciated until they have been completed and transferred to the appropriate category of property, plant and equipment. The costs of financing assets in the course of construction are not included in the costs of the assets. Assets in the course of construction are included within the impairment test referred to above where appropriate.

A previously recognised impairment charge on an asset may be reversed in full or in part where a change in circumstances leads to a change in the estimates used to determine its recoverable amount. The carrying value of the asset will not be increased above the carrying value at which it would have been held had the impairment not been recognised.

(t) Investment property

Investment properties represent properties held as investments to earn rentals or for capital appreciation, or both. Investment properties are included in the Balance Sheet at fair value with changes recognised in the Income Statement in the period of change. Fair values are determined by independent professional valuers by application of recognised valuation techniques.

(u) Leases

Rentals under operating leases are charged to ‘administrative expenses’ on a straight line basis to the date of change in the rental amount. Typically operating leases have rent review dates in their terms which are several years apart and between those dates the annual rent remains constant. Any initial rent-free period and any lease premia paid are amortised over the full lease period on a straight line basis.

If a lease agreement in which the Group is a lessee transfers the risks and rewards of the asset, the lease is recorded as a finance lease and the related asset is capitalised. At inception the asset is recorded at the lower of the present value of the minimum lease payments and fair value, and is depreciated over the shorter of the estimated useful life and the term of the lease. The lease obligations are recorded as borrowings. If the lease does not transfer the risks and rewards of the asset, the lease is recorded as an operating lease.

Where an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor in compensation is charged to the Income Statement in the period in which termination is made.

Where the Group leases assets out under an operating lease agreement, the asset is included in the Balance Sheet based on the nature of the asset. Lease income is recognised over the term of the lease on a straight line basis.

(v) Provisions and contingent liabilities

Provisions are recognised when, and only when, the following criteria are all met:

- there is a present obligation (legal or constructive) as a result of a past event;
- it is probable that an outflow of resources will be required to settle the obligation; and
- a reliable estimate can be made of the amount of the obligation.

Provisions are reviewed at each Balance Sheet date and are released if they no longer meet the above criteria.

Provisions are discounted to net present value, using rates which reflect the risks specific to the provision, if the effect of discounting is material.

Contingent liabilities are possible obligations whose existence depends upon the outcome of uncertain future events or are present obligations where the outflows of resources are uncertain or cannot be reliably measured. Contingent liabilities are not recognised in the Balance Sheet but are disclosed unless they are remote.

(w) Investment securities held

Investment securities intended for use on a continuing basis in the Group’s activities are categorised either as ‘available-for-sale’ or as ‘loans and receivables’; for each instrument, the Directors adopt the category which they consider to be the most appropriate.

Investment securities categorised as available-for-sale are carried at fair value with movements in fair value, excluding impairment provisions, being taken to the available-for-sale reserve. If an investment security which has been categorised as available-for-sale becomes impaired, the impairment is charged to the Income Statement in the ‘net impairment on investment securities’ line.

Investment securities categorised as loans and receivables are carried at amortised cost less any impairment, with any impairment being charged to the Income Statement in the ‘net impairment on investment securities’ line.

Where the Directors believe it appropriate to do so, investment securities which were initially categorised as ‘at fair value through profit or loss’ or ‘available-for-sale’ have subsequently been re-categorised to ‘loans and receivables’ in accordance with the revisions to IAS 39 issued by the IASB in October 2008.

1. Principal accounting policies (continued)

(x) Financial guarantees

The Group applies insurance accounting to financial guarantee contracts and provides against any claims arising under such contracts.

(y) Loan commitments

Loan commitments are disclosed but are accounted for only if there is an onerous commitment; there were no onerous loan commitments in the period or previous year. The commitment ceases to be disclosed once it is advanced or expires. Loan commitments comprise commitments to advance cash sums, and to allow drawdown of monies previously overpaid (where the terms of the loan specifically allow). In respect of lifetime monthly drawdown products the commitment reflects an estimate of the future drawdowns to redemption.

2. Critical judgements and accounting estimates

In preparing the Financial Statements, management are required to make a series of judgements and estimates. Judgements involve an interpretation of requirements to decide how to allocate, value or recognise an item. Estimates arise from using assumptions which result in a range of possible outcomes. The most important judgements and estimates used in preparing these Financial Statements are described below.

(a) Qualifying hedge relationships

In designating a financial instrument as part of a qualifying hedge relationship the Group has determined that the hedge is expected to be highly effective over the life of the hedging instrument. In accounting for a derivative as a cash flow hedge the Group has determined that the hedged cash flow exposure relates to highly probable future cash flows.

(b) Impairment of investment securities

For investment securities carried at fair value, judgement is applied in determining whether any fall in value represents impairment, and whether any increase represents a reversal of impairment. Factors considered in determining whether an asset is impaired, or impairment has reversed, are detailed in note 1(k).

(c) Impairment losses on loans

The Group reviews its loan impairment on a monthly basis and assesses individual impairment losses by reference to an individual review of the underlying asset and utilises actual loss experience to provide both probabilities of defaults and property forced sale discounts across a portfolio of products. Collective impairment losses on loans are calculated using a statistical model. The key assumptions used in this model are: the probability of any balance entering into default as a result of an event that had occurred prior to the Balance Sheet date; the probability of this default resulting in possession or write-off; and the estimated subsequent loss incurred. These key assumptions are based on observed data trends and are updated on a regular basis within agreed methodology to ensure the impairment allowance is entirely representative of the current portfolio. The accuracy of the impairment calculation would, therefore, be affected by unanticipated changes to the economic situation and assumptions which differ from actual outcomes. To the extent that house prices were to change by +/ – 10%, the residential impairment allowance would be an estimated £108.7m lower (2012: £174.3m) or £115.5m higher (2012: £184.1m) respectively.

(d) Provisions

Provisions are carried in respect of certain known or forecast future expenditure, as described in note 26. Where the future payment amount is unknown, provisions are set at a level which covers the estimated number of future payments and the estimated average payment amount. Provisions are calculated using the best available information, but the actual future outcomes of items provided for may differ from expectations.

(e) Fair value calculations

For the majority of instruments carried at fair value, fair value is determined by reference to quoted market prices or lead manager prices. Where these are not available, fair value is calculated using discounted cash flows, applying independently sourced market parameters including interest rates and currency rates. Other factors are also considered, such as counterparty credit quality and liquidity. Management must use judgement to arrive at estimates where not all necessary data can be externally sourced or where factors specific to the Group's holdings need to be considered. The accuracy of the fair value calculations may, therefore, be affected by unexpected market movements, or variations in actual outcomes when compared to estimates and assumptions used for modelling purposes. For example, if management were to use a tightening in the credit spread of 10 basis points, the fair value of derivatives would decrease from the reported fair values by £9.4m (2012: £20.8m).

3. Net interest income

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Interest receivable and similar income		
On secured loans	**2,714.9**	2,426.2
On other lending	**89.6**	111.2
On investment securities and deposits	**80.0**	86.6
Total interest receivable and similar income	**2,884.5**	2,624.0
Interest expense and similar charges		
On amounts due to banks and HM Treasury	**(741.9)**	(676.2)
State guarantee fee*	**(46.9)**	(47.4)
On debt securities and other	**(265.1)**	(415.5)
Total interest expense and similar charges	**(1,053.9)**	(1,139.1)
Net interest income	**1,830.6**	1,484.9
Average balances		
Interest-earning assets ('IEA')	**75,489**	84,117
Financed by:		
– interest-bearing funding	**50,805**	59,769
– interest-free funding**	**24,684**	24,348
Average rates:	**%**	%
– gross yield on IEA	**3.07**	3.12
– cost of interest-bearing funding	**(1.66)**	(1.83)
Interest spread	**1.41**	1.29
State guarantee fee*	**(0.05)**	(0.06)
Contribution of interest-free funding**	**0.59**	0.54
Net interest margin on average IEA	**1.95**	1.77
Average Bank Base Rate	**0.50**	0.50
Average 1-month LIBOR	**0.49**	0.62
Average 3-month LIBOR	**0.51**	0.83

* At the time of the nationalisation of B&B, HM Treasury provided guarantees with regard to certain wholesale borrowings and derivative transactions existing at that time. The amount of this fee is dependent on balances outstanding, and hence it is included within 'interest expense and similar charges'. At the time of the nationalisation of NRAM, HM Treasury provided a guarantee with regard to certain wholesale borrowings and derivative transactions existing at that time. The amount of this fee is currently £12m pa, and is not dependent on balances outstanding, and hence it is included within 'fee and commission expense'.

** Interest-free funding is calculated as an average over the financial period and includes the Statutory Debt and share capital and reserves.

Total interest receivable and similar income includes interest accrued on individually impaired assets of £37.4m (2012: £30.4m).

4. Net gains on financial instruments designated at fair value

The gains of £17.5m in 2012 arose on the disposal of assets which had previously been held at a fair value of £nil on the Balance Sheet.

5. Net realised gains less losses on investment securities

Net realised gains less losses on investment securities recognised in the Income Statement comprised the following:

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Net realised gains on available-for-sale instruments	**11.6**	1.4
Net realised losses on instruments at amortised cost	**(24.1)**	(16.3)
Total net realised losses on investment securities	**(12.5)**	(14.9)

6. Unrealised fair value movements on financial instruments and hedge ineffectiveness

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Net (loss)/gain in fair value:		
– translation losses on underlying instruments	(38.8)	(291.9)
– fair value movements on derivatives which are economic hedges but are not in hedge accounting relationships	9.2	249.1
Unrealised fair value movements	(29.6)	(42.8)
Net gains on fair value hedging instruments	180.4	110.0
Net losses on fair value hedged items attributable to hedged risk	(197.7)	(118.4)
Ineffectiveness on cash flow hedges	(10.3)	(20.0)
Net hedge ineffectiveness losses	(27.6)	(28.4)
Total	(57.2)	(71.2)

7. Administrative expenses

Certain employees of B&B provide services to NRAM and to UKARcs, and the staff numbers below show B&B's employees split by which company they provide services to. NRAM and UKARcs had no direct employees during the periods presented.

The monthly average number of persons employed by UKAR Group companies during the period was as follows:

	15 months to 31 Mar 2014 Number	12 months to 31 Dec 2012 Number
Average headcount:		
Full time	1,830	1,923
Part time	418	501
Total employed	2,248	2,424
Providing services to NRAM:		
Full time	862	1,017
Part time	255	342
Total providing services to NRAM	1,117	1,359
Providing services to B&B:		
Full time	965	906
Part time	163	159
Total providing services to B&B	1,128	1,065
Providing services to UKARcs:		
Full time	3	-
Part time	-	-
Total providing services to UKARcs	3	-
Total average full time equivalent	2,111	2,249
Total average full time equivalent providing services to NRAM	1,029	1,234
Total average full time equivalent providing services to B&B	1,079	1,015
Total average full time equivalent providing services to UKARcs	3	-

The full time equivalent is based on the average hours worked by employees in the period.

7. Administrative expenses (continued)

The number of persons employed by UKAR Group companies at the end of the period was as follows:

	31 Mar 2014 Number	31 Dec 2012 Number
Full time	**1,741**	1,965
Part time	**401**	471
Total employed	**2,142**	2,436
Providing services to NRAM:		
Full time	**788**	839
Part time	**236**	319
Total providing services to NRAM	**1,024**	1,158
Providing services to B&B:		
Full time	**941**	1,126
Part time	**165**	152
Total providing services to B&B	**1,106**	1,278
Providing services to UKARcs:		
Full time	**12**	-
Part time	**-**	-
Total providing services to UKARcs	**12**	-
Total full time equivalent headcount	**2,014**	2,277
Total full time equivalent headcount providing services to NRAM	**945**	1,046
Total full time equivalent headcount providing services to B&B	**1,057**	1,231
Total full time equivalent headcount providing services to UKARcs	**12**	-

Staff numbers include Executive but not Non-Executive Directors.

In addition to the permanent staff above, the Group employed a full time equivalent of 334 temporary staff and specialist contractors at 31 March 2014 (31 December 2012: 346).

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
The Group's aggregate costs of permanent staff were as follows:		
Wages and salaries	**71.3**	65.0
Social security costs	**7.4**	6.6
Defined benefit pension costs (see note 18)	**(0.8)**	0.6
Defined contribution pension costs (see note 18)	**4.2**	3.4
Other retirement benefit costs (see note 18)	**0.6**	0.5
Total staff costs	**82.7**	76.1
IT costs	**63.0**	56.0
Outsourced and professional services	**30.4**	25.5
Depreciation and amortisation (see notes 20 and 21)	**19.4**	12.6
Other administrative expenses	**50.8**	37.1
Ongoing administrative expenses	**246.3**	207.3
Other net administrative expenses:		
– transformation costs	**-**	51.4
– accelerated depreciation (see note 20)	**-**	8.3
Total other net administrative expenses	**-**	59.7
Total administrative expenses	**246.3**	267.0

Transformation costs of £51.4m in 2012 mainly related to the change of primary IT service provider, and redundancy costs and write-downs of assets following the announcement of the UKAR restructure and the phased exit from the Gosforth site.

7. Administrative expenses (continued)

Services provided by the Group's auditors and network firms

During the period the Group obtained services from the Group's auditors, as detailed below:

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Fees payable to Company auditor for the audit of the UKAR Company and Group Financial Statements	**0.1**	**0.1**
Fees payable to Company auditor and its associates for other services:		
– the audit of the Company's subsidiaries pursuant to legislation	**0.6**	**0.5**
– audit-related assurance services	**0.3**	**0.1**
Total	**1.0**	**0.7**

Amounts shown in the above analysis are exclusive of VAT.

8. Gain on repurchase of own liabilities and equity

15 months to 31 Mar 2014	Reserve capital instruments £m	Total gains taken to reserves £m	Tier one notes £m	Subordinated liabilities £m	Securitised notes £m	Total Income Statement gains £m
Principal amount of instruments repurchased	**-**	**-**	**-**	**5.3**	**-**	**5.3**
Amount paid to repurchase instruments	**-**	**-**	**-**	**(3.2)**	**-**	**(3.2)**
Other net gains resulting from the repurchase*	**-**	**-**	**-**	**0.8**	**-**	**0.8**
Gain on repurchase of own liabilities	**-**	**-**	**-**	**2.9**	**-**	**2.9**

12 months to 31 Dec 2012	Reserve capital instruments £m	Total gains taken to reserves £m	Tier one notes £m	Subordinated liabilities £m	Securitised notes £m	Total Income Statement gains £m
Principal amount of instruments repurchased	0.9	0.9	0.2	0.2	537.2	537.6
Amount paid to repurchase instruments	(0.5)	(0.5)	(0.1)	(0.1)	(391.6)	(391.8)
Other net losses resulting from the repurchase*	(0.1)	(0.1)	(0.1)	-	(2.2)	(2.3)
Gain on repurchase of own liabilities and equity	0.3	0.3	-	0.1	143.4	143.5

* The other net gains and losses were principally release of deferred coupons and hedge adjustments, less accelerated amortisation of the discounting effect of deferral of coupons and fees.

During 2012, the gain on repurchase of reserve capital instruments was reported in reserves as these instruments were accounted for as equity; after tax of £0.1m the net gain taken to reserves was £0.2m. The gain on repurchase of tier one notes, subordinated liabilities and securitised notes was reported in the Income Statement as these instruments were accounted for as liabilities.

9. Taxation

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
The tax charge for the period comprises:		
Current tax:		
– on profit for the period	**(291.3)**	(121.6)
– adjustments in respect of prior periods	**19.1**	12.1
Total current tax	**(272.2)**	(109.5)
Deferred tax (see note 16):		
– origination and reversal of temporary differences	**(36.9)**	(28.5)
– change in rate on deferred tax items	**0.8**	11.3
Total deferred tax	**(36.1)**	(17.2)
Total taxation charge per the Income Statement	**(308.3)**	(126.7)

The following tax amounts have been (charged)/credited to equity:

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Current tax:		
– relating to available-for-sale investments	**(15.8)**	(15.6)
– relating to repurchase of equity (see note 8)	**-**	(0.1)
Deferred tax:		
– relating to cash flow hedge reserve	**29.9**	(45.4)
– relating to retirement benefit remeasurements	**1.0**	19.6
– relating to available-for-sale investments	**(1.7)**	(1.7)
Net credit/(charge) to equity	**13.4**	(43.2)

There was no foreign tax charged in the period (2012: £nil).

The tax charge on the Group's profit before tax differs from the theoretical amount that would arise using the standard weighted average rate of UK corporation tax of 23.2% (2012: 24.5%) as follows:

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Profit before taxation	**1,374.3**	690.5
Tax calculated at rate of 23.2% (2012: 24.5%)	**(318.8)**	(169.2)
Effects of:		
– change in rate on deferred tax items	**0.8**	11.3
– expenses not deductible for tax purposes	**(7.4)**	(7.7)
– adjustments in respect of prior years	**17.1**	38.9
Total taxation charge for the period	**(308.3)**	(126.7)

Taxation appropriately reflects changes in tax rates which had been substantively enacted by the Balance Sheet date, as detailed in note 16.

10. Balances with the Bank of England

	31 Mar 2014 £m	31 Dec 2012 £m
Balances for liquidity purposes	**3,213.5**	2,995.2
Collateral balances	**1,806.8**	2,604.6
Total	**5,020.3**	5,599.8

Balances with the Bank of England represent cash liquidity and collateral held on account which earn Bank Base Rate.

11. Investment securities

	31 Mar 2014 £m	31 Dec 2012 £m
Available-for-sale securities	**321.3**	635.5
Investment securities held as loans and receivables	**679.4**	1,195.0
Unsecured investment loans	**74.0**	219.4
Total	**1,074.7**	2,049.9

In the Balance Sheet the carrying values of impaired assets are presented net of the impairment allowances shown in note 12.

Net impairment on investment securities for the period comprised:

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Net impairment reversals on available-for-sale securities	**14.0**	45.4
Net impairment reversals/(losses) on investment securities held as loans and receivables and unsecured investment loans	**3.7**	(15.2)
Total net impairment reversals	**17.7**	30.2

(a) Available-for-sale securities

	31 Mar 2014 £m	31 Dec 2012 £m
At fair value:		
Listed	**303.1**	542.6
Unlisted	**18.2**	92.9
Total	**321.3**	635.5

The movement in available-for-sale securities was as follows:

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
At start of period	**635.5**	970.4
Additions	**-**	104.3
Disposals (sales and redemptions)	**(327.3)**	(459.8)
Exchange differences	**3.2**	(10.9)
Net gains on changes in fair value	**9.9**	31.5
At end of period	**321.3**	635.5

(b) Investment securities held as loans and receivables

	31 Mar 2014 £m	31 Dec 2012 £m
Carrying value	**679.4**	1,195.0
Fair value	**688.7**	1,182.1
Listed	**668.0**	1,175.9
Unlisted	**11.4**	19.1
Total	**679.4**	1,195.0

11. Investment securities (continued)

(c) Unsecured investment loans

	31 Mar 2014 £m	31 Dec 2012 £m
Carrying value	**74.0**	219.4
Fair value	**85.1**	189.7
Listed	**74.0**	219.4
Total	**74.0**	219.4

12. Wholesale assets

The assets in the following table are of a wholesale nature as opposed to individual customer assets. The credit and concentration risk characteristics of these portfolios should, therefore, be considered together.

	31 Mar 2014 £m	31 Dec 2012 £m
Balances with the Bank of England (see note 10)	**5,020.3**	5,599.8
Cash at bank and in hand	**2,503.2**	4,129.2
Investment securities (see note 11)	**1,074.7**	2,049.9
Total	**8,598.2**	11,778.9

The Group had no collateral or other credit enhancements in respect of these assets.

(a) Credit risk

The credit quality of wholesale assets is set out in the table below:

At 31 March 2014	Balances with the Bank of England £m	Cash at bank and in hand £m	Available-for-sale securities £m	Investment securities held as loans and receivables £m	Unsecured investment loans £m	Total £m
Neither past due nor impaired	**5,020.3**	**2,503.2**	**181.6**	**661.1**	**-**	**8,366.2**
Impaired	**-**	**-**	**374.1**	**85.1**	**216.9**	**676.1**
	5,020.3	**2,503.2**	**555.7**	**746.2**	**216.9**	**9,042.3**
Provisions	**-**	**-**	**(234.4)**	**(66.8)**	**(142.9)**	**(444.1)**
Total	**5,020.3**	**2,503.2**	**321.3**	**679.4**	**74.0**	**8,598.2**

At 31 December 2012	Balances with the Bank of England £m	Cash at bank and in hand £m	Available-for-sale securities £m	Investment securities held as loans and receivables £m	Unsecured investment loans £m	Total £m
Neither past due nor impaired	5,599.8	4,129.2	467.5	1,109.5	219.4	11,525.4
Impaired	-	-	495.2	185.4	239.6	920.2
	5,599.8	4,129.2	962.7	1,294.9	459.0	12,445.6
Provisions	-	-	(327.2)	(99.9)	(239.6)	(666.7)
Total	5,599.8	4,129.2	635.5	1,195.0	219.4	11,778.9

12. Wholesale assets (continued)

The credit quality of wholesale assets by reference to credit ratings is set out in the table below:

At 31 March 2014	£m	AAA %	AA %	A %	BBB to B %	CCC and below %
Balances with the Bank of England	5,020.3	100	-	-	-	-
Cash at bank and in hand	2,503.2	13	52	28	7	-
Investment securities:						
– available-for-sale securities	321.3	42	1	27	4	26
– investment securities held as loans and receivables	679.4	3	23	31	32	11
– unsecured investment loans	74.0	-	-	-	-	100
Total investment securities	1,074.7	15	16	30	23	16
Total	**8,598.2**	**64**	**17**	**12**	**5**	**2**

At 31 December 2012	£m	AAA %	AA %	A %	BBB to B %	CCC and below %
Balances with the Bank of England	5,599.8	100	-	-	-	-
Cash at bank and in hand	4,129.2	13	48	34	1	4
Investment securities:						
– available-for-sale securities	635.5	49	5	25	2	19
– investment securities held as loans and receivables	1,195.0	1	25	39	30	5
– unsecured investment loans	219.4	-	-	-	100	-
Total investment securities	2,049.9	16	16	30	29	9
Total	11,778.9	55	20	17	5	3

Additional information in respect of impairment of investment securities is provided in note 11.

(b) Concentration risk

Wholesale assets are analysed by geographical region at their carrying amounts in the table below:

At 31 March 2014	UK £m	Europe £m	US £m	Other countries £m	Total £m
Balances with the Bank of England	5,020.3	-	-	-	5,020.3
Cash at bank and in hand	1,809.8	520.3	173.1	-	2,503.2
Investment securities:					
– available-for-sale securities	70.5	202.6	7.7	40.5	321.3
– investment securities held as loans and receivables	269.7	36.2	11.4	362.1	679.4
– unsecured investment loans	-	-	-	74.0	74.0
Total investment securities	340.2	238.8	19.1	476.6	1,074.7
Total	**7,170.3**	**759.1**	**192.2**	**476.6**	**8,598.2**

12. Wholesale assets (continued)

At 31 December 2012	UK £m	Europe £m	US £m	Other countries £m	Total £m
Balances with the Bank of England	5,599.8	-	-	-	5,599.8
Cash at bank and in hand	2,844.7	1,160.4	16.0	108.1	4,129.2
Investment securities:					
– available-for-sale securities	288.6	292.3	8.2	46.4	635.5
– investment securities held as loans and receivables	586.7	82.5	58.5	467.3	1,195.0
– unsecured investment loans	-	-	-	219.4	219.4
Total investment securities	875.3	374.8	66.7	733.1	2,049.9
Total	9,319.8	1,535.2	82.7	841.2	11,778.9

At 31 March 2014 and 31 December 2012 the Group held no investment securities issued by the governments of Portugal, the Republic of Ireland, Italy, Greece or Spain.

13. Loans to customers

	31 Mar 2014 £m	31 Dec 2012 £m
Residential mortgages	**59,344.6**	66,056.3
Commercial loans	**623.0**	781.9
Total secured loans	**59,967.6**	66,838.2
Unsecured loans	**1,281.9**	1,895.4
Total	**61,249.5**	68,733.6

Residential mortgages include all of the Group's buy-to-let loans. Commercial loans comprise loans secured on commercial properties. The 'Together' product, previously offered by NRAM, combines a secured and unsecured loan all at one interest rate and with flexible payments. Outstanding secured balances in respect of this product are included within total residential mortgages while outstanding unsecured balances are included within unsecured loans.

All of the Group's loans to customers are to UK customers.

Balances include accounting adjustments in respect of provisioning requirements.

Loans to customers include loans amounting to £41,152.6m (31 December 2012: £46,455.1m) which have been sold to bankruptcy-remote SPVs whereby substantially all of the risks and rewards of the portfolio are retained by the Group. Accordingly, all of these loans are retained on the Group's Balance Sheet. Further details are provided in note 24.

Fair value adjustments on portfolio hedging amounting to £308.8m (2012: £493.8m) relate to interest rate derivatives designated in a fair value portfolio hedge relationship.

13. Loans to customers (continued)

Loans to customers and redemptions comprise the following product types:

	Balances At 31 Mar 2014 £m	%	Redemptions 15 months to 31 Mar 2014 £m	Balances At 31 Dec 2012 £m	%	Redemptions 12 months to 31 Dec 2012 £m
Residential mortgages						
Buy-to-let	**23,061.9**	**39**	**(1,299.5)**	24,543.5	37	(843.5)
Self Cert	**5,983.6**	**10**	**(400.6)**	6,561.8	10	(291.0)
Together	**11,615.4**	**20**	**(1,379.2)**	13,185.8	20	(884.9)
Standard and other	**18,683.7**	**31**	**(2,739.3)**	21,765.2	33	(2,534.3)
Total residential mortgages	**59,344.6**	**100**	**(5,818.6)**	66,056.3	100	(4,553.7)
Residential loans	**59,344.6**	**97**	**(5,818.6)**	66,056.3	96	(4,553.7)
Commercial loans	**623.0**	**1**	**(150.2)**	781.9	1	(60.6)
Total secured loans	**59,967.6**	**98**	**(5,968.8)**	66,838.2	97	(4,614.3)
Unsecured loans	**1,281.9**	**2**	**(88.4)**	1,895.4	3	(231.9)
Total	**61,249.5**	**100**	**(6,057.2)**	68,733.6	100	(4,846.2)

Currently 46% of the Group's residential mortgage accounts (excluding buy-to-let) held by 152,000 customers are 'interest only' with 73% of these having more than ten years until maturity.

Redemptions comprise full redemptions and voluntary partial redemptions, but exclude overpayments and regular monthly payments.

In July 2012 NRAM announced the sale of £465m of loans to customers, at par, secured on residential property, to Virgin Money. These sold loans are excluded from the 2012 redemptions disclosed in the above table. In July 2013 NRAM completed the sale of its standalone unsecured personal loan book realising a profit on sale of £21.2m. These sold loans are excluded from the 2014 redemptions disclosed in the above table.

14. Impairment on loans to customers

Allowances for credit losses against loans to customers have been made as follows:

	On residential mortgages £m	On commercial loans £m	On unsecured loans £m	Total £m
At 1 January 2013	**1,411.1**	**100.0**	**403.8**	**1,914.9**
Movements during the period:				
– write-offs	**(374.1)**	**(19.4)**	**(82.2)**	**(475.7)**
– loan impairment charge	**114.8**	**10.3**	**41.4**	**166.5**
– sale of unsecured loans (see note 13)	**-**	**-**	**(148.3)**	**(148.3)**
Net movements during the period	**(259.3)**	**(9.1)**	**(189.1)**	**(457.5)**
At 31 March 2014	**1,151.8**	**90.9**	**214.7**	**1,457.4**
The Income Statement charge comprises:				
– loan impairment charge	**114.8**	**10.3**	**41.4**	**166.5**
– recoveries net of costs	**(62.0)**	**(4.4)**	**(5.0)**	**(71.4)**
Total Income Statement charge	**52.8**	**5.9**	**36.4**	**95.1**

14. Impairment on loans to customers (continued)

	On residential mortgages £m	On commercial loans £m	On unsecured loans £m	Total £m
At 1 January 2012	1,644.5	102.2	501.6	2,248.3
Movements during the year:				
– write-offs	(458.8)	(14.9)	(155.4)	(629.1)
– loan impairment charge	225.4	12.7	57.6	295.7
Net movements during the year	(233.4)	(2.2)	(97.8)	(333.4)
At 31 December 2012	1,411.1	100.0	403.8	1,914.9
The Income Statement charge comprises:				
– loan impairment charge	225.4	12.7	57.6	295.7
– recoveries net of costs	(38.4)	(0.6)	(15.3)	(54.3)
Total Income Statement charge	187.0	12.1	42.3	241.4

In respect of lifetime mortgages, the allowances include an additional provision reflecting estimated future impairment up to redemption. In the Balance Sheet the carrying values of loans to customers are presented net of these allowances.

15. Credit quality of loans to customers

In respect of loans to residential customers, the Group holds collateral in the form of mortgages over residential properties. The fair value of this collateral was as follows:

	31 Mar 2014 £m	31 Dec 2012 £m
Neither past due nor impaired	**80,744.9**	82,351.1
Past due but not impaired	**4,651.8**	6,547.0
Impaired	**784.9**	1,151.6
Total	**86,181.6**	90,049.7

If the collateral amount on each individual loan were capped at the amount of the balance outstanding, and any surplus of collateral values over balances outstanding ignored, the fair value of collateral held would be as follows:

	31 Mar 2014 £m	31 Dec 2012 £m
Neither past due nor impaired	**55,139.6**	58,712.3
Past due but not impaired	**3,757.9**	5,605.3
Impaired	**695.5**	1,045.2
Total	**59,593.0**	65,362.8
The impaired balances above include the following carrying amount of assets in possession, capped at the balance outstanding	**147.0**	260.4

The fair value of the collateral is estimated by taking the most recent valuation of the property and adjusting for house price inflation or deflation up to the Balance Sheet date.

15. Credit quality of loans to customers (continued)

The indexed loan to value ('LTV') of residential loan balances, weighted by loan balance, falls into the following ranges:

	31 Mar 2014 %	31 Dec 2012 %
To 50%	**7.6**	6.7
50% to 75%	**21.8**	14.7
75% to 100%	**52.7**	45.3
Over 100%	**17.9**	33.3
Total	**100.0**	100.0

The average indexed loan to value based on a simple average is 70.2% (31 December 2012: 74.9%) on a weighted average is 82.9% (31 December 2012: 89.1%).

	At 31 March 2014				At 31 December 2012			
	Residential mortgages £m	Commercial loans £m	Unsecured loans £m	Total £m	Residential mortgages £m	Commercial loans £m	Unsecured loans £m	Total £m
Neither past due nor impaired	**55,856.3**	**446.4**	**1,225.8**	**57,528.5**	60,347.7	599.0	1,724.8	62,671.5
Past due but not impaired:								
– less than 3 months	**2,303.3**	**1.5**	**84.0**	**2,388.8**	3,358.9	0.5	160.5	3,519.9
– 3 to 6 months	**919.3**	**-**	**26.9**	**946.2**	1,455.8	-	49.3	1,505.1
– over 6 months	**643.3**	**-**	**130.8**	**774.1**	1,088.1	-	136.6	1,224.7
Impaired	**774.2**	**266.0**	**29.1**	**1,069.3**	1,216.9	282.4	228.0	1,727.3
	60,496.4	**713.9**	**1,496.6**	**62,706.9**	67,467.4	881.9	2,299.2	70,648.5
Impairment allowances	**(1,151.8)**	**(90.9)**	**(214.7)**	**(1,457.4)**	(1,411.1)	(100.0)	(403.8)	(1,914.9)
Loans to customers net of impairment allowances	**59,344.6**	**623.0**	**1,281.9**	**61,249.5**	66,056.3	781.9	1,895.4	68,733.6
Impairment allowances:								
– individual	**146.4**	**90.9**	**44.0**	**281.3**	217.3	100.0	131.9	449.2
– collective	**1,005.4**	**-**	**170.7**	**1,176.1**	1,193.8	-	271.9	1,465.7
Total impairment allowances	**1,151.8**	**90.9**	**214.7**	**1,457.4**	1,411.1	100.0	403.8	1,914.9

The above table includes balances within 'neither past due nor impaired' which would have been shown as past due or impaired other than due to renegotiation; these were loans where arrears were capitalised during the period. These loans amounted to £9.9m (2012: £31.4m). A loan is eligible for capitalisation of arrears only once the borrower has complied with stringent terms for a set period.

15. Credit quality of loans to customers (continued)

Arrears and possessions on residential mortgages and unsecured loans

Arrears and possessions are monitored for the Group as a whole and also split by type of product.

		At 31 March 2014		At 31 December 2012	
		Residential	Unsecured	Residential	Unsecured
Arrears 3 months and over					
Number of cases	No.	**14,139**	**10,445**	23,376	31,140
Proportion of total cases	%	**2.68**	**8.76**	3.99	13.67
Asset value	£m	**2,067.5**	**172.7**	3,341.1	410.1
Proportion of book	%	**3.48**	**13.47**	5.06	21.64
Total value of payments overdue	£m	**84.3**	**23.0**	132.3	96.9
Proportion of total book	%	**0.14**	**1.80**	0.20	5.11
Possessions					
Number of cases	No.	**1,344**	**-**	2,205	-
Proportion of total cases	%	**0.25**	**-**	0.37	-
Asset value	£m	**199.0**	**-**	320.5	-
Proportion of book	%	**0.34**	**-**	0.48	-
Total value of payments overdue	£m	**14.0**	**-**	20.8	-
Proportion of total book	%	**0.02**	**-**	0.03	-
New possessions *	No.	**6,996**	**-**	7,326	-
Total arrears 3 months and over and possessions					
Number of cases	No.	**15,483**	**10,445**	25,581	31,140
Proportion of total cases	%	**2.93**	**8.76**	4.36	13.67
Asset value	£m	**2,266.5**	**172.7**	3,661.6	410.1
Proportion of book	%	**3.82**	**13.47**	5.54	21.64
Total value of payments overdue	£m	**98.3**	**23.0**	153.1	96.9
Proportion of total book	%	**0.16**	**1.80**	0.23	5.11

In respect of all arrears (including those which are less than 3 months in arrears) together with possessions, the total value of payments overdue was:

		At 31 March 2014 Residential	At 31 March 2014 Unsecured	At 31 December 2012 Residential	At 31 December 2012 Unsecured
Payments overdue					
Total value of payments overdue	£m	**121.2**	**23.8**	185.8	99.0
Proportion of total book	%	**0.20**	**1.86**	0.28	5.22
Loan impairment provision					
As % of total balances	%	**1.90**	**14.35**	2.09	17.56

* New possessions for the 15 months to 31 March 2014 and the 12 months to 31 December 2012.

15. Credit quality of loans to customers (continued)

Analysis of residential mortgages and unsecured loans 3 months and over in arrears by product

		At 31 March 2014		At 31 December 2012	
		Residential	Unsecured	Residential	Unsecured
Buy-to-let					
Number of cases	No.	**2,138**	-	3,390	-
Proportion of total cases	%	**1.11**	-	1.66	-
Asset value	£m	**324.8**	-	527.9	-
Proportion of book	%	**1.41**	-	2.15	-
Total value of payments overdue	£m	**12.1**	-	19.7	-
Proportion of total book	%	**0.05**	-	0.08	-
Self Cert					
Number of cases	No.	**1,166**	-	1,563	-
Proportion of total cases	%	**2.86**	-	3.60	-
Asset value	£m	**202.3**	-	273.4	-
Proportion of book	%	**3.38**	-	4.17	-
Total value of payments overdue	£m	**5.4**	-	7.2	-
Proportion of total book	%	**0.09**	-	0.11	-
Together					
Number of cases	No.	**4,761**	**10,445**	8,422	13,541
Proportion of total cases	%	**4.08**	**8.76**	6.49	10.18
Asset value	£m	**546.9**	**172.7**	958.2	228.4
Proportion of book	%	**4.71**	**13.47**	7.27	15.21
Total value of payments overdue	£m	**23.7**	**23.0**	40.0	22.9
Proportion of total book	%	**0.20**	**1.80**	0.30	1.52
Standard and other					
Number of cases	No.	**6,074**	-	10,001	17,599
Proportion of total cases	%	**3.42**	-	4.80	18.57
Asset value	£m	**993.5**	-	1,581.6	181.7
Proportion of book	%	**5.34**	-	7.27	46.21
Total value of payments overdue	£m	**43.1**	-	65.4	74.0
Proportion of total book	%	**0.23**	-	0.30	18.82

16. Deferred taxation

The net deferred taxation liability is attributable to the following:

	Assets		Liabilities		Net	
	31 Mar 2014 £m	31 Dec 2012 £m	31 Mar 2014 £m	31 Dec 2012 £m	31 Mar 2014 £m	31 Dec 2012 £m
Changes in accounting basis on adoption of IFRS	**17.7**	20.5	**(9.6)**	(4.5)	**8.1**	16.0
Cash flow hedges	**-**	-	**(53.6)**	(83.5)	**(53.6)**	(83.5)
Accelerated tax depreciation	**1.1**	1.8	**(2.4)**	(0.5)	**(1.3)**	1.3
Available-for-sale reserve and fair value	**-**	-	**(5.2)**	(9.6)	**(5.2)**	(9.6)
Employee benefits	**7.3**	24.2	**(13.0)**	(14.8)	**(5.7)**	9.4
Taxation value of losses carried forward	**6.9**	22.5	**-**	-	**6.9**	22.5
	33.0	69.0	**(83.8)**	(112.9)	**(50.8)**	(43.9)
Offset	**(33.0)**	(69.0)	**33.0**	69.0	**-**	-
Total	**-**	-	**(50.8)**	(43.9)	**(50.8)**	(43.9)

There were no deferred tax assets unrecognised at 31 March 2014 (31 December 2012: £nil). £6.9m (2012: £22.5m) of deferred tax assets have been recognised in respect of tax losses carried forward; based upon detailed business plans, there will be sufficient taxable profits in future years to utilise the losses on which deferred tax has been recognised.

The movements in the Group's temporary differences during the period and previous year were as follows:

	1 January 2013 £m	Recognised in income £m	Recognised in equity £m	31 March 2014 £m
Changes in accounting basis on adoption of IFRS	**16.0**	**(7.9)**	**-**	**8.1**
Cash flow hedges	**(83.5)**	**-**	**29.9**	**(53.6)**
Accelerated tax depreciation	**1.3**	**(2.6)**	**-**	**(1.3)**
Available-for-sale reserve and fair value	**(9.6)**	**3.4**	**1.0**	**(5.2)**
Employee benefits	**9.4**	**(13.4)**	**(1.7)**	**(5.7)**
Taxation value of losses carried forward	**22.5**	**(15.6)**	**-**	**6.9**
Total	**(43.9)**	**(36.1)**	**29.2**	**(50.8)**

	1 January 2012 £m	Recognised in income £m	Recognised in equity £m	31 December 2012 £m
Changes in accounting basis on adoption of IFRS	3.2	12.8	-	16.0
Cash flow hedges	(38.1)	-	(45.4)	(83.5)
Accelerated tax depreciation	4.0	(2.7)	-	1.3
Available-for-sale reserve and fair value	(10.3)	2.4	(1.7)	(9.6)
Employee benefits	(4.5)	(5.7)	19.6	9.4
Taxation value of losses carried forward	46.5	(24.0)	-	22.5
Total	0.8	(17.2)	(27.5)	(43.9)

The announced UK corporation tax rate reduction to 20% with effect from 1 April 2015 has been reflected in the 31 March 2014 deferred tax balance.

17. Other assets

	At 31 Mar 2014 £m	At 31 Dec 2012 £m
Prepayments and accrued income	**7.5**	24.0
Other	**29.9**	16.7
Total	**37.4**	40.7

18. Retirement benefit assets and obligations

The UKAR Group operates a number of retirement benefit plans for its current and former employees, including defined benefit pension plans, defined contribution pension plans and post-retirement healthcare benefits. Further details in respect of the Group's schemes are given in sections (a) (B&B schemes) and (b) (NRAM schemes) below. The 'administrative expenses' line of the Income Statement includes the cost of contributions to the healthcare and defined contribution pension schemes, and for each defined benefit scheme the current service cost of providing pension benefits, and the interest cost on the scheme's net asset or liability. The current service cost of the Group's defined benefit schemes is nil, as the schemes are now closed to future service accrual. The full net surplus or deficit in respect of the healthcare scheme and each defined benefit pension scheme is carried on the UKAR Group Balance Sheet, and gains and losses arising due to remeasurements are taken to UKAR Group other comprehensive income rather than being credited or charged in the Income Statement. During the period, the UKAR Group has adopted the revisions to IAS 19 which were issued in June 2011 and adopted for use in the EU in June 2012. The main effect on the Group of these revisions to IAS 19 is that instead of an expected rate of return being applied to defined benefit plan assets, the discount rate previously applied to defined benefit plan obligations is instead applied to the net surplus or deficit on the plan.

(a) Bradford & Bingley schemes

Defined pension benefit scheme

The B&B Group operated a defined benefit pension scheme, the Bradford & Bingley Staff Pension Scheme ('the principal scheme'), which is administered by 'the Trustee'. Mercer Limited are the actuarial advisors to the principal scheme, and also independently provide actuarial information in respect of the principal scheme to the Company. Investment advice is provided by Towers Watson Limited. Legal advice is provided by Squire Sanders. The Trustee is responsible for ensuring the principal scheme meets its Statutory Funding Objective which is set by The Pensions Regulator. The principal scheme provided benefits to employees on a final salary basis. On 31 December 2009 the principal scheme was closed to future service accrual; all members became deferred members and were given the option to join the B&B Group's defined contribution scheme from 1 January 2010. The normal pension age of employees in the principal scheme is 65. In respect of deferred members, deferred pension entitlement increases are calculated by reference to the Consumer Prices Index ('CPI'), limited to 5% per annum.

The cost to the Group of funding the principal scheme guaranteed benefits varies over time, dependent on market conditions and life expectancies. The cost in the period was £2.4m (31 December 2012: £0.9m) and the retirement benefit remeasurement gain recognised in other comprehensive income during the period was £18.9m (2012: loss £64.8m).

The assets of the principal scheme are held in a separate trustee-administered fund. The Trustee of the principal scheme has passed a resolution for the ultimate refund to B&B of any future surpluses on the principal scheme.

Under an agreed recovery plan to address the deficit on the principal scheme, the Group is committed to making annual contributions to the principal scheme up to and including June 2019. Under this plan the Group will contribute £35.1m in the year to 31 March 2015, and future contributions will increase at a compounding annual rate of 10%. The recovery plan will be reassessed following the next formal triennial valuation in June 2015.

The Trustee manages the volatility in the value of the principal scheme's assets by limiting the exposure to return-seeking assets and using liability-driven investment strategies to increase the level of hedging against investment risks. The two key investment risks are interest rate risk and inflation risk relating to the principal scheme's obligations. By holding swaps, fixed interest gilts, index-linked gilts and corporate bonds, approximately 65% of the interest rate risk and approximately 65% of the inflation risk has been hedged. The holding of return-seeking assets is close to the target level required to achieve the investment return assumed within the deficit recovery plan.

The principal scheme has a written guarantee from HM Treasury that benefits will be paid in full to the members.

Defined contribution pension scheme

The B&B Group also operates a defined contribution pension scheme, the UKAR Pension Plan, into which both employees and the Group make contributions. The assets of this scheme are independent from those of the Group. The UKAR Group and Company had no liabilities or prepayments associated with this scheme at 31 March 2014 (31 December 2012: £nil). The cost in the period to the UKAR Group of this scheme was £4.2m (2012: £3.4m). The cost to the Group varies according to the number of employees in the Group and their salary levels, but the Group has no risk of being required to provide additional funding to the scheme.

Healthcare scheme

The B&B Group provides healthcare benefits to some of its pensioners. The healthcare benefits are provided through a scheme into which the UKAR Group contributes 100% towards the cost of providing the benefits for members who retired before 1 January 1996 and 50% for members who retired after this date. The total number of members of the scheme at 31 March 2014 was 314 (31 December 2012: 323). The value of the Group's obligation is assessed in accordance with the advice of a qualified actuary. The cost in the period to the UKAR Group of this scheme was £0.6m (2012: £0.5m) and the remeasurement gain recognised in the UKAR Group's other comprehensive income during the period was £1.5m (2012: gain £0.5m).

18. Retirement benefit assets and obligations (continued)

(a) Bradford & Bingley schemes (continued)

Defined benefit obligations

The amounts carried on the UKAR Group Balance Sheet are as follows:

	Defined benefit pension plans		Post-retirement medical benefits		Total	
	31 Mar 2014	31 Dec 2012	31 Mar 2014	31 Dec 2012	31 Mar 2014	31 Dec 2012
	£m	£m	£m	£m	£m	£m
Present value of defined benefit obligations	**(782.2)**	(730.8)	**(8.0)**	(9.6)	**(790.2)**	(740.4)
Fair value of defined benefit assets	**769.9**	669.9	**-**	-	**769.9**	669.9
Net defined benefit liability	**(12.3)**	(60.9)	**(8.0)**	(9.6)	**(20.3)**	(70.5)

The amounts recognised in the UKAR Group Income Statement were as follows:

	Defined benefit pension plans		Post-retirement medical benefits		Total	
	15 months to 31 Mar 2014	12 months to 31 Dec 2012	15 months to 31 Mar 2014	12 months to 31 Dec 2012	15 months to 31 Mar 2014	12 months to 31 Dec 2012
	£m	£m	£m	£m	£m	£m
Net interest expense	**2.4**	0.9	**0.6**	0.5	**3.0**	1.4
Total recognised in Income Statement	**2.4**	0.9	**0.6**	0.5	**3.0**	1.4

Movements in the present value of defined benefit obligations were as follows:

	Defined benefit pension plans		Post-retirement medical benefits		Total	
	15 months to 31 Mar 2014	12 months to 31 Dec 2012	15 months to 31 Mar 2014	12 months to 31 Dec 2012	15 months to 31 Mar 2014	12 months to 31 Dec 2012
	£m	£m	£m	£m	£m	£m
At start of period	**730.8**	663.7	**9.6**	9.9	**740.4**	673.6
Interest on defined benefit obligations	**40.4**	30.8	**0.6**	0.5	**41.0**	31.3
Remeasurements:						
– effect of changes in demographic assumptions	**-**	22.5	**-**	-	**-**	22.5
– effect of changes in financial assumptions	**34.8**	35.7	**(1.7)**	-	**33.1**	35.7
– effect of experience adjustments	**1.4**	(3.0)	**0.2**	(0.5)	**1.6**	(3.5)
Administrative expenses included within defined benefit obligation	**(1.4)**	-	**-**	-	**(1.4)**	-
Benefits paid from plan	**(23.8)**	(18.9)	**(0.7)**	(0.3)	**(24.5)**	(19.2)
At end of period	**782.2**	730.8	**8.0**	9.6	**790.2**	740.4

18. Retirement benefit assets and obligations (continued)

(a) Bradford & Bingley schemes (continued)

Movements in the fair value of defined benefit assets were as follows:

	Defined benefit pension plans		Post-retirement Medical benefits		Total	
	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
At start of period	**669.9**	649.0	**-**	-	**669.9**	649.0
Interest income on defined benefit assets	**38.0**	29.9	**-**	-	**38.0**	29.9
Defined benefit company contributions	**32.1**	19.4	**0.7**	0.3	**32.8**	19.7
Remeasurements:						
– return on plan assets (excluding interest income)	**55.1**	(9.6)	**-**	-	**55.1**	(9.6)
Administrative expenses paid from plan assets	**(1.4)**	-	**-**	-	**(1.4)**	-
Benefits paid from plan	**(23.8)**	(18.8)	**(0.7)**	(0.3)	**(24.5)**	(19.1)
At end of period	**769.9**	669.9	**-**	-	**769.9**	669.9

The major categories of defined benefit assets at the end of the period were as follows:

			31 March 2014			31 December 2012
	Quoted £m	Unquoted £m	Total £m	Quoted £m	Unquoted £m	Total £m
Equity instruments	**155.3**	**5.5**	**160.8**	170.5	5.2	175.7
Property	**2.1**	**40.5**	**42.6**	1.2	39.2	40.4
Bonds						
– of which UK	**8.4**	**116.3**	**124.7**	8.3	126.1	134.4
– of which overseas	**48.5**	**98.7**	**147.2**	47.2	103.4	150.6
Liability hedging investments	**3.1**	**253.3**	**256.4**	3.0	165.7	168.7
Cash and cash equivalents	**-**	**38.2**	**38.2**	-	0.1	0.1
Total	**217.4**	**552.5**	**769.9**	230.2	439.7	669.9

Summary actuarial assumptions (expressed as weighted averages) were as follows:

	31 Mar 2014	31 Dec 2012
To determine benefit obligations:		
Discount rate	**4.6%**	4.5%
Inflation (RPI)	**3.5%**	3.0%
Inflation (CPI)	**2.7%**	2.4%
Future pension increases	**3.3%**	2.9%
To determine net pension cost:		
Discount rate	**4.5%**	4.7%
For post-retirement medical plan:		
Discount rate	**4.6%**	4.5%
Medical cost trend for duration of liability	**5.5%**	6.1%

In determining the expected long-term return on defined benefit assets, the B&B Group considered the current level of expected returns on risk-free investments (primarily government bonds), the historical level of risk premium associated with the other asset classes in which the portfolio is invested and the expectations for future returns on each asset class. The expected return for each asset class was then weighted based on the target asset allocation to develop the expected long-term return for the portfolio.

18. Retirement benefit assets and obligations (continued)

(a) Bradford & Bingley schemes (continued)

The table below shows the life expectancy assumptions from age 60:

	31 March 2014 Pensioner	31 March 2014 Non-retired member	31 December 2012 Pensioner	31 December 2012 Non-retired member
Male	**28.5**	**30.0**	28.3	29.8
Female	**31.2**	**32.8**	31.0	32.6

The basis of estimation of life expectancy was changed during 2012 to use data which is believed better to reflect the characteristics of the membership of the plan.

The defined benefit pension scheme has a weighted average maturity of around 22 years.

Sensitivity

The following table illustrates the sensitivity of the defined benefit pension scheme obligations to three key assumptions: the discount rate, the rate of inflation and the mortality assumption:

Assumption	Change in assumption	Impact on obligations
Discount rate	Decrease by 0.5%	Increase by 12%
Inflation	Increase by 0.5%	Increase by 10%
Mortality	Decrease by 1 year	Increase by 2%

If the assumptions were to change by the same amount in the opposite direction to those illustrated, the obligations would decrease by a similar percentage to those shown in the table in each case.

Assumed healthcare cost trend rates have an effect on the amounts recognised in staff costs. A one percentage point change in assumed healthcare cost trend rates would have the following effects:

	At 31 Mar 2014 £m	At 31 Dec 2012 £m
Effect on interest cost	**0.1**	0.1
Effect on defined benefit obligation	**1.2**	1.5

(b) NRAM schemes

Defined benefit pension scheme

The NRAM Group operated a staff pension scheme ('the Scheme'), which had both defined benefit and defined contribution sections. Towers Watson Limited are the actuarial and investment advisors to the Scheme, and also independently provide actuarial information in respect of the Scheme to the Company. Legal advice is provided by Sackers. On 1 January 2010 all employees previously employed by the NRAM Group transferred to Northern Rock plc under the terms of the Northern Rock Transfer Order 2009. As a consequence of this, members of the Scheme became members of the Northern Rock (2010) Pension Scheme, which had both defined benefit and defined contribution sections, and the existing Scheme was closed. The assets of the closed Scheme are held in a separate trustee-administered fund. The normal pension age of employees in this Scheme is 60. The Scheme provided benefits to employees on a final salary basis. Deferred pension entitlement increases are calculated by reference to the Retail Prices Index ('RPI'). The trustees of the Scheme are responsible for ensuring the Scheme meets its Statutory Funding Objective which is set by The Pensions Regulator. The trustees of the Scheme have passed a resolution for the ultimate refund to NRAM of any future surpluses on the Scheme.

The cost to the Group of funding the Scheme guaranteed benefits varies over time, dependent on market conditions and life expectancies. The credit in the period was £3.2m (31 December 2012: credit £0.3m) and the retirement benefit remeasurement loss recognised in other comprehensive income during the period was £16.2m (2012: loss £22.4m).

As at 31 March 2014 and 31 December 2012, the Scheme was in surplus on an accounting basis but in deficit on a trustee's funding basis. Under an agreed recovery plan to address this deficit, the Group is committed to making annual contributions to the Scheme up to and including April 2019. Under this plan, the Group has contributed £34.0m in April 2014 and the level of contributions will be reassessed each year.

Following the nationalisation of Northern Rock plc in 2008, the Scheme's trustees disposed of the majority of the return-seeking assets, retaining a small holding in private equity funds; the remaining assets are split between gilts and corporate bonds. The Scheme has instigated a liability-driven investment programme to hedge approximately 77% of the interest rate risk and 77% of the inflation risk.

18. Retirement benefit assets and obligations (continued)

(b) NRAM schemes (continued)

Defined contribution pension scheme

Of the employees who transferred to the Northern Rock (2010) Pension Scheme, 1,254 subsequently transferred to B&B on 1 November 2010 and were eligible to join that company's defined contribution pension scheme (the UKAR Pension Plan) into which both employees and the Group make contributions. The Group and Company had no liabilities or prepayments associated with the UKAR Pension Plan as at 31 March 2014 (2012: £nil). The cost in the period to the NRAM Group arising from amounts recharged by B&B, in respect of employees providing services to the NRAM Group who participate in this scheme, was £2.6m (2012: £2.0m); the cost to the NRAM Group varies according to the number of B&B employees providing services to the NRAM Group and their salary levels, but the NRAM Group has no risk of being required to provide additional funding to the scheme.

Defined benefit section of the Scheme

The amounts carried on the UKAR Group Balance Sheet are as follows:

	31 Mar 2014 £m	31 Dec 2012 £m
Present value of defined benefit obligations	**(480.7)**	(459.2)
Fair value of defined benefit assets	**546.0**	502.2
Net defined benefit asset	**65.3**	43.0

The amounts recognised in the UKAR Group Income Statement were as follows:

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Net interest income	**(4.2)**	(0.3)
Total recognised in Income Statement	**(4.2)**	(0.3)

Movements in the present value of defined benefit obligations were as follows:

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
At start of period	**459.2**	423.7
Interest on defined benefit obligations	**25.6**	19.6
Remeasurements:		
– effect of changes in financial assumptions	**11.3**	24.5
– effect of experience adjustments	**(1.4)**	2.7
Benefits paid from plan	**(14.0)**	(11.3)
At end of period	**480.7**	459.2

Movements in the fair value of defined benefit assets were as follows:

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
At start of period	**502.2**	473.5
Interest income on defined benefit assets	**29.8**	19.9
Defined benefit company contributions	**34.3**	15.3
Remeasurements: – return on plan assets (excluding interest income)	**(6.3)**	4.8
Benefits paid from plan	**(14.0)**	(11.3)
At end of period	**546.0**	502.2

18. Retirement benefit assets and obligations (continued)

(b) NRAM schemes (continued)

Defined benefit section of the Scheme (continued)

The major categories of defined benefit assets at the end of the period were as follows:

			31 March 2014			31 December 2012
	Quoted £m	Unquoted £m	Total £m	Quoted £m	Unquoted £m	Total £m
Equity instruments	**-**	**13.7**	**13.7**	-	13.5	13.5
Bonds						
– of which UK	**84.2**	**-**	**84.2**	85.6	-	85.6
– of which overseas	**31.2**	**-**	**31.2**	29.3	-	29.3
Liability hedging investments	**195.6**	**-**	**195.6**	175.0	-	175.0
Bulk annuity contract	**-**	**186.5**	**186.5**	-	188.7	188.7
Cash and cash equivalents	**34.8**	**-**	**34.8**	10.1	-	10.1
Total	**345.8**	**200.2**	**546.0**	300.0	202.2	502.2

Summary actuarial assumptions (expressed as weighted averages) were as follows:

	31 Mar 2014	31 Dec 2012
To determine benefit obligations:		
Discount rate	**4.6%**	4.5%
Inflation (RPI)	**3.5%**	3.0%
Future pension increases	**3.0% – 3.75%**	2.9% – 3.6%
To determine net pension cost:		
Discount rate	**4.5%**	4.7%

In determining the expected long-term return on defined benefit assets, the NRAM Group considered the current level of expected returns on risk-free investments (primarily government bonds), the historical level of risk premium associated with the other asset classes in which the portfolio is invested and the expectations for future returns on each asset class. The expected return for each asset class was then weighted based on the target asset allocation to develop the expected long-term return for the portfolio.

The table below shows the life expectancy assumptions from age 60:

		31 March 2014		31 December 2012
	Pensioner	Non-retired member	Pensioner	Non-retired member
Male	**27.7**	**29.2**	27.5	29.0
Female	**30.1**	**31.7**	29.9	31.5

The basis of estimation of life expectancy was changed during 2012 to use data which is believed better to reflect the characteristics of the membership of the Scheme.

The defined benefit pension scheme has a weighted average maturity of around 21 years.

Sensitivity

The following table illustrates the sensitivity of the defined benefit pension Scheme obligations to three key assumptions: the discount rate, the rate of inflation and the mortality assumption:

Assumption	Change in assumption	Impact on obligations
Discount rate	Decrease by 0.5%	Increase by 12%
Inflation	Increase by 0.5%	Increase by 8%
Mortality	Decrease by 1 year	Increase by 2%

If the assumptions were to change by the same amount in the opposite direction to those illustrated, the obligations would decrease by a similar percentage to those shown in the table in each case.

19. Investment property

The Group carried its investment property at fair value. Fair value was determined by independent professional valuers applying recognised valuation techniques.

During 2012, rental income in respect of the property of £3.3m was recognised in the Income Statement.

19. Investment property (continued)

The property was sold to Virgin Money on 22 June 2012.

Movements in the value of investment property are analysed as follows:

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Investment properties at fair value at start of period	-	26.6
Fair value movement	-	2.9
Disposals	-	(29.5)
Investment properties at fair value at end of period	-	-

20. Property, plant and equipment

	Land and buildings £m	Plant, equipment, fixtures, fittings and vehicles £m	Total £m
Cost			
At 1 January 2013	**37.7**	**70.9**	**108.6**
Additions	**-**	**1.8**	**1.8**
Disposals	**(14.6)**	**(0.8)**	**(15.4)**
At 31 March 2014	**23.1**	**71.9**	**95.0**
Depreciation			
At 1 January 2013	**26.6**	**53.3**	**79.9**
Charged in period	**0.7**	**5.2**	**5.9**
Disposals	**(11.9)**	**(0.8)**	**(12.7)**
At 31 March 2014	**15.4**	**57.7**	**73.1**
Net book amount:			
At 1 January 2013	**11.1**	**17.6**	**28.7**
At 31 March 2014	**7.7**	**14.2**	**21.9**

	Land and buildings £m	Plant, equipment, fixtures, fittings and vehicles £m	Total £m
Cost			
At 1 January 2012	63.2	88.7	151.9
Additions	-	4.5	4.5
Disposals	(25.5)	(22.3)	(47.8)
At 31 December 2012	37.7	70.9	108.6
Depreciation			
At 1 January 2012	34.2	68.5	102.7
Charged in year	1.2	3.8	5.0
Accelerated depreciation	8.3	-	8.3
Disposals	(17.1)	(19.0)	(36.1)
At 31 December 2012	26.6	53.3	79.9
Net book amount:			
At 1 January 2012	29.0	20.2	49.2
At 31 December 2012	11.1	17.6	28.7

20. Property, plant and equipment (continued)

During the period ended 31 March 2014, £2.0m of work in progress held at 31 December 2012 and £1.8m of additions have begun depreciating. The work in progress relates to an IT investment programme to simplify existing infrastructure and reduce ongoing costs.

Sale proceeds from asset disposals were £10.0m (2012: £11.3m) resulting in a profit on sale of £7.3m (2012: £0.4m loss). NRAM's Doxford site (including Solar House) was disposed of in a sale and leaseback transaction in September 2013. NRAM's Gosforth site was sold to Virgin Money on 22 June 2012.

An accelerated depreciation charge of £8.3m was made in 2012 relating mainly to NRAM's Doxford site. This followed an external property valuation carried out during 2012.

21. Intangible assets

	£m
Cost	
At 1 January 2013	**75.2**
Additions	**8.9**
At 31 March 2014	**84.1**
Impairment and amortisation	
At 1 January 2013	**27.9**
Amortisation charged in period	**13.5**
At 31 March 2014	**41.4**
Net book amount:	
At 1 January 2013	**47.3**
At 31 March 2014	**42.7**

	£m
Cost	
At 1 January 2012	58.4
Additions	20.0
Disposals	(3.2)
At 31 December 2012	75.2
Impairment and amortisation	
At 1 January 2012	23.9
Amortisation charged in year	7.2
Disposals	(3.2)
At 31 December 2012	27.9
Net book amount:	
At 1 January 2012	34.5
At 31 December 2012	47.3

Intangible assets comprise capitalised computer software systems and licences.

At 31 March 2014, work in progress of £5.2m (2012: £4.1m) has been capitalised and is not being amortised.

During the period ended 31 March 2014, £4.1m of work in progress held at 31 December 2012 (2012: £32.8m) and £3.7m of additions (2012: £15.9m) have begun amortising. The work in progress relates to an IT investment programme to simplify existing infrastructure and reduce ongoing costs.

All assets sold in 2012 had already been fully depreciated, and no sale proceeds were received, and hence there was no profit or loss on the sales.

22. Amounts due to banks

	At 31 Mar 2014 £m	At 31 Dec 2012 £m
Cash collateral received (see note 36)	**3,119.1**	4,754.0
Other	**0.1**	40.9
Total	**3,119.2**	4,794.9

23. Statutory Debt and HM Treasury loans

	At 31 Mar 2014 £m	At 31 Dec 2012 £m
HM Treasury loan to NRAM	**14,935.2**	18,063.1
B&B Statutory Debt	**18,416.2**	18,416.2
HM Treasury Working Capital Facility to B&B	**4,999.1**	7,008.0
Total	**38,350.5**	43,487.3

The HM Treasury loan to NRAM is repayable on demand. Interest has been charged at Bank of England Base Rate + 100 bps since 4 May 2012 (prior to that date interest was charged at Bank of England Base Rate + 25 bps). At the signing date of these Financial Statements, HM Treasury has confirmed its intentions to continue to fund NRAM as a going concern, and to enable NRAM to meet its debts as and when they fall due until at least 1 January 2016. It has also committed to convert up to £1.6bn of its loan to NRAM to meet regulatory capital requirements if so required. It is expected that the HM Treasury loan will be repaid out of the cash flows generated by NRAM during its wind-down. These cash flows will principally comprise interest and redemptions arising on loans to customers. The redemption profile of loans to customers is uncertain; many of these loans have contractual maturities of 25 years or more from the date of advance but experience has been that most loans to customers redeem earlier than their contractual maturity dates. Consequently, the timing of the repayment of the HM Treasury loan to NRAM is uncertain.

B&B has an interest-free Statutory Debt of £18,416.2m as at 31 March 2014 and 31 December 2012. This replaced B&B's savings-related assets and liabilities which were transferred to Banco Santander Group on 29 September 2008. £15,654.5m of the Statutory Debt is owed to the Financial Services Compensation Scheme ('FSCS'). At the time of nationalisation, the FSCS covered the first £35,000 per depositor; HM Treasury agreed to cover the excess over £35,000, amounting to a total of £2,761.7m. It is expected that the Statutory Debt will be repaid out of the cash flows generated by B&B during its wind-down. These cash flows will principally comprise interest and redemptions arising on loans to customers. The redemption profile of loans to customers is uncertain; many of these loans have contractual maturities of 25 years or more from the date of advance but experience has been that most loans to customers redeem earlier than their contractual maturity dates. Consequently, the timing of the repayment of the Statutory Debt is uncertain.

B&B has an interest-bearing Working Capital Facility ('WCF') provided by HM Treasury. Since 1 August 2011 the rate charged has been Bank of England Base Rate + 500bps and prior to that date the rate was Bank of England Base Rate + 150bps. HM Treasury has the option to vary the rate charged. At 31 March 2014 B&B had drawn £4,975.0m (2012: £6,975.0m) of this facility; £4,999.1m including accrued interest (2012: £7,008.0m). HM Treasury has confirmed its intentions to continue to fund B&B as a going concern and to enable B&B to meet its debts as and when they fall due, until at least 1 January 2016. HM Treasury has indicated that it expects the WCF to be repaid out of the cash flows generated by B&B during its wind-down. These cash flows will principally comprise interest and redemptions arising on loans to customers. The redemption profile of loans to customers is uncertain; many of these loans have contractual maturities of 25 years or more from the date of advance but experience has been that most loans to customers redeem earlier than their contractual maturity dates. Consequently, the timing of the repayment of the WCF is uncertain.

24. Debt securities in issue

	Securitised notes £m	Covered Bonds £m	Other £m	Total £m
At 1 January 2013	**19,624.7**	**11,083.4**	**912.0**	**31,620.1**
Repayments	**(3,461.0)**	**(1,828.2)**	**(363.1)**	**(5,652.3)**
Other movements	**14.9**	**(91.3)**	**(5.4)**	**(81.8)**
At 31 March 2014	**16,178.6**	**9,163.9**	**543.5**	**25,886.0**
Securitised assets	**26,183.9**	**16,298.6**	**-**	**42,482.5**
Reserve fund	**1,388.5**	**22.9**	**-**	**1,411.4**

24. Debt securities in issue (continued)

	Securitised notes £m	Covered Bonds £m	Other £m	Total £m
At 1 January 2012	23,883.5	12,096.0	2,082.0	38,061.5
Repayments	(3,186.9)	(440.3)	(1,122.0)	(4,749.2)
Repurchase	(537.8)	-	-	(537.8)
Other movements	(534.1)	(572.3)	(48.0)	(1,154.4)
At 31 December 2012	19,624.7	11,083.4	912.0	31,620.1
Securitised assets	29,416.3	18,807.8	-	48,224.1
Reserve fund	1,393.1	23.0	-	1,416.1

Other movements comprise exchange rate movements, accrued interest and hedge accounting adjustments.

During 2012 the Group purchased securitised notes which had been issued by certain of the Group's securitisation vehicles, generating a profit of £143.4m as shown in note 8. No such purchases were made in 2013/14.

The B&B and NRAM Groups issued debt securities to securitise loans to customers through SPVs and Covered Bonds and also raised unsecured medium term funding, the amounts of which are shown above. Certain of these were subject to fair value hedge designation and the carrying values of these instruments include unamortised adjustments in respect of the notes that were hedged.

HM Treasury has provided guarantees with regard to certain wholesale borrowings of the B&B and NRAM Groups; the Group pays fees for these guarantees, as detailed in note 3.

Securitised assets represent loans to customers which have been used to securitise issued notes, including notes which are held by other companies in the UKAR Group. B&B and NRAM pass to their SPVs cash received in relation to the securitised assets. The SPVs use the cash to service the bonds, retain a margin specified under the terms of the issue and return any surplus cash to B&B and NRAM. To the extent that the total cash receipts in relation to the securitised assets are insufficient to satisfy interest and principal payments in relation to the bonds, the holders of the bonds have no recourse against the Group. Provided that the total cash receipts in relation to the securitised assets are sufficient to satisfy interest and principal payments in relation to the bonds, B&B/NRAM bear the cost of any impairment of the securitised assets. While the assets remain securitised the Group may not use, sell or pledge these assets.

In respect of Covered Bonds, B&B and NRAM pass to Bradford & Bingley Covered Bonds LLP and NRAM Covered Bond LLP all cash received in relation to the securitised assets. Bradford & Bingley Covered Bonds LLP and NRAM Covered Bond LLP use cash receipts to service the bonds and return any surplus cash to B&B/NRAM. B&B and NRAM bear the cost of any impairment of the securitised assets. While the assets remain securitised, the Group may not use, sell or pledge these assets.

Further details of debt securities in issue are provided in the Annual Reports and Accounts of B&B and NRAM, copies of which are available on the corporate website of each of these companies.

At 31 March 2014 the SPVs had cash deposits (including accrued interest) amounting to £3,254.4m, including collateral deposits of £1,275.0m (2012: £3,594.2m, including collateral deposits of £1,568.9m). These balances (excluding the collateral deposits) are restricted in use to the servicing of the debt securities issued by the SPVs and other legal obligations.

On 10 May 2012 a Non-Asset Trigger Event (as defined in the Offering Circular) occurred within B&B's Master Trust securitisation structure due to the aggregate current balance of loans comprising the Trust Property falling below the minimum trust size of £10.7bn. The impact of this event is to change the order of priority of the Funding 1 Available Principal Receipts. As a result of the Non-Asset Trigger Event, all principal receipts from customers are allocated to Funding 1 and will continue to be so allocated until all holders of Aire Valley residential mortgage-backed securities have been repaid in full if sufficient funds are ultimately available. The principal is then passed to the Issuers based on their respective notes outstanding. Each Issuer then utilises this principal to pay down notes pro-rata and sequentially by class. The timing of future redemptions will be dependent on the availability of funds.

On 11 November 2008, as a result of a breach of a non-asset trigger, the Granite Master Trust moved into pass through. The main consequence of this is that the repayments of the loan notes no longer adhere to the controlled amortisation schedules detailed in the SPVs' offering circulars. All principal cash received by the Trust is allocated between Granite Finance Funding Limited and Granite Finance Funding 2 Limited in accordance with their respective shares of the Trust's property as at 1 November 2008, this being the last determination date prior to the breach of the non-asset trigger. The principal cash allocated to Granite Finance Funding Limited is then distributed pro-rata between the relevant issuers in the Granite Finance Funding Limited group by reference to the size of their inter-company loans outstanding with Granite Finance Funding Limited at each determination date. The principal cash received by the issuers is utilised in full on each quarterly payment date to make repayments in respect of the loan notes. The priority of loan note repayment is by reference to their original credit ratings on issue, with AAA notes repaid first, then AA notes, then A notes and finally BBB notes. The principal cash allocated to Granite Finance Funding 2 Limited is used to repay the loan from Granite Master Issuer plc, which in turn uses the cash to repay the loan notes in issue by reference to their original credit ratings on issue in the same manner as detailed above. The average time taken to repay the loan notes is now expected to be significantly extended beyond the maturity profiles envisaged by the original controlled amortisation schedules. As a result of the change in repayment process as detailed above, the repayment of the loans did not occur ahead of the step-up dates and as such an increased amount of interest on the loan notes is now being made. Also as a result of this, some of the reserve funds have had additional amounts applied to them to cover the increased payment risk.

Other debt securities in issue comprise notes issued under B&B's and NRAM's Medium Term Notes programmes.

As detailed in note 39, certain securities issued by Group companies have been purchased by NRAM since the Balance Sheet date.

25. Other liabilities

	31 March 2014 £m	31 Dec 2012 £m
Accruals and deferred income	**72.4**	71.7
Other	**87.4**	98.1
Total	**159.8**	169.8

26. Provisions

	Customer redress £m	Onerous contracts £m	Restructuring £m	Total £m
At 1 January 2013	**168.8**	**8.4**	**50.4**	**227.6**
Utilised in the period	**(144.1)**	**(3.1)**	**(39.2)**	**(186.4)**
Charged in the period	**132.0**	**-**	**-**	**132.0**
Released in the period	**-**	**(0.7)**	**(4.8)**	**(5.5)**
At 31 March 2014	**156.7**	**4.6**	**6.4**	**167.7**

	Customer redress £m	Onerous contracts £m	Restructuring £m	Total £m
At 1 January 2012	173.7	12.2	29.1	215.0
Utilised in the year	(194.7)	(3.0)	(13.4)	(211.1)
Charged in the year	419.0	-	34.7	453.7
Released in the year	-	(0.8)	-	(0.8)
Allocation against customer balances	(229.2)	-	-	(229.2)
At 31 December 2012	168.8	8.4	50.4	227.6

As reported in the Group's 2012 ARA, a provision was made in 2012 in respect of non-compliant Consumer Credit Act ('CCA') loans. An additional remediation charge of £47.0m was made in respect of this in June 2013 together with £16.2m of interest. A further charge of £17.9m has been made at the period end mainly relating to additional redress required as a result of ongoing remediation exercises impacting CCA regulated loans. £42.2m of the CCA provision remains at the period end.

The payment protection insurance ('PPI') provision was increased by £29.0m during the period, with £71.0m remaining at the period end.

In addition, there has been a net charge of £21.9m in respect of other remediation activities. This includes £15.0m for customers who have potentially been incorrectly maintained on interest only products beyond their expectations, having originally switched from capital repayment plans for a temporary period.

All customer redress payments are expected to be processed during the year to 31 March 2015 except for PPI, the majority of which is expected to be processed by 31 March 2017. The timing and total value of future PPI payments is uncertain and is dependent on a number of external factors; it has been assumed that the volume of PPI claims will continue to decline over time and beyond 31 March 2017 will not be material.

The onerous contracts provision relates to empty leasehold premises which, as at the Balance Sheet date, were no longer used by the business but were subject to lease agreements. The rental payments are due to be made during the period to 2025.

The restructuring provision mainly relates to the change in primary IT service provider and we expect the majority of this to be paid out during the year to 31 March 2015.

27. Capital instruments

	Initial interest rate	First due or callable	Final maturity	Issuer	31 March 2014 Carrying amount £m	31 March 2014 Principal £m	31 December 2012 Carrying amount £m	31 December 2012 Principal £m
Dated subordinated notes	7.625%	2010	2049	B&B	**17.6**	**12.2**	16.1	12.2
Dated fixed rate step-up subordinated notes	5.50%	2018	2018	B&B	**5.6**	**4.4**	5.4	4.4
Callable perpetual subordinated notes	5.625%	2013	Undated	B&B	**22.5**	**18.1**	21.5	18.1
Callable perpetual subordinated notes	6.00%	2019	Undated	B&B	**18.2**	**14.7**	23.1	20.0
Undated perpetual subordinated bonds	13.00%	Perpetual	Undated	B&B	**51.1**	**41.5**	42.6	41.5
Undated perpetual subordinated bonds	11.625%	Perpetual	Undated	B&B	**44.1**	**35.7**	37.5	35.7
Subordinated loan	11.734%	See below	2016	NRAM	**14.1**	**12.0**	19.6	16.0
HM Treasury PIK interest	See below	See below	2013	NRAM	**-**	**-**	150.9	150.7
Tier one notes	7.053%	2027	Undated	NRAM	**42.1**	**30.5**	42.5	30.5
Total					**215.3**	**169.1**	359.2	329.1

The capital instruments are all denominated in sterling.

The carrying values of these instruments are on an EIR basis which takes into account issue costs. Carrying values include hedge accounting adjustments.

The 11.734% subordinated loan 2016 is repayable in five equal annual instalments from 2012 to 2016.

The HM Treasury PIK interest represented the amount of margin payable to HM Treasury which was subordinated under the terms of the facility (see note 23). This amount was repaid on 1 April 2013. Interest was payable on this loan at a floating rate above the Bank Base Rate.

The tier one notes carry a coupon of 7.053% payable annually in arrears on 21 September.

Since mid-June 2009, the B&B Board have deferred payment of all principal and coupons in respect of B&B's capital instruments. Each decision was taken on a case-by-case basis until 23 February 2010. Following the Board meeting of 23 February 2010, the B&B Group announced that it had resolved not to make any payment of principal or interest in respect of the B&B Group's capital instruments, as listed in the table above, during the period prior to the date on which it repays in full the Statutory Debt described in note 23. This Board decision followed the notification to the B&B Group on 25 January 2010 of the EC's approval of State Aid. The EC's decision set various conditions on the B&B Group receiving State Aid, one of which was that the B&B Group should not make payments of principal or interest on its capital instruments during the period prior to the date on which it repays in full the Statutory Debt.

As a consequence of the announcement of 23 February 2010, the carrying value of B&B's capital instruments was reduced by £104.3m, with an equal gain being recognised in the Income Statement, to reflect the revised present value of the new expected cash flows of these instruments. Following this reduction, for accounting purposes the interest (including unwind of the reduction in carrying value) accrues on the reduced liabilities on an EIR basis at the original EIR of the liability, such that the carrying value will ultimately accrete up to principal plus interest due. For capital instruments where interest is compound, the interest accrual also takes into account interest on the deferred coupons on an EIR basis.

As detailed in note 8, in 2013/14 and 2012 the Group bought back certain of its capital instruments.

Redemptions of any capital instruments prior to their final maturity date are subject to obtaining prior consent of the FCA.

The rights of repayment of holders of capital instruments are subordinated to the claims of other creditors.

Further details of capital instruments are provided in the Annual Reports and Accounts of B&B and NRAM, copies of which are available on the corporate website of each of these companies.

28. Share capital

Group and Company	25p Ordinary shares Number	25p Preference shares Number	25p Ordinary shares £	25p Preference shares £	Total share capital £
At 1 January 2012, 31 December 2012 and 31 March 2014	**4,955,595**	**4,000**	**1,238,899**	**1,000**	**1,239,899**

In accordance with the Companies Act 2006, the Company does not have authorised capital other than its issued capital.

The Ordinary shares rank equally in respect of rights attached to voting, dividends and in the event of a winding up.

Dividends on Preference shares are discretionary and, subject to Board approval, are payable annually on 4 July at a rate of 6.8509% based on a principal amount of £1,000 per share.

No dividends were declared or paid in 2013/14 or 2012 on the Company's Ordinary or Preference shares.

29. Reserves

Reserves comprise the following:

	At 31 Mar 2014 £m	At 31 Dec 2012 £m
Available-for-sale reserve	**(3.4)**	(53.4)
Cash flow hedge reserve	**194.0**	250.1
Merger reserve	**1,122.6**	1,122.6
Total	**1,313.2**	1,319.3

Available-for-sale reserve

	31 Mar 2014 £m	31 Dec 2012 £m
At start of period	**(53.4)**	(106.9)
Amounts recognised in equity	**51.5**	55.2
Amounts transferred to net income	**(1.5)**	(1.7)
At end of period	**(3.4)**	(53.4)

The available-for-sale reserve represents cumulative fair value movements on assets classified as available-for-sale.

Cash flow hedge reserve

	31 Mar 2014 £m	31 Dec 2012 £m
At start of period	**250.1**	210.4
Amounts recognised in equity	**(270.4)**	(589.8)
Amounts transferred to net income	**214.3**	629.5
At end of period	**194.0**	250.1

The cash flow hedge reserve represents cumulative fair value movements on financial instruments which are effective cash flow hedges.

Merger reserve

	31 Mar 2014 £m	31 Dec 2012 £m
At start and end of period	**1,122.6**	1,122.6
Generated on acquisition of B&B	**589.3**	589.3
Generated on acquisition of NRAM	**533.3**	533.3
Total	**1,122.6**	1,122.6

The merger reserve was generated on 1 October 2010 when the Company acquired all the issued shares of B&B and NRAM from the Treasury Solicitor via a share-for-share exchange. The merger reserve represents the difference between the value attributed to the Company's investment in each company and the capital and non-distributable reserves of the acquired groups.

30. Release of time-expired provision for unclaimed shares

Following demutualisation of Bradford & Bingley Building Society in 2000, a number of shares in B&B were unclaimed as the Registered Holders could not be traced. In accordance with B&B's Articles of Association, these shares were sold in March 2004 and the proceeds held by B&B for a further period of nine years to satisfy any claims received from the Registered Holders who were originally entitled to the shares. During the period from demutualisation to 31 March 2013, B&B sought periodically to trace the Registered Holders. The Registered Holders' entitlement to the proceeds of the sale of the unclaimed shares expired in March 2013 and the remaining provision of £13.2m was, therefore, released to retained earnings during the latest financial period.

31. Non-shareholders' funds

In accordance with the requirements of IAS 32, the following instruments are classified as equity:

	31 Mar 2014 £m	31 Dec 2012 £m
Reserve capital instruments	**101.4**	101.4
Subordinated notes	**23.4**	23.4
	124.8	124.8
Withheld coupons (see note 31(c) below)	**71.8**	53.8
Total non-shareholders' funds	**196.6**	178.6

(a) Reserve capital instruments

Reserve capital instruments were issued by NRAM for a value of £200.0m in September 2000 and for £100.0m in May 2001 and are undated. They carry a coupon of 8.399% payable annually in arrears on 21 September. At each payment date NRAM will decide whether to declare or defer the coupon. If NRAM decides to declare the coupon, the holder will receive a cash payment equivalent to the coupon which will be achieved either by the payment of cash directly, or while NRAM is in public ownership, as per the terms of Article 5 of The Northern Rock Transfer Order 2008 (the 'Transfer Order') which was made on 21 February 2008 pursuant to the Banking (Special Provisions) Act 2008. If NRAM elects to defer the coupon, it may not declare or pay a dividend on any share until the deferred coupons are satisfied. While NRAM is in public ownership, deferred coupons and any interest accruing thereon can only be satisfied in accordance with the terms of Article 5 of the Transfer Order.

NRAM has a call option in September 2015 which it can only exercise with the consent of the FCA. If the issue is not called, the coupon resets to yield 4.725% above the prevailing 5-year benchmark Gilt rate.

As detailed in note 8, in 2012 the Group bought back certain of its reserve capital instruments.

The reserve capital instruments are denominated in sterling.

(b) Subordinated notes

	Interest rate	Terms	Denomination	At 31 Mar 2014 £m	At 31 Dec 2012 £m
Perpetual subordinated notes	12.625%	Not redeemable	Sterling	**13.5**	13.5
Perpetual fixed to floating rate subordinated notes	6.594%	Not redeemable before 28/06/17	US$	**1.2**	1.2
Undated subordinated notes	5.60%	Not redeemable before 30/04/14	US$	**8.7**	8.7
Total				**23.4**	23.4

Redemptions of any subordinated notes are at the issuer's option only and are subject to obtaining the prior consent of the FCA.

The rights of repayment of holders of subordinated notes are subordinated to the claims of other creditors.

(c) Appropriations

Coupons on non-shareholders' funds are treated as appropriations.

One of the conditions resulting from NRAM's State Aid approval in October 2009 requires NRAM to withhold coupon payments on all subordinated instruments where possible. Consequently no appropriations have been made in respect of NRAM's reserve capital instruments or subordinated notes during 2013/14 (2012: £nil).

In the table above, the cumulative amount of withheld coupons is presented as part of non-shareholders' funds. This is a change in presentation compared to the 2012 Annual Report and Accounts.

32. Off-Balance Sheet commitments

(a) Commitments payable

At 31 March 2014	Within one year £m	In one to five years £m	Over five years £m	Total £m
Loan commitments:				
– lifetime mortgages	0.8	2.8	4.5	8.1
– other loans	1,749.2	-	-	1,749.2
Total loan commitments	1,750.0	2.8	4.5	1,757.3
Operating lease commitments:				
– land and buildings	1.1	4.0	8.5	13.6
Capital commitments	0.7	-	-	0.7
Total	**1,751.8**	**6.8**	**13.0**	**1,771.6**

At 31 December 2012	Within one year £m	In one to five years £m	Over five years £m	Total £m
Loan commitments:				
– lifetime mortgages	1.0	3.4	6.2	10.6
– other loans	1,967.3	-	-	1,967.3
Total loan commitments	1,968.3	3.4	6.2	1,977.9
Operating lease commitments:				
– land and buildings	0.2	0.6	0.1	0.9
Capital commitments	2.8	-	-	2.8
Total	1,971.3	4.0	6.3	1,981.6

Loan commitments represent contractual amounts to which the Group is committed for extension of credit to customers. In respect of lifetime mortgages, the commitment reflects estimates of future drawdowns. On other loans, the commitment comprises cash which could be drawn down by customers in respect of further advances and re-drawal of amounts voluntarily overpaid.

Operating lease commitments represent minimum future lease payments under non-cancellable operating leases.

Capital commitments represent contractual amounts to which the Group is committed in respect of IT infrastructure investment.

(b) Commitments receivable

The Group had no commitments receivable at 31 March 2014.

At 31 December 2012	Within one year £m	In one to five years £m	Over five years £m	Total £m
Operating lease commitments:				
– land and buildings	-	0.1	-	0.1
Total	-	0.1	-	0.1

Operating lease commitments represent minimum future lease payments receivable under non-cancellable operating leases.

33. Related party disclosures

(a) Key management personnel

The Group considers the Boards of Directors and the members of the Executive Committees of UKAR, B&B and NRAM to be the key management personnel. There were no amounts owed to or by key management personnel at any time during the period (2012: £nil).

A summary of the Group's remuneration of the 16 (2012: 16) key management personnel is set out in the table below. These amounts include the remuneration of the Directors which is set out in more detail in the Directors' Remuneration Report on pages 22 to 32. The Directors' Remuneration Report gives details of the UKAR Group's Directors' salaries, fees, bonuses, pension benefits, other incentives and other benefits.

Remuneration of key management personnel	15 months to 31 Mar 2014 £000	12 months to 31 Dec 2012 £000
Short-term employee benefits	4,333	3,240
Post-employment benefits	370	293
Termination benefits	-	103
Total	4,703	3,636

Further details of the accounting treatment of pensions and of the Group's and Company's transactions and balances with the Group's pension schemes are given in note 18. There were no amounts due to or from the schemes at 31 March 2014 (31 December 2012: £nil). The key management personnel contributed £35,000 (2012: £59,000) to Group pension schemes during the period.

Included in the Group's Income Statement, the aggregate Directors' emoluments and the emoluments of the highest paid Director amounted to £1,952,323 and £980,771 respectively (2012: £1,680,357 and £642,820 respectively). Included in these amounts are £36,256 (2012: £37,781) which the Group paid into the Group's money purchase pension scheme. In addition, Directors paid £7,251 (2012: £18,891) into this scheme.

(b) UK government

As described in note I to the Parent Company Financial Statements, the Company considers the UK government to be its ultimate controlling party. The Group's material balances with departments and bodies of the government comprise deposits with the Bank of England (see note 10), loans from HM Treasury (see note 23), the Statutory Debt (see note 23) and UK government securities held. HM Treasury has also provided guarantee arrangements to the Group, for which the Group pays fees (see note 3). In addition to these loans and guarantees, the Group has balances and transactions with numerous government bodies on an arm's length basis in relation to the payment of corporation tax, VAT and employee taxes, and the payment of regulatory fees and levies.

(c) UKAR Company

The UKAR Company's balances and transactions with related parties are detailed in note G to the Parent Company Financial Statements.

34. Capital structure

The UK financial regulator the FCA regulates three of the Company's principal subsidiaries, B&B, NRAM and Mortgage Express, under the MIPRU regime which applies to mortgage administration companies. Each of these companies manages its capital resources in order to meet the FCA's regulatory requirements. Capital adequacy is monitored on an ongoing basis by the Group's executive management and Board based on the regulations established by the FCA. Each of these three companies met its capital requirements in full throughout 2013/14 and 2012; further information is available in the Annual Reports and Accounts of each company, which do not form part of these Financial Statements. The Board considers core equity, formerly Tier 1 capital, to be of pre-eminent importance in the capital structure of the regulated companies and continues to monitor this closely in addition to the total level of capital. The Directors believe that each regulated Group company has an appropriate and adequate level of capital to support its activities, subject to the continuing support of HM Treasury. Strictly, the regulated companies within the Group are required to hold capital in excess of 1% of total Balance Sheet assets plus any undrawn commitments. However, the Board believes they should hold capital above 1% and as at 31 March 2014, capital in B&B represented 6.6% of B&B assets and NRAM capital represented 8.8% of NRAM assets.

The primary objectives of the Group's capital management are to maintain capital resources to support the objectives of the business, to cover risks inherent in its activities and to ensure compliance with externally imposed capital requirements. The capital structure is managed in response to changes in the nature of the Group's activities and economic conditions.

The Group defines equity and certain other capital instruments as capital. Capital excludes accounting reserves for available-for-sale assets and cash flow hedges. The Group's capital adequacy and capital resources are managed and monitored in accordance with the regulatory capital rules of the FCA. The Group must at all times monitor and demonstrate compliance with the relevant regulatory capital requirements of the FCA. The required capital information is filed with the FCA on a quarterly basis.

35. Financial instruments

(a) Categories of financial assets and financial liabilities: carrying value compared to fair value

The following table summarises the carrying amounts and fair values of financial assets and liabilities. Assets are generally presented at bid prices, whereas offer prices are used for liabilities. The accounting policy note 1(g) sets out the key principles used for estimating the fair values of financial instruments. This note provides some additional information in respect of the methodologies used.

At 31 March 2014	Available – for-sale £m	Assets at fair value through profit or loss £m	Loans and receivables £m	Hedging adjustments £m	Total carrying value £m	Fair value £m
Financial assets:						
Balances with the Bank of England	-	-	5,020.3	-	5,020.3	5,020.3
Cash at bank and in hand	-	-	2,503.2	-	2,503.2	2,503.2
Investment securities	317.2	-	753.4	4.1	1,074.7	1,095.1
Loans to customers	-	-	61,247.3	2.2	61,249.5	57,354.6
Fair value adjustments on portfolio hedging	-	-	-	308.8	308.8	-
Derivative financial instruments	-	4,616.2	-	-	4,616.2	4,616.2
Other financial assets	-	-	29.9	-	29.9	29.9
Total financial assets	**317.2**	**4,616.2**	**69,554.1**	**315.1**	**74,802.6**	**70,619.3**

	Liabilities at fair value through profit or loss £m	Liabilities at amortised cost £m	Hedging adjustments £m	Total carrying value £m	Fair value £m
Financial liabilities:					
Amounts due to banks	-	3,119.2	-	3,119.2	3,119.2
Statutory Debt and HM Treasury loans	-	38,350.5	-	38,350.5	38,350.5
Derivative financial instruments	446.0	-	-	446.0	446.0
Debt securities in issue	-	25,250.4	635.6	25,886.0	27,063.4
Capital instruments	-	202.5	12.8	215.3	189.9
Other financial liabilities	-	126.1	-	126.1	126.1
Total financial liabilities	**446.0**	**67,048.7**	**648.4**	**68,143.1**	**69,295.1**

At 31 December 2012	Available – for-sale £m	Assets at fair value through profit or loss £m	Loans and receivables £m	Hedging adjustments £m	Total carrying value £m	Fair value £m
Financial assets:						
Balances with the Bank of England	-	-	5,599.8	-	5,599.8	5,599.8
Cash at bank and in hand	-	-	4,129.2	-	4,129.2	4,129.2
Investment securities	623.2	-	1,414.4	12.3	2,049.9	2,007.3
Loans to customers	-	-	68,729.7	3.9	68,733.6	64,419.7
Fair value adjustments on portfolio hedging	-	-	-	493.8	493.8	-
Derivative financial instruments	-	5,720.2	-	-	5,720.2	5,720.2
Other financial assets	-	-	33.4	-	33.4	33.4
Total financial assets	623.2	5,720.2	79,906.5	510.0	86,759.9	81,909.6

35. Financial instruments (continued)

(a) Categories of financial assets and financial liabilities: carrying value compared to fair value (continued)

	Liabilities at fair value through profit or loss £m	Liabilities at amortised cost £m	Hedging adjustments £m	Total carrying value £m	Fair value £m
Financial liabilities:					
Amounts due to banks	-	4,794.9	-	4,794.9	4,794.9
Statutory Debt and HM Treasury loans	-	43,487.3	-	43,487.3	43,487.3
Derivative financial instruments	783.7	-	-	783.7	783.7
Debt securities in issue	-	30,729.0	891.1	31,620.1	30,011.3
Capital instruments	-	342.8	16.4	359.2	263.0
Other financial liabilities	-	125.4	-	125.4	125.4
Total financial liabilities	783.7	79,479.4	907.5	81,170.6	79,465.6

Note: Other than loans to customers, the fair values above as at 31 December 2012 have not been restated to comply with IFRS 13. However, any differences between the fair values above and IFRS 13-compliant fair values would not be material. The methodology for calculating the fair value of loans to customers has been revised since 2012 and the 2012 fair value has been changed from that disclosed in the 2012 Annual Report and Accounts.

No financial assets or liabilities were reclassified during the period between amortised cost and fair value categories (2012: none).

At 31 March 2014 assets carried by NRAM at amortised cost which were previously carried at fair value were carried at £653.4m (31 December 2012: £1,243.9m). The difference between the carrying value at the date of reclassification and the expected value at the redemption date is recognised in profit and loss on an effective interest rate basis over the expected lives of the assets; their carrying amounts will accrete up to their redemption amounts over their expected lives. The amount recognised in profit and loss during the period was a loss of £55.8m (2012: gain of £67.8m) which was exactly offset by losses transferred from the available-for-sale reserve during the period. If the assets had not been reclassified, it is estimated that fair value gains of £160.4m would have been reflected in the available-for-sale reserve during 2013/14 in respect of these assets (2012: gains of £195.4m). The expected redemption value of the remaining assets is £833.7m (2012: £1,442.9m). The fair value of these assets at 31 March 2014 was £731.4m (31 December 2012: £1,182.1m).

Valuation methods for calculations of fair values in the table above are set out in note 35(e).

(b) Interest income and expense on financial instruments that are not at fair value through profit or loss

	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Interest income	**3,092.7**	2,876.2
Interest expense	**(1,428.7)**	(1,458.7)
Net interest income	**1,664.0**	1,417.5

These amounts represent interest income and expense before hedging arrangements.

(c) Impaired financial assets

Allowance accounts for credit losses in respect of impairment of loans to customers are detailed in note 14 and in respect of investment securities in note 12. No impairment loss has been recognised in respect of any other class of financial asset, and no other class of financial asset includes assets that are past due.

(d) Hedge accounting

Strategy in using derivative financial instruments

The Board has authorised the use of derivative instruments for the purpose of supporting the strategic and operational business activities of the Group and reducing the risk of loss arising from changes in interest rates and exchange rates. All use of derivative instruments within the Group is to hedge risk exposure, and the Group takes no trading positions in derivatives.

The objective when using any derivative instrument is to ensure that the risk-to-reward profile of any transaction is optimised. The intention is only to use derivatives to create economically effective hedges. However IAS 39 requires certain tests to be satisfied before hedge accounting is permitted. Consequently not all economic hedges are designated as accounting hedges, either because natural accounting offsets are expected or because obtaining hedge accounting would be especially onerous.

35. Financial instruments (continued)

(d) Hedge accounting (continued)

(i) Fair value hedges

The Group designates a number of derivatives as fair value hedges. In particular, the Group has three approaches establishing relationships for:

- Hedging the interest rate and foreign currency exchange rate risk of non-prepayable, foreign currency denominated fixed rate assets or liabilities on a one-for-one basis with fixed/floating or floating/fixed cross currency interest rate swaps.
- Hedging the interest rate risk of a single currency portfolio of sterling, US Dollar or Euro non-prepayable fixed rate assets/liabilities on a one-for-one basis with vanilla fixed/floating or floating/fixed interest rate swaps.
- Hedging the interest rate risk of a portfolio of prepayable fixed rate assets with interest rate derivatives. This solution is used to establish a macro fair value hedge for derivatives hedging fixed rate mortgages. The Group believes this solution is consistent with its policy for hedging fixed rate mortgages on an economic basis.

(ii) Cash flow hedges

The Group designates a number of derivatives as cash flow hedges. In particular, the Group adopts the following approaches:

- Using fixed interest rate swaps to hedge floating rate sterling liabilities.
- To address the volatility generated by floating/floating cross currency swaps, they are placed into cash flow hedges; the accounting hedge relationship is to hedge the foreign currency exchange rate risk of the foreign currency denominated asset/liability.
- Fixed/floating cross currency swaps are split into their separate risk components and separately designated into cash flow hedges.
- Basis swaps are split into their separate risk components and separately designated into cash flow hedges.

(iii) Net investment hedges

The Group has not designated any derivatives as net investment hedges in 2013/14 or 2012.

The Group had the following types of hedges:

At 31 March 2014	Fair value hedges £m	Cash flow hedges £m	Economic hedges £m	Total £m	Nominal amounts £m
Exchange rate contracts	4.6	4,603.1	1.6	4,609.3	17,432.4
Interest rate contracts	2.1	1.4	3.4	6.9	6,677.5
Total asset balances	**6.7**	**4,604.5**	**5.0**	**4,616.2**	
Exchange rate contracts	-	7.0	22.6	29.6	1,421.0
Interest rate contracts	320.8	80.0	15.6	416.4	22,199.0
Total liability balances	**320.8**	**87.0**	**38.2**	**446.0**	
Fair value of hedging instruments	**(314.1)**	**4,517.5**	**(33.2)**	**4,170.2**	

At 31 December 2012	Fair value hedges £m	Cash flow hedges £m	Economic hedges £m	Total £m	Nominal amounts £m
Exchange rate contracts	6.5	5,674.9	18.5	5,699.9	22,646.7
Interest rate contracts	11.8	1.6	6.9	20.3	4,016.1
Total asset balances	18.3	5,676.5	25.4	5,720.2	
Exchange rate contracts	-	3.9	7.1	11.0	723.1
Interest rate contracts	531.0	180.1	61.6	772.7	26,429.8
Total liability balances	531.0	184.0	68.7	783.7	
Fair value of hedging instruments	(512.7)	5,492.5	(43.3)	4,936.5	

35. Financial instruments (continued)

(e) Fair value measurement

Financial assets and liabilities carried at fair value are valued on the following bases:

At 31 March 2014	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets:				
Investment securities – available-for-sale	**106.3**	**215.0**	**-**	**321.3**
Derivative financial instruments	**-**	**4,616.2**	**-**	**4,616.2**
Financial liabilities:				
Derivative financial instruments	**-**	**(446.0)**	**-**	**(446.0)**
Net financial assets	**106.3**	**4,385.2**	**-**	**4,491.5**

At 31 December 2012	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets:				
Investment securities – available-for-sale	224.7	410.8	-	635.5
Derivative financial instruments	-	5,720.2	-	5,720.2
Financial liabilities:				
Derivative financial instruments	-	(783.7)	-	(783.7)
Net financial assets	224.7	5,347.3	-	5,572.0

Level 1: Quoted prices (unadjusted) in active markets for identical assets and liabilities.

Level 2: Inputs other than quoted prices that are observable for the asset or liability, whether directly (ie as price) or indirectly (ie derived from the implications of prices).

Level 3: Inputs for the asset or liability that are not based on observable market data, or have significant unobservable inputs.

Instruments which had been disclosed as 'Level 3' at 31 December 2012 have been recategorised as 'Level 2' as the unobservable inputs have been assessed to be insignificant.

There were no transfers between Level 1 and Level 2 during the period (2012: none).

Available-for-sale investment securities which are categorised as Level 1 are valued based on quoted market prices.

Available-for-sale investment securities which are categorised as Level 2 are those which are less frequently traded, hence trade prices are not considered sufficient evidence of fair value. Fair value is estimated by the securities' lead managers, taking into account recent trades, similar assets adjusted for credit spreads and where applicable the underlying performance of assets backing the securities; unobservable inputs are not considered significant.

Derivative financial instruments which are categorised as Level 2 are those which either:

(a) Have future cash flows which are on known dates and for which the cash flow amounts are known or calculable by reference to observable interest and foreign currency exchange rates; or

(b) Have future cash flows which are not pre-defined, but for which the fair value of the instrument has very low sensitivity to unobservable inputs.

In each case the fair value is calculated by discounting future cash flows using observable market parameters including swap rates, interest rates and currency rates.

35. Financial instruments (continued)

(e) Fair value measurement (continued)

For financial assets and liabilities which are not carried at fair value, the fair values disclosed in note 35(a) are calculated on the following bases:

At 31 March 2014	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets:				
Balances with the Bank of England	**5,020.3**	**-**	**-**	**5,020.3**
Cash at bank and in hand	**2,503.2**	**-**	**-**	**2,503.2**
Investment securities	**-**	**773.8**	**-**	**773.8**
Loans to customers	**-**	**-**	**57,354.6**	**57,354.6**
Other financial assets	**-**	**29.9**	**-**	**29.9**
	7,523.5	**803.7**	**57,354.6**	**65,681.8**
Financial liabilities:				
Amounts due to banks	**3,119.2**	**-**	**-**	**3,119.2**
Statutory debt and HM Treasury loans	**38,350.5**	**-**	**-**	**38,350.5**
Debt securities in issue	**-**	**27,063.4**	**-**	**27,063.4**
Capital instruments	**-**	**189.9**	**-**	**189.9**
Other financial liabilities	**-**	**126.1**	**-**	**126.1**
	41,469.7	**27,379.4**	**-**	**68,849.1**

At 31 December 2012	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets:				
Balances with the Bank of England	5,599.8	-	-	5,599.8
Cash at bank and in hand	4,129.2	-	-	4,129.2
Investment securities	-	1,371.8	-	1,371.8
Loans to customers	-	-	64,419.7	64,419.7
Other financial assets	-	33.4	-	33.4
	9,729.0	1,405.2	64,419.7	75,553.9
Financial liabilities:				
Amounts due to banks	4,794.9	-	-	4,794.9
Statutory debt and HM Treasury loans	43,487.3	-	-	43,487.3
Debt securities in issue	-	30,011.3	-	30,011.3
Capital instruments	-	263.0	-	263.0
Other financial liabilities	-	125.4	-	125.4
	48,282.2	30,399.7	-	78,681.9

Valuation methods for calculations of fair values in the table above are as follows:

Balances with the Bank of England

Fair value approximates to carrying value because they have minimal credit losses and are either short term in nature or reprice frequently.

Cash at bank and in hand

Fair value is estimated by using discounted cash flows applying either market rates where practicable or rates offered by other financial institutions for accounts with similar characteristics. The fair value of floating rate placements, fixed rate placements with less than six months to maturity and overnight deposits is estimated to be their carrying amount.

Investment securities

The fair values of investment securities held as loans and receivables are based on quoted prices or lead manager prices where available or by using discounted cash flows applying independently sourced market parameters including interest rates and currency rates. The fair value of unsecured investment loans is based on prices supplied by third parties.

Loans to customers

Loans to customers include loans of varying rates and maturities. Fair value is estimated by discounting expected future cash flows using market interest rates. Expected future cash flows take account of estimated future losses. Market interest rates are based on current lending activity in the mortgage market. In respect of the majority of the Group's fixed interest rate loans, the change in interest rates since inception means that their fair value can vary significantly from their carrying value; however, as the Group's policy is to hedge fixed rate loans in respect of interest rate risk, the Group has no material exposure to this difference in fair value. The methodology for calculating the fair value has been revised since 2012 and the 2012 fair value disclosed has been changed from that disclosed in the 2012 Annual Report and Accounts.

35. Financial instruments (continued)

(e) Fair value measurement (continued)

Amounts due to banks

Fair values of deposit liabilities repayable on demand or with variable interest rates are considered to approximate to carrying value. The fair value of fixed interest deposits with less than six months to maturity is estimated to be their carrying amount. The fair value of all other deposit liabilities is estimated using discounted cash flows, applying independently sourced market parameters including interest rates and currency rates.

Statutory Debt and HM Treasury loans

The fair value is estimated to be the carrying amount as the interest rate charged varies in line with changes in market rates, or the loans are considered to be repayable on demand subject to timing of repayment of loans to customers.

Debt securities in issue and capital instruments

Fair values are based on quoted prices or lead manager prices where available, or by using discounted cash flows, applying independently sourced market parameters including interest rates and currency rates.

Other financial assets and liabilities

Fair value approximates to carrying value because the balances are short term in nature.

(f) Transferred financial assets

As set out in note 24, the Group has transferred financial assets (loans and receivables) to securitisation structures. The Group retains all of the risks and rewards associated with these loans and they are, therefore, retained on the Group's Balance Sheet.

The table below sets out the carrying values of the transferred assets and the associated liabilities. For securitisation structures, the associated liabilities represent the external notes in issue (see note 24). None of these notes have recourse to the transferred assets.

At 31 March 2014	**Transferred assets Carrying amount £m**	**Associated liabilities Carrying amount £m**
Loans to customers securitised	**40,570.3**	**25,342.5**

At 31 December 2012	Transferred assets Carrying amount £m	Associated liabilities Carrying amount £m
Loans to customers securitised	45,662.5	30,708.1

(g) Offsetting

No financial assets have been offset against financial liabilities. Balances which are subject to enforceable master netting arrangements or similar agreements are as follows:

At 31 March 2014	**Gross and net amounts, as reported on the Balance Sheet**	**Amounts available to be offset (but not offset on the Balance Sheet)**		**Net amounts after offsetting under IFRS 7**
		Master netting arrangements	**Financial collateral**	
	£m	**£m**	**£m**	**£m**
Derivative financial assets	**4,616.2**	**(33.0)**	**(2,734.6)**	**1,848.6**
Derivative financial liabilities	**(446.0)**	**33.0**	**394.4**	**(18.6)**
	4,170.2	**-**	**(2,340.2)**	**1,830.0**

At 31 December 2012	Gross and net amounts, as reported on the Balance Sheet	Amounts available to be offset (but not offset on the Balance Sheet)		Net amounts after offsetting under IFRS 7
		Master netting arrangements	Financial collateral	
	£m	£m	£m	£m
Derivative financial assets	5,720.2	(85.1)	(3,977.9)	1,657.2
Derivative financial liabilities	(783.7)	85.1	648.4	(50.2)
	4,936.5	-	(3,329.5)	1,607.0

36. Collateral pledged and received

	31 Mar 2014 £m	31 Dec 2012 £m
Cash collateral which the Group has provided in respect of derivative contracts	**414.8**	667.8
Total collateral pledged	**414.8**	667.8

	31 Mar 2014 £m	31 Dec 2012 £m
Cash collateral which the Group has received in respect of derivative contracts	**3,119.1**	4,754.0
Securities collateral held	**235.4**	4.7
Total collateral received	**3,354.5**	4,758.7

In addition to the collateral amounts shown above, certain loans to customers provide security in respect of securitised note and Covered Bond funding as detailed in note 24. These loans, and also cash collateral pledged shown above, are carried on the Balance Sheet. The liability to repay the cash collateral received is included within amounts due to banks in the Balance Sheet. In the absence of counterparty default, the Group has no right to sell or re-pledge the securities collateral received and, therefore, in accordance with the provisions of IAS 39 such securities are not recognised on the Balance Sheet.

37. Financial risk management

A description of the principal risks to which the Group is exposed is provided on pages 52 to 55 which form an integral part of the audited Financial Statements.

(a) Credit risk

Credit risk is the potential for financial loss caused by a party failing to meet an obligation as it becomes due. The Group considers its most significant credit risk to be the exposure to retail, commercial and wholesale counterparties failing to meet their obligations. As credit risk is the main risk to the Group, a credit risk framework has been established as part of the overall governance framework to measure, mitigate and manage credit risk within risk appetite. The Group closely monitors its credit risk against the Board's credit policies.

The maximum credit risk exposure at the Balance Sheet date before taking account of any collateral netting and other credit enhancements was as follows:

	At 31 Mar 2014 £m	At 31 Dec 2012 £m
On Balance Sheet:		
Balances with the Bank of England	**5,020.3**	5,599.8
Cash at bank and in hand	**2,503.2**	4,129.2
Investment securities	**1,074.7**	2,049.9
Loans to customers	**61,249.5**	68,733.6
Derivative financial instruments	**4,616.2**	5,720.2
Other financial assets	**29.9**	33.4
Total on Balance Sheet	**74,493.8**	86,266.1
Off Balance Sheet:		
Loan commitments (see note 32)	**1,757.3**	1,977.9

Loans to customers include loans which are secured on property. Additional information in respect of credit risk is provided in note 12 (for wholesale assets) and note 15 (for loans to customers).

The Board has approved a framework for maximum wholesale credit counterparty limits against which total wholesale credit exposures are continually monitored and controlled. The credit limit structure adopts a risk based matrix whereby lower rated counterparties are afforded lower overall levels of limit. Although publicly available ratings produced by rating agencies provide a useful guide to the creditworthiness of counterparties, an internal evaluation is also used in the limit assignment process. Counterparties are assigned maximum limits in accordance with the ratings matrix, based on the lowest rating afforded to any part of the counterparty group.

The Group has investments in a range of investment securities issued by government bodies and banks and in asset-backed securities, in both the UK and overseas. UK government securities, bank and supranational bonds comprise 10% (2012: 15%) of investment securities held. 39% (2012: 53%) of the asset-backed securities are backed by UK assets. Further details in respect of concentrations in the wholesale assets portfolio are given in note 12.

The Group operates primarily in the UK and adverse changes to the UK economy could impact all areas of the Group's business. Residential loans to customers are all secured on property in the UK. 39% (2012: 37%) of residential loans to customers are concentrated in the buy-to-let market; most of the remaining balances are secured on residential owner-occupied properties.

37. Financial risk management (continued)

(a) Credit risk (continued)

The residential loan book of £59.3bn (2012: £66.1bn) is geographically spread across the UK broadly in line with the country's housing stock. Consequently, there is a geographic concentration of mortgages secured on properties in London and the South-East representing 42% (2012: 42%) of the book.

Within the commercial mortgage portfolio and housing association loans there are 115 loans (2012: 147) totalling £0.6bn (2012: £0.8bn), with the largest 10 loans accounting for 65% (2012: 67%) of the portfolio. All of these loans are secured on commercial properties.

(b) Liquidity risk

The Group closely monitors its liquidity position against the Board's liquidity policy. Minimum and target liquidity levels are established through stress testing and cash flow forecasting, taking into consideration an assessment of any emerging and potentially extreme funding conditions.

The table below analyses the Group's financial assets and liabilities into relevant maturity groupings:

At 31 March 2014	On demand £m	Within three months £m	After three months but within six months £m	After six months but within one year £m	After one year but within five years £m	After five years £m	Total £m
Financial assets:							
Balances with the Bank of England	5,019.8	0.5	-	-	-	-	5,020.3
Cash at bank and in hand	2,503.1	0.1	-	-	-	-	2,503.2
Investment securities	-	38.9	40.3	32.2	98.8	864.5	1,074.7
Loans to customers	321.3	131.2	130.8	258.6	3,892.6	56,515.0	61,249.5
Fair value adjustments on portfolio hedging	-	2.5	3.0	6.5	38.7	258.1	308.8
Derivative financial instruments	-	13.4	3.0	6.9	1,968.2	2,624.7	4,616.2
Other financial assets	-	29.9	-	-	-	-	29.9
Total financial assets	7,844.2	216.5	177.1	304.2	5,998.3	60,262.3	74,802.6
Financial liabilities:							
Amounts due to banks	3,119.2	-	-	-	-	-	3,119.2
Statutory Debt and HM Treasury loans	38,326.4	24.1	-	-	-	-	38,350.5
Derivative financial instruments	-	11.0	6.7	10.8	104.9	312.6	446.0
Debt securities in issue	3.0	945.6	857.4	1,615.7	16,101.6	6,362.7	25,886.0
Capital instruments	-	-	-	4.7	9.5	201.1	215.3
Other financial liabilities	-	126.1	-	-	-	-	126.1
Total financial liabilities	41,448.6	1,106.8	864.1	1,631.2	16,216.0	6,876.4	68,143.1
Net liquidity gap	(33,604.4)	(890.3)	(687.0)	(1,327.0)	(10,217.7)	53,385.9	6,659.5

At 31 December 2012	On demand £m	Within three months £m	After three months but within six months £m	After six months but within one year £m	After one year but within five years £m	After five years £m	Total £m
Financial assets:							
Balances with the Bank of England	5,599.8	–	-	-	-	-	5,599.8
Cash at bank and in hand	2,685.7	1,443.5	-	-	-	-	4,129.2
Investment securities	-	91.5	82.0	45.6	627.4	1,203.4	2,049.9
Loans to customers	424.9	123.1	130.5	394.7	4,061.5	63,598.9	68,733.6
Fair value adjustments on portfolio hedging	-	10.5	20.0	26.1	146.9	290.3	493.8
Derivative financial instruments	-	400.6	147.4	210.5	3,242.3	1,719.4	5,720.2
Other financial assets	-	33.4	-	-	-	-	33.4
Total financial assets	8,710.4	2,102.6	379.9	676.9	8,078.1	66,812.0	86,759.9
Financial liabilities:							
Amounts due to banks	4,754.2	-	40.7	-	-	-	4,794.9
Statutory Debt and HM Treasury loans	43,487.3	-	-	-	-	-	43,487.3
Derivative financial instruments	-	13.4	7.0	22.9	257.2	483.2	783.7
Debt securities in issue	-	2,617.5	901.5	1,544.3	17,654.9	8,901.9	31,620.1
Capital instruments	-	0.2	150.7	5.5	14.7	188.1	359.2
Other financial liabilities	-	125.4	-	-	-	-	125.4
Total financial liabilities	48,241.5	2,756.5	1,099.9	1,572.7	17,926.8	9,573.2	81,170.6
Net liquidity gap	(39,531.1)	(653.9)	(720.0)	(895.8)	(9,848.7)	57,238.8	5,589.3

37. Financial risk management (continued)

(b) Liquidity risk (continued)

HM Treasury has indicated that it expects the loans and the WCF provided to the Group by HM Treasury and the Statutory Debt due to the FSCS to be repaid out of the cash flows generated by the Group during its wind-down. It is not possible to specify the contractual maturity dates of the loans to the Group from HM Treasury and from the FSCS and, therefore, they have been included in the table above as though repayable on demand.

Debt securities in issue include notes which securitise loans to customers through SPVs. These notes are repaid on a pass-through basis. In the above table, maturities of such notes are based on the expected repayment of notes which, in turn, are derived from the expected redemption profiles of securitised loans.

In the above table, where derivatives have been entered into to hedge mortgage backed securitised notes, the timings of derivative payments are based on the expected repayment dates of the hedged notes.

As described in note 27, B&B announced in 2010 that it had resolved not to make any payment of principal or interest in respect of capital instruments during the period prior to the date on which it repays in full the Statutory Debt. Given the uncertainty of the timing of this, the table above includes payments of principal and interest on capital instruments at the earliest date they would have become contractually payable as per the original terms, regardless of the announcement. Capital instruments include perpetual instruments as shown in note 27: the table above assumes these instruments will be redeemed on 31 December 2055.

Other assets and liabilities are included in the above table according to the earliest date that payment can be contractually demanded. It should be noted that many financial instruments are settled earlier than their contractual maturity date; in particular, many mortgage loans are repaid early, in full or in part.

Assets and liabilities with a remaining period to contractual maturity of within one year are classed as current and those with a remaining period of more than one year are classed as non-current. Non-financial assets and liabilities amount to £137.4m and £455.9m respectively (2012: £126.3m and £450.5m) of which £7.5m and £183.4m respectively are classed as current (2012: £7.3m and £64.1m) and £129.9m and £272.5m respectively are classed as non-current (2012: £119.0m and £386.4m).

Non-derivative cash flows

The table below analyses the Group's non-derivative cash flows payable into relevant periods. The assumptions used in the preparation of this table are consistent with those used in the maturity table on page 118. The amounts disclosed are the contractual undiscounted cash outflows. These differ from Balance Sheet values due to the effects of discounting on certain Balance Sheet items and due to the inclusion of contractual future interest flows.

At 31 March 2014	On demand £m	Within three months £m	After three months but within six months £m	After six months but within one year £m	After one year but within five years £m	After five years £m	Total £m
Financial liabilities:							
Amounts due to banks	**3,119.2**	**-**	**-**	**-**	**-**	**-**	**3,119.2**
Statutory Debt and HM Treasury loans	**38,326.4**	**24.1**	**-**	**-**	**-**	**-**	**38,350.5**
Debt securities in issue	**3.0**	**1,012.6**	**882.4**	**1,857.7**	**16,855.9**	**6,979.8**	**27,591.4**
Capital instruments	**-**	**1.1**	**3.3**	**4.5**	**17.7**	**629.4**	**656.0**
Other financial liabilities	**-**	**126.1**	**-**	**-**	**-**	**-**	**126.1**
Loan commitments	**1,749.2**	**0.2**	**0.2**	**0.4**	**2.8**	**4.5**	**1,757.3**
Total	**43,197.8**	**1,164.1**	**885.9**	**1,862.6**	**16,876.4**	**7,613.7**	**71,600.5**

At 31 December 2012	On demand £m	Within three months £m	After three months but within six months £m	After six months but within one year £m	After one year but within five years £m	After five years £m	Total £m
Financial liabilities:							
Amounts due to banks	4,754.2	-	40.7	-	-	-	4,794.9
Statutory Debt and HM Treasury loans	43,487.3	-	-	-	-	-	43,487.3
Debt securities in issue	-	2,642.9	1,016.5	1,707.7	18,678.5	9,239.4	33,285.0
Capital instruments	-	1.1	152.0	7.1	38.2	637.7	836.1
Other financial liabilities	-	125.4	-	-	-	-	125.4
Loan commitments	1,967.3	0.3	0.2	0.5	3.4	6.2	1,977.9
Total	50,208.8	2,769.7	1,209.4	1,715.3	18,720.1	9,883.3	84,506.6

37. Financial risk management (continued)

(b) Liquidity Risk (continued)

Derivative cash flows

The following table analyses cash outflows for the Group's derivative financial liabilities. The amounts are allocated into relevant periods using assumptions consistent with those used in the preparation of the maturity table on page 118.

At 31 March 2014	On demand £m	Within three months £m	After three months but within six months £m	After six months but within one year £m	After one year but within five years £m	After five years £m	Total £m
Derivative financial liabilities to be settled on a net basis	-	38.7	29.6	56.1	266.5	891.9	1,282.8
Derivative financial liabilities to be settled on a gross basis:							
– outflows	-	151.0	144.5	351.3	1,257.1	615.8	2,519.7
– inflows	-	(146.4)	(140.2)	(342.8)	(1,224.8)	(602.5)	(2,456.7)
Total	-	**43.3**	**33.9**	**64.6**	**298.8**	**905.2**	**1,345.8**

At 31 December 2012	On demand £m	Within three months £m	After three months but within six months £m	After six months but within one year £m	After one year but within five years £m	After five years £m	Total £m
Derivative financial liabilities to be settled on a net basis	-	51.5	50.2	88.3	406.8	976.8	1,573.6
Derivative financial liabilities to be settled on a gross basis:							
– outflows	-	80.3	6.9	13.6	135.6	101.0	337.4
– inflows	-	(79.4)	(6.8)	(13.4)	(134.7)	(98.6)	(332.9)
Total	-	52.4	50.3	88.5	407.7	979.2	1,578.1

(c) Market risk

The following table describes the significant activities that were undertaken by the Group prior to nationalisation and which currently give rise to financial or market risk, the potential consequences associated with such activities and the derivative instruments used by the Group to mitigate the risks arising.

Activity	Risk	Type of derivative instrument used
Legacy funding in sterling involving either fixed rate instruments or instruments with embedded options	Sensitivity to changes in interest rates	Interest rate swaps
Fixed and capped rate mortgages and legacy investments involving either fixed rate instruments or instruments with embedded options	Sensitivity to changes in interest rates	Interest rate swaps and options
Variable rate mortgage balances	Sensitivity to changes in interest rates	Interest rate swaps
Legacy investments and funding in foreign currencies	Sensitivity to changes in foreign currency exchange rates	Cross-currency interest rate swaps and foreign exchange contracts

Interest rate swaps:

The notional principal amounts of the outstanding interest rate swap contracts in Cash Flow Hedge Relationships ('CFHR') as at 31 March 2014 were £19.8bn (31 December 2012: £20.0bn).

Gains and losses recognised in the cash flow hedge reserve on interest rate swap contracts as at 31 March 2014 will be continually released to the Income Statement up until the maturity of the hedging instruments in 2022.

Cross currency swaps:

The notional principal amounts of the outstanding cross currency swaps in an eligible CFHR as at 31 March 2014 were £17.4bn (31 December 2012: £22.1bn).

The hedged transactions denominated in foreign currency are expected to mature at various intervals over the next 41 years. Gains and losses recognised in the cash flow hedge reserve on cross currency swap contracts as at 31 March 2014 will be released to the Income Statement during the periods in which the hedged transactions affect the Income Statement, the latest maturity of these transactions being in 2055.

The accounting policy for derivatives and hedge accounting is described in note 1 (i), and further details of hedge accounting are provided in note 35(d).

37. Financial risk management (continued)

(c) Market risk (continued)

Interest rate risk

Interest rate risk typically arises from mismatches between the repricing dates of interest-bearing assets and liabilities on the Group's Balance Sheet, and from the investment profile of the Group's capital and reserves. The Finance & Investment Director is responsible for managing this exposure within the risk exposure limits set out in the Market Risk policy, as approved by the Board. This policy sets out the nature of the market risks that may be taken along with aggregate risk limits and stipulates the procedures, instruments and controls to be used in managing market risk.

Market risk is the potential adverse change in income or net worth arising from movements in interest rates, exchange rates or other market prices. Effective identification and management of market risk is essential for maintaining stable net interest income.

The Group measures, monitors and controls the following interest rate risks and sensitivities:
- Mismatch risk
- Curve
- Prepayment risk
- Basis risk
- Reset risk

Exposures are reviewed as appropriate by senior management and the Board with a frequency between daily and monthly, related to the granularity of the position.

Interest rate risk exposure is predominantly managed through the use of interest rate derivatives, principally interest rate swaps. The Group also uses asset and liability positions to offset exposures naturally wherever possible to minimise the costs and risks of arranging transactions external to the Group.

Interest rate sensitivities are reported to ALCO monthly and are calculated using a range of interest rate scenarios, including non-parallel shifts in the yield curve. The main metrics used by management are:

(i) the change in value of the Group's net worth due to a notional 2% parallel move in market and base rates.

	31 Mar 2014 **£m**	At 31 Dec 2012 £m
2% increase	**(0.6)**	10.9
2% decrease	**1.4**	3.5

(ii) the sensitivity of the Group's interest margin over 12 months to a notional 2% parallel move in market and base rates.

	31 Mar 2014 **£m**	At 31 Dec 2012 £m
2% increase	**485.2**	491.0
2% decrease	**(126.0)**	(124.4)

Foreign currency risk

The Group's policy is to hedge all material foreign currency exposures by use of naturally offsetting foreign currency assets and liabilities or by the use of derivatives. Consequently, at 31 March 2014 and 31 December 2012 the Group had no net material exposure to foreign exchange rate fluctuations or changes in foreign currency interest rates. The impact on the Group's profit and equity of reasonably possible changes in exchange rates compared to actual rates would not have been material at 31 March 2014 or 31 December 2012.

The table below summarises the Group's exposure to foreign currency exchange rate risk at the Balance Sheet date. Included in the table are the Group's financial instruments, including those classified as equity, under the relevant currency headings. The amounts disclosed are the sterling equivalents of the notional amounts due on maturity, including interest accrued at the Balance Sheet date, less any impairment provisions.

37. Financial risk management (continued)

(c) Market risk (continued)

Foreign currency risk (continued)

At 31 March 2014	€ £m	$ £m	Other £m	Total £m
Financial assets:				
Cash at bank and in hand	**1,202.6**	**209.1**	**-**	**1,411.7**
Investment securities	**741.3**	**95.4**	**-**	**836.7**
Derivative financial instruments	**14,026.3**	**5,497.3**	**732.9**	**20,256.5**
Total financial assets	**15,970.2**	**5,801.8**	**732.9**	**22,504.9**
Financial liabilities:				
Amounts due to banks	**1,642.9**	**161.4**	**-**	**1,804.3**
Derivative financial instruments	**194.1**	**(89.4)**	**-**	**104.7**
Debt securities in issue	**14,148.3**	**5,707.4**	**732.9**	**20,588.6**
Total financial liabilities	**15,985.3**	**5,779.4**	**732.9**	**22,497.6**
Non-shareholders' funds	**-**	**10.4**	**-**	**10.4**
Total	**15,985.3**	**5,789.8**	**732.9**	**22,508.0**
Net currency gap	**(15.1)**	**12.0**	**-**	**(3.1)**

At 31 December 2012	€ £m	$ £m	Other £m	Total £m
Financial assets:				
Cash at bank and in hand	2,291.7	472.4	-	2,764.1
Investment securities	1,026.7	126.3	-	1,153.0
Derivative financial instruments	16,990.3	6,926.2	918.9	24,835.4
Total financial assets	20,308.7	7,524.9	918.9	28,752.5
Financial liabilities:				
Amounts due to banks	2,689.1	434.2	-	3,123.3
Derivative financial instruments	849.8	44.7	-	894.5
Debt securities in issue	16,758.2	7,002.7	919.3	24,680.2
Total financial liabilities	20,297.1	7,481.6	919.3	28,698.0
Non-shareholders' funds	-	10.7	-	10.7
Total	20,297.1	7,492.3	919.3	28,708.7
Net currency gap	11.6	32.6	(0.4)	43.8

38. Contingent liabilities

The Consumer Credit Act ('CCA') regulates certain classes of mortgages and loans including the majority of the unsecured element of NRAM's 'Together' mortgage portfolio. As detailed in the NRAM Group's 2012 Annual Report & Accounts, NRAM did not comply with the requirements of the CCA in respect of some documentation provided to certain customers with CCA regulated loans. NRAM, therefore, made provisions during 2012 and the current period for NRAM's best estimate of the cost of providing remediation to those customers (see note 26).

Where NRAM made unsecured loans for sums in excess of £25,000 prior to 6 April 2008, the documentation incorrectly stated that these loans were also regulated under the CCA. Having considered all the information available to us, including legal advice and favourable adjudications by the Financial Ombudsman Service, we are of the view that such loans are not covered by CCA regulation and, therefore, do not require remediation or a provision. However, to provide clarity for ourselves and our customers, NRAM has commenced declaratory proceedings in the High Court to determine whether customers who took out such loans are entitled to the same or similar rights and remedies as those customers who took out loans that were regulated under the CCA. We expect this clarity by 31 March 2015. If the Court makes a decision adverse to our position, then NRAM would consider the impact and could be liable for remediation to these customers. Any such remediation would be likely to be through adjustment to customer balances. The current exposure, as at 31 March 2014, resulting from this uncertainty, together with any other potential actions following a judgement, falls within a range up to an estimated maximum of £240m.

On 20 January 2009 a solicitor's letter was received notifying B&B and certain present and former B&B directors of a potential claim by former individual shareholders who subscribed for additional shares in the £401m rights issue approved on 17 July 2008. These former shareholders claim to have suffered loss through having been induced to subscribe for shares in the rights issue by allegedly materially misleading and/or incomplete statements made in the associated prospectus dated 24 June 2008 as revised and supplemented by the supplementary prospectus dated 11 July 2008. Should such a claim result in proceedings which are pursued through the courts and which succeed, the defendant directors and/or B&B could be liable in damages to certain former shareholders in B&B who subscribed for shares in the rights issue. In May 2009 B&B together with its legal advisors responded to the allegations raised. Nothing further was heard until 23 January 2012 when correspondence was received from the solicitors representing the former shareholders, to which B&B together with its legal advisors responded. This correspondence contained no further allegations or details of the former shareholders' potential claim. It is not possible at this stage to determine the outcome or timing of any conclusion to this matter. No provision has been made in respect of these allegations.

In July 2013 the Group completed the £400m sale of its standalone unsecured personal loan book, realising a profit on sale of £21.2m. Under the terms of the sale, the Group provided certain warranties. Any claim under the warranties must be made by 12 March 2015. The Group's maximum liability under these warranties is limited to £35m.

39. Events after the reporting period

On 15 May 2014 NRAM announced tender offers in respect of certain securities issued by Whinstone Capital Management Limited and Whinstone 2 Capital Management Limited. The tender process closed on 27 May 2014, resulting in the purchase of notes with a face value of £87.2m and €156.4m, for cash of £233.6m including costs, resulting in a loss of £19.6m.

Independent Auditors' report to the Members of UK Asset Resolution Limited

Report on the Financial Statements

Our opinion

In our opinion the Financial Statements, defined below:

- give a true and fair view of the state of the Company's affairs as at 31 March 2014 and of its result and cash flows for the period then ended;
- have been properly prepared in accordance with International Financial Reporting Standards ('IFRS') as adopted by the European Union; and;
- have been prepared in accordance with the requirements of the Companies Act 2006.

This opinion is to be read in the context of what we say in the remainder of this report.

What we have audited

The Financial Statements, which are prepared by UK Asset Resolution Limited, comprise:

- Company Balance Sheet as at 31 March 2014;
- Company Cash Flow Statement for the period then ended;
- Company Statement of Changes in Equity for the period then ended; and
- the notes to the Financial Statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in their preparation is applicable law and IFRS as adopted by the European Union.

In applying the financial reporting framework, the Directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Certain disclosures required by the financial reporting framework have been presented elsewhere in the Annual Report and Accounts (the 'Annual Report'), rather than in the notes to the Financial Statements. These are cross-referenced from the Financial Statements and are identified as audited.

What an audit of financial statements involves

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ('ISAs (UK & Ireland)'). An audit involves obtaining evidence about the amounts and disclosures in the Financial Statements sufficient to give reasonable assurance that the Financial Statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the Directors; and
- the overall presentation of the Financial Statements.

In addition, we read all the financial and non-financial information in the 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 other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Directors' Report for the financial period for which the Financial Statements are prepared is consistent with the Financial Statements.

Opinion on additional disclosures

Directors' Remuneration Report

The Company voluntarily prepares a Directors' Remuneration Report in accordance with the provisions of the Companies Act 2006. The Directors have requested that we audit the part of the Directors' Remuneration Report specified by the Companies Act 2006 to be audited as if the Company were a quoted company.

In our opinion the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

Independent Auditors' report to the Members of UK Asset Resolution Limited (continued)

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Financial Statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

Matter on which we have agreed to report by exception

Directors' remuneration

The Company voluntarily provides the disclosures relating to directors' remuneration required by the Listing Rules of the Financial Conduct Authority as if it were a premium listed company and the Directors have requested that we review the elements of the report to shareholders by the Board on directors' remuneration specified for auditor review by the Listing Rules. We have nothing to report having performed our review.

Other matter

We have reported separately on the Group Financial Statements of UK Asset Resolution Limited for the 15 month period ended 31 March 2014.

Responsibilities for the Financial Statements and the audit

Our responsibilities and those of the Directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 59, 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 ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's Members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Craig Gentle (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London

2 June 2014

Company Balance Sheet

	Note	31 Mar 2014 £m	31 Dec 2012 £m
Assets			
Investments in Group undertakings	E	**2,634.1**	2,634.1
Total assets		**2,634.1**	2,634.1
Equity			
Issued capital and reserves attributable to equity holder of the parent:			
– share capital	28	**1.2**	1.2
– merger reserve	F	**2,632.8**	2,632.8
– retained earnings		**0.1**	0.1
Share capital and reserves		**2,634.1**	2,634.1

The notes on pages 128 to 130 form an integral part of these Financial Statements.

The Financial Statements on pages 126 to 130 were approved by the Board of Directors on 2 June 2014 and signed on its behalf by:

Richard Banks
Chief Executive Officer

Richard Pym
Chairman

UK Asset Resolution Limited is registered in England and Wales under company number 07301961.

Company Statement of Changes in Equity

	Share capital £m	Merger reserve £m	Retained earnings £m	Total share capital and reserves £m
At 1 January 2012, 31 December 2012 and 31 March 2014	1.2	2,632.8	0.1	2,634.1

Company Cash Flow Statement

During the 15 month period ended 31 March 2014 and the comparative 12 month period ended 31 December 2012 the Company had no material cash flows or balances. Consequently no Cash Flow Statement has been presented.

The Company had no significant non-cash transactions during the period.

A. Principal accounting policies

The Company is a private limited company incorporated on 1 July 2010 and domiciled in the United Kingdom. The principal activity of the Company is to provide management services to its subsidiary undertakings. The Company applies the accounting policies of the UKAR Group, set out on pages 70 to 78, with the following additional item.

Investments in Group undertakings

In the Financial Statements of the UKAR Company, investments in Group undertakings are carried at cost less any impairment. UKAR's acquisition of the entire issued share capital of B&B and NRAM in a share-for-share exchange has been accounted for under 'predecessor accounting' and the cost of each of these investments has been deemed to be the net assets of the B&B company and the NRAM company at 30 June 2010. Investments are reviewed at each published Balance Sheet date for any indication of impairment. If there is indication of impairment of any investment, the carrying value of the investment is reviewed and any impairment identified is charged immediately to the Company's Income Statement.

B. Critical judgements and accounting estimates

In preparing the Financial Statements, management have made the following critical judgement.

Investments in Group undertakings

The Directors consider the value of the Company's investments in subsidiary undertakings to be supported by their underlying assets.

C. Profit

The Company's profit after tax for the period was £21,000 (31 December 2012: £23,000). As permitted by s408 of the Companies Act 2006 the Company's individual Income Statement, Statement of Comprehensive Income and related notes have not been presented.

D. Taxation

The Company bears tax at the standard weighted average rate of UK corporation tax of 23.2% (2012: 24.5%), and has no deferred tax provided or unprovided.

E. Investments in Group undertakings

The investments in Group undertakings represent the Company's holdings of the entire issued share capital of B&B and NRAM, which were acquired in a share-for-share exchange on 1 October 2010, and also of UKARcs which was incorporated on 20 June 2013.

The Company's principal subsidiary undertakings at 31 March 2014 held directly or indirectly, all of which are wholly owned and are fully consolidated into the Group Financial Statements, are listed below. All operate in their country of incorporation.

	Nature of business	Country of incorporation	Class of shares held
Direct			
Bradford & Bingley plc ('B&B')	Mortgage administration	UK	Ordinary
NRAM plc ('NRAM')	Mortgage administration	UK	Ordinary and preference
UKAR Corporate Services Limited ('UKARcs')	Administration	UK	Ordinary
Indirect			
Mortgage Express	Mortgage administration	UK	Ordinary

Further details of the subsidiaries of the B&B and NRAM companies, including their SPVs, are provided in the Annual Reports and Accounts of B&B and NRAM.

The Directors consider the value of investments in Group undertakings to be supported by their underlying assets.

SPVs

The following entities are SPVs established in connection with the Group's securitisation and secured funding programmes (see note 24). Although the Company has no direct or indirect ownership interest in these entities and no rights to vote or to receive dividends they are regarded as subsidiaries. This is because they are principally engaged in providing a source of long-term funding to the Group, which in substance has the rights to all benefits from the activities of the SPVs. They are, therefore, effectively controlled by the Group. B&B is a member of Bradford & Bingley Covered Bonds LLP and NRAM is a member of NRAM Covered Bond LLP.

E. Investments in Group undertakings (continued)

SPVs (continued)

	Nature of business	Country of incorporation
Aire Valley Mortgages 2004-1 plc	Issue of securitised notes	UK
Aire Valley Mortgages 2005-1 plc	Issue of securitised notes	UK
Aire Valley Mortgages 2006-1 plc	Issue of securitised notes	UK
Aire Valley Mortgages 2007-1 plc	Issue of securitised notes	UK
Aire Valley Mortgages 2007-2 plc	Issue of securitised notes	UK
Aire Valley Mortgages 2008-1 plc	Issue of securitised notes	UK
Bradford & Bingley Covered Bonds LLP	Mortgage funding	UK
Granite Mortgages 03-2 plc	Issue of securitised notes	UK
Granite Mortgages 03-3 plc	Issue of securitised notes	UK
Granite Mortgages 04-1 plc	Issue of securitised notes	UK
Granite Mortgages 04-2 plc	Issue of securitised notes	UK
Granite Mortgages 04-3 plc	Issue of securitised notes	UK
Granite Master Issuer plc	Issue of securitised notes	UK
Granite Finance Funding Limited	Holding company	Jersey
Granite Finance Funding 2 Limited	Holding company	UK
Whinstone Capital Management Limited	Issue of credit linked notes	Jersey
Whinstone 2 Capital Management Limited	Issue of credit linked notes	Jersey
NRAM Covered Bond LLP	Mortgage funding	UK

Summarised financial information for material SPVs

Set out below is summarised financial information for each material SPV:	Net assets		Profit after tax	
	At 31 Mar 2014 £m	At 31 Dec 2012 £m	15 months to 31 Mar 2014 £m	12 months to 31 Dec 2012 £m
Aire Valley Mortgages 2004-1 plc	**2.9**	4.1	**(1.2)**	(6.3)
Aire Valley Mortgages 2005-1 plc	**0.8**	1.2	**0.4**	(3.6)
Aire Valley Mortgages 2006-1 plc	**13.9**	12.0	**1.9**	(14.7)
Aire Valley Mortgages 2007-1 plc	**3.0**	2.6	**0.4**	(8.0)
Granite Mortgages 03-2 plc	**1.3**	1.5	**(0.2)**	(3.0)
Granite Mortgages 03-3 plc	**0.3**	(0.1)	**0.4**	(2.0)
Granite Mortgages 04-1 plc	**1.1**	1.3	**(0.2)**	(4.5)
Granite Mortgages 04-2 plc	**0.2**	0.4	**(0.2)**	(3.2)
Granite Mortgages 04-3 plc	**0.5**	0.6	**(0.1)**	(2.4)
Granite Master Issuer plc	**(18.0)**	(6.3)	**(11.7)**	-
Granite Finance Funding Limited	**0.3**	0.3	**-**	-
Granite Finance Funding 2 Limited	**0.1**	0.1	**-**	-
Whinstone Capital Management Limited	**49.7**	68.6	**(18.9)**	3.4
Whinstone 2 Capital Management Limited	**45.7**	61.3	**(15.6)**	6.2

The Directors consider that to give full particulars of all subsidiaries would lead to a statement of excessive length. A full list of subsidiaries at 31 March 2014 will be annexed to the Company's next Annual Return to be filed at Companies House.

F. Merger reserve

	£m
At 1 January 2012, 31 December 2012 and 31 March 2014	**2,632.8**

The merger reserve was generated on 1 October 2010 when the Company acquired all the issued shares of B&B and NRAM from the Treasury Solicitor via a share-for-share exchange. The merger reserve represents the difference between the value attributed to the Company's investment in each company and the nominal value of the share capital issued by the Company in exchange.

G. Related party disclosures

(a) Subsidiary companies

The Company had no material balances outstanding with subsidiary companies during the period.

The Company had transactions with its subsidiaries as follows:

	15 months to 31 Mar 2014 £000	12 months to 31 Dec 2012 £000
Management charges to subsidiary undertakings	**827**	709
Costs recharged by subsidiary undertakings	**791**	678

(b) Key management personnel

The Group considers the Boards of Directors and the members of the Executive Committees of UKAR, B&B and NRAM to be the key management personnel. The Company had no transactions or balances directly with any key management personnel during the period. The Company's non-executive Directors have service contracts with the Company. Their fees are paid by B&B and recharged at cost to the Company, along with other related costs.

(c) Directors' emoluments

The aggregate UKAR Group emoluments of the Directors of the UKAR Company for the 15 months ended 31 March 2014 were £1,952,323 and of the highest paid Director £980,771 (31 December 2012: £1,680,357 and £642,820 respectively).

H. Financial risk management

The Company has no significant financial risks.

I. Ultimate controlling party

All shares in the Company are owned by the Treasury Solicitor as nominee for HM Treasury, and the Company considers the UK government to be its ultimate controlling party.

Unaudited Consolidated Income Statement

	12 months to 31 Mar 2014 £m	12 months to 31 Mar 2013 £m
Interest receivable and similar income	**2,291.5**	2,540.6
Interest expense and similar charges	**(822.3)**	(1,099.6)
Net interest income	**1,469.2**	1,441.0
Fee and commission income	**26.9**	26.1
Fee and commission expense	**(12.1)**	(12.2)
Net fee and commission income	**14.8**	13.9
Net realised gains less losses on investment securities	**(8.3)**	(18.1)
Unrealised fair value movements on financial instruments	**(33.3)**	4.7
Hedge ineffectiveness	**(18.2)**	(28.4)
Provision for customer redress	**(115.8)**	(419.0)
Other operating income	**10.6**	9.0
Non-interest income	**(150.2)**	(437.9)
Net operating income	**1,319.0**	1,003.1
Administrative expenses:		
– ongoing	**(189.8)**	(207.5)
– other net expenses	**-**	(59.7)
Impairment on loans to customers	**(46.6)**	(200.2)
Net impairment release on investment securities	**9.2**	35.5
Profit on sale of unsecured loans	**21.2**	-
Gain on repurchase of own liabilities	**-**	146.4
Profit before taxation	**1,113.0**	717.6
Taxation	**(243.3)**	(138.6)
Profit for the period	**869.7**	579.0

The unaudited information above has been prepared using accounting bases and policies which are consistent with those used in the audited Financial Statements set out on pages 65 to 123.

Reconciliation of underlying profit before taxation to statutory profit before taxation

	12 months to 31 Mar 2014 £m	12 months to 31 Mar 2013 £m
Net interest income	**1,469.2**	1,441.0
Underlying net non-interest income	**17.1**	4.8
Underlying net operating income	**1,486.3**	1,445.8
Ongoing administrative expenses	**(189.8)**	(207.5)
Impairment on loans to customers	**(46.6)**	(200.2)
Net impairment release on investment securities	**9.2**	35.5
Underlying profit before taxation	**1,259.1**	1,073.6
Unrealised fair value movements on financial instruments	**(33.3)**	4.7
Hedge ineffectiveness	**(18.2)**	(28.4)
Other net administrative expenses	**-**	(59.7)
Provision for customer redress	**(115.8)**	(419.0)
Profit on sale of unsecured loans	**21.2**	-
Gain on repurchase of own liabilities	**-**	146.4
Statutory profit before taxation	**1,113.0**	717.6

Unaudited Consolidated Balance Sheet

	31 March 2013 £m
Assets	
Balances with the Bank of England	5,629.5
Cash at bank and in hand	3,237.3
Investment securities	1,810.3
Loans to customers	67,542.3
Fair value adjustments on portfolio hedging	475.3
Derivative financial instruments	6,380.4
Other assets	68.9
Retirement benefit assets	64.2
Property, plant and equipment	27.5
Intangible assets	45.8
Total assets	85,281.5
Liabilities	
Amounts due to banks	4,824.9
Statutory Debt and HM Treasury loans	42,994.2
Derivative financial instruments	763.9
Debt securities in issue	30,277.0
Other liabilities	167.6
Current tax liabilities	120.6
Deferred tax liabilities	44.6
Retirement benefit obligations	72.3
Provisions	206.3
Capital instruments	357.3
Total liabilities	79,828.7
Equity	
Issued capital and reserves attributable to equity holder of the parent:	
– share capital	1.2
– reserves	1,308.8
– retained earnings	3,960.3
Share capital and reserves	5,270.3
Non-shareholders' funds	182.5
Total equity	5,452.8
Total equity and liabilities	85,281.5

The unaudited information above has been prepared using accounting bases and policies which are consistent with those used in the audited Financial Statements set out on pages 65 to 123.