The Co-operative Bank plc announces that the following document has today been submitted to the National Storage Mechanism and will shortly be available for inspection at www.hemscott.com/nsm.do:

- Annual Report and Accounts 2014.

A copy of the Annual Report and Accounts 2014, Pillar III Report 2014 and an investor presentation are available within the Investor Relations section of our website www.co-operativebank.co.uk/investorrelations.

This announcement also contains additional information for the purposes of compliance with the Disclosure and Transparency Rules, including a consolidated set of financial statements, principal risks and uncertainties, details of related party transactions and a responsibility statement. This information is extracted, in full unedited text, from the Annual Report and Accounts 2014. Reference to pages and numbers refer to page numbers and notes to the 2014 Annual Report and Accounts and all 2013 comparatives are as restated in those accounts.

Issued: 27 March 2015

Co-operative Bank Annual Report and Accounts for the full year ended 31 December 2014

Summary:

- Operating loss of £55.3m in 2014 (£662.0m in 2013) is a significant improvement due to reduced impairments partially offset by reduced income from lower assets and high project costs.
- Statutory loss before tax of £264.2m in 2014 considerably better than 2013 (£632.8m loss including LME gain of £688.3m).
- Capital position of the Bank strengthened following the capital raising and the capital injection from The Co-operative Group – Common Equity Tier 1 (CET1) of 13.0% at the end of 2014 (7.2% at the end of 2013).
- Total operating costs down to £594.6m for 2014 (£655.9m in 2013).
- Increase in project costs to £226.5m (£164.7m in 2013) due to the need to invest in systems, processes and platform.
- Performance of the Core Bank stabilised in the second half of 2014 – the number of primary current accounts stabilised and the mortgage pipeline is improved when compared to the early part of 2014.
- Total conduct and legal related charges, including PPI, £101.2m down from £411.5m in 2013.
- Non-core customer assets reduced to £10.3bn from £12.5bn at the end of 2013 (ahead of year-end target 2014 of £11.0bn) and resulting in a reduction of £1.4bn of Risk Weighted Assets (RWAs).
- Revised plan, as announced at time of Bank of England stress tests and accepted by the regulator, designed to deliver a business which can withstand a severe economic stress by 2019.
- Strategy remains unchanged – the only material development is the significant acceleration in the reduction of RWAs.
- Focus for management in 2015 continues to be the turnaround of the Bank, making it more resilient and implementing the revised plan accepted by the PRA in December with a view to building a profitable bank focussed on retail and SME customers over the longer term.

- Reinvestment in the brand commenced in the second half of 2014, with a new advertising campaign continuing in 2015.
- Expanded Ethical Policy launched in January 2015, based on views of over 74,000 customers and colleagues, will provide a guide to the way the Bank is run including its products and services.

Updates:

- The Board of The Co-operative Bank today announces that it has agreed an employment contract to retain the services of Chief Executive Niall Booker until 31 December 2016. Please refer to the separate RNS announcement of 27 March 2015 for further details.
- Further to the RNS announcement of 16 December 2014, The Co-operative Bank is considering various strategies to reduce its risk exposure to its Non-core residential mortgage portfolio (Optimum); these include the structuring of residential mortgage backed securities ('RMBS') focused on the sale of notes across the capital structure including junior tranches. Further updates regarding a potential transaction will follow.

Chief Executive Niall Booker said:

"Over the course of 2014 the management team has continued to take significant steps to implement the strategy and to turn the Bank around. The Co-operative Bank is stronger than a year ago and we end the year with a strengthened capital position, ahead of schedule in the reduction of Non-core assets and having made progress reducing underlying costs and improving the day-to-day management and governance. However, we are in the early stages of the turnaround and there is still much to do to transform the organisation into a sustainable business. There are a number of matters where the Bank does not yet meet FCA and PRA regulatory requirements and expectations. The revised plan, accepted by the regulators, seeks to address this.

Improving the resilience of the Bank remains key to delivering our revised plan. This will be primarily achieved through the further reduction of our Risk Weighted Assets and by improving the resilience of our IT infrastructure. These actions will continue to build a stronger and better business for all our stakeholders and are critical to providing the platform to focus on what matters to our customers. In the second half of 2014 we began to invest in the brand, to more actively market our products and also made a significant investment in our digital offering. The performance of the Core Bank has begun to stabilise, and we aim to build on this in 2015 by continuing to invest in our brand and developing our products guided by our expanded Ethical Policy.

We have always been clear that the journey to reshape the business would take time but I am confident that our approach to banking is as relevant in today's world as it ever was, and that we remain the bank of choice for anyone who shares the values and ethics which lie at the heart of our business."

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Forward looking statements

This document contains certain forward looking statements with respect to the business, strategy and plans of The Co-operative Bank and its current goals and expectations relating to its future financial condition and performance. Statements that are not historical facts, including statements about The Co-operative Bank's or its Directors' and/or management's beliefs and expectations, are forward looking statements. By their nature, forward looking statements involve risk and uncertainty because they relate to events and depend upon circumstances that will or may occur in the future. Factors that could cause actual business, strategy, plans and/or results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward looking statements made by the Bank or on its behalf include, but are not limited to: general economic and business conditions in the UK and internationally; inflation, deflation, interest rates and policies of the Bank of England, the European Central Bank and other G8 central banks; fluctuations in exchange rates, stock markets and currencies; changes to The Co-operative Bank's credit ratings; changing demographic developments, including mortality and changing customer behaviour, including consumer spending, saving and borrowing habits; changes in customer preferences; changes to borrower or counterparty credit quality; instability in the global financial markets, including Eurozone instability and the impact of any sovereign credit rating downgrade or other sovereign financial issues; technological changes; natural and other disasters, adverse weather and similar contingencies outside The Co-operative Bank's control; inadequate or failed internal or external processes, people and systems; terrorist acts and other acts of war or hostility and responses to those acts; geopolitical, pandemic or other such events; changes in laws, regulations, taxation, accounting standards or practices; regulatory capital or liquidity requirements and similar contingencies outside The Co-operative Bank's control; the policies and actions of governmental or regulatory authorities in the UK, the European Union, the US or elsewhere; the implementation of the EU Bank Recovery and Resolution Directive and banking reform, following the recommendations made by the Independent Commission on Banking; the ability to attract and retain senior management and other employees; the extent of any future impairment charges or write-downs caused by depressed asset valuations, market disruptions and illiquid markets; market relating trends and developments; exposure to regulatory scrutiny, legal proceedings, regulatory investigations or complaints; changes in competition and pricing environments; the inability to hedge certain risks economically; the adequacy of loss reserves; the actions of competitors, including non-bank financial services and lending companies; and the success of The Co-operative Bank in managing the risks of the foregoing.

The ability of the Bank to implement its revised plan and to achieve the results set out in the plan requires the regulators' continued acceptance of the plan and entails particular challenges including (but are not limited to): ability to execute a substantial re-engineering of the Bank's operating model and a very large and complex IT remediation programme; ability to achieve targeted cost savings; ability to retain customers and deposits; the timing and quantum of impacts to capital from the Bank's asset reduction exercise; meeting its planned improvements in net interest margin; a possible deterioration in the quality of the Bank's asset portfolio; unplanned costs from (for example) conduct risk matters; ability to maintain the Bank's access at an appropriate cost to liquidity and funding and the ability of the Bank to raise further capital assumed in its revised plan.

Any forward-looking statements made in this document speak only as of the date they are made and it should not be assumed that they have been revised or updated in the light of new information of future events. Except as required by the Prudential Regulation Authority, the Financial Conduct Authority, the London Stock Exchange plc or applicable law, The Co-operative Bank expressly disclaims any obligation or undertaking to release publicly any updates of revisions to any forward-looking statements contained in this document to reflect any change in The Co-operative Bank's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

Key highlights and outlook

Over 2014 the management team has continued to take significant steps in implementing the Bank's strategy and towards turning the Bank around

- The Bank's year end CET1 ratio stood at 13.0%. This follows the £400m capital raising in May 2014, the final £313m capital contribution from The Co-operative Group, the write back of credit impairment provisions on Non-core assets and the speed and timing of the deleverage of those assets.
- Good levels of liquidity were maintained during 2014.
- Bank continued to exceed its target for reductions in Non-core assets, from £12.5bn to £10.3bn at year end resulting in a corresponding reduction of £1.4bn of Risk Weighted Assets (RWAs).
- Progress made on improving day to day management, in beginning to embed cultural change across the organisation and in improving governance.
- Begun to reinvest in the Bank's brand, starting with an advertising campaign focused on the Bank's values and ethics, and the new Ethical Policy was announced in January 2015.

Statutory losses before taxation of £264.2m, considerably better than 2013 but the issues that came to light during 2013 continue to dominate the financial performance of the business

- Compares to a loss before taxation of £632.8m in 2013 driven by significant reductions in the level of credit and conduct related charges.
- Total conduct charges and legal related charges, including PPI, are down from £411.5m in 2013 to £101.2m in 2014 and predominantly comprise of £69.0m relating to previously identified breaches of the technical provisions of CCA and includes a provision of £17.4m separately provided for packaged accounts.
- The reduction in underlying costs has been offset by the need to increase specialist and temporary resource in the short to medium term to support the Bank's transformation and the necessary remediation of systems and processes.
- As a result of active management the net interest margin has increased year on year by 0.15% to 1.19% largely driven by the reduced cost of deposits.

As announced at time of Bank of England Stress tests, a revised plan (1) has been accepted by the regulator and runs until 2019

- Only material change from previously announced strategy is the planned significant acceleration of the reduction in Risk Weighted Assets (RWAs), primarily through reducing the Optimum portfolio, a closed book of residential mortgages, which is particularly susceptible to a severe economic stress.
- Whilst the Bank was temporarily compliant with Individual Capital Guidance (ICG) at the year end, as we have outlined previously, we only anticipate meeting ICG on a sustainable basis by the latter part of the planning period.
- Sale of Optimum has revenue implications which require further reduction in the Bank's cost base if the Bank is to achieve its longer term cost income ratio of below 60%.
- Total Bank RWAs are now targeted to fall below £7.5bn by end of 2018.

Simplifying of the business and reducing underlying costs continues as we reshape

- Direct Retail costs reduced by 10.2% over 2014 against 2013.
- Size of branch network reduced by 72 branches in 2014 and a programme to close a further 57 branches later this year announced.
- Year end FTE numbers reduced from 6,704 in 2013 to 5,711.

Performance of the Core Bank stabilised in the second half of the year as we were able to begin reinvesting in the brand

- Total number of current accounts decreased by 4% during 2014.
- Primary current accounts improved in the second half of the year although there remains considerable work ahead to re-establish the Bank's market position.
- Competitive positioning in second half of the year led to an improved year for new intermediary mortgage sales and the mortgage pipeline is improved when compared with the early part of 2014.
- Mortgage balances reduced as a greater number of mortgages came to the end of their natural term or switched to a competitor.
- Significant investment and progress has been made in improving our digital offering and the Bank's new mobile app launched in March 2014 now has more than 275,000 active users.

Values and ethics remain at the heart of the business as expanded Ethical Policy launched

- Over 74,000 customers and colleagues participate in Ethical Poll in June.
- Bank recommits to all its existing policy statements around the businesses and organisations it will and won't lend to.
- Expanded Ethical Policy announced in January 2015 also covers the products and services offered to customers, the Bank's relationships with external stakeholders and suppliers and the workplace and culture in the Bank.

Focus for 2015 continues to be on derisking the Bank and on making it more resilient

- Continued reduction of RWAs primarily through reducing the Optimum portfolio.
- Migration of the management of the IT infrastructure from The Co-operative Group to IBM which will, when delivered, improve the resilience of the Bank's IT infrastructure.
- Continued investment in the brand and development of products and services which reflect the expanded Ethical Policy including the launch of a new overdraft proposition.
- Further improvement in margins, processes, cost control and asset generation in the retail business.
- Risk Management Framework continues to be embedded.

(1) See page 26 for more information.

Chairman's statement

"We remain in the early stages of our turnaround and are well aware that much further work is required before the task is completed."

The Co-operative Bank has made significant progress since the depths of its crisis in 2013, driven by a renewed management team under the leadership of Niall Booker, and a revitalised Board of Directors led until October 2014 by my predecessor, Richard Pym. The Board and I would like to thank Richard again for his vital contribution which helped deliver stability and improved overall governance. Immediate priorities were to improve capital strength, to preserve prudent levels of liquidity and to surface the scale of risk within the portfolio, particularly in terms of asset quality, IT and conduct risk. This was essential before the Bank could sustain the journey to regain the confidence of our customers and to build a profitable Bank that will meet the expectations of all of our stakeholders – customers, colleagues, regulators and investors. Risks remain, there is still a considerable task ahead to turn the Bank around, but we are making good progress against our strategic plan. The Bank's regulators (Financial Conduct Authority (FCA), and Prudential Regulation Authority (PRA)) understand the current situation of the Bank and have accepted the revised plan (1).

Following the successful completion of the Liability Management Exercise in December 2013, we began implementing our plan focused on strengthening the resilience of the Bank and reshaping the organisation around its individual and small and medium sized business customers. During 2014 the Bank's capital position continued to improve following the additional £400m capital raising in May and the final £313m contribution from The Co-operative Group. Our Core Capital CET1 ratio was 13.0% at the end of 2014 and whilst we do not yet meet the Bank of England's stress test scenario of extreme economic circumstances, a clear plan is in place to achieve this. This revised plan, which has been accepted by the Prudential Regulation Authority, is based on the Bank accelerating its strategy to significantly reduce Risk Weighted Assets. The Bank's management has demonstrated a strong track record on this to date. Although the Bank temporarily met Individual Capital Guidance (ICG) at the end of the year, this plan will see the Bank meet ICG on a sustainable basis towards the end of the plan. Liquidity has improved at the end of 2014 and new provisions for bad debts and conduct risks are materially lower than at the end of 2013.

Our focus now is to build on this progress. We are making headway in deleveraging Non-core assets at acceptable pricing levels, and we are currently ahead of schedule. We have begun repositioning the Core Bank in terms of products and distribution, and the Bank has seen an improvement in its service and satisfaction measures over the course of 2014. Our initial reinvestment in the brand in October will continue through 2015 as will the journey towards a more modern, digitally led Bank as we respond to the changing trends in how customers want to bank. In terms of IT and Operations, we have clear plans in place to address past underinvestment and to provide robust and cost effective standards. We are also supporting our colleagues through this period of major change whilst building skills and supporting a customer focused culture.

Over 2014 governance standards have been enhanced, and the Bank has made material progress against the issues outlined in Sir Christopher Kelly's independent report, published in April 2014. Improvement of our risk management processes and practices remains a critical priority and we have overhauled the structure and began to embed it. Management strength is being rebuilt and we are well advanced in assembling a Board with the quality and experience to effectively oversee our transformation programme. Although The Co-operative Group remains our largest single shareholder and we remain united by our brand and our values, we also continue to progress the necessary separation of our systems and processes as part of transforming the business.

We remain in the early stages of our turnaround and are well aware that much further work is required to reduce risk and build resilience in the business before the task is completed. However, we now have a clear vision of a sustainable Bank with a distinctive customer proposition rooted in our Values and Ethics. These are as much a part of our future as our history. There remains much to be done to rebuild The Co-operative Bank as a viable alternative to the traditional banks but we are encouraged on that journey by the loyalty of our customers; the determination of our staff to restore the good name of The Co-operative Bank; and the commitment and support of our investors.

(1) For more information see page 26.

Chief Executive's review

Overarching strategy

The Co-operative Bank's overarching strategy to turn the business around is to leverage our historic brand strength and high levels of customer service satisfaction to create, over time, an efficient and profitable bank with a reduced overall risk profile.

This requires us to simplify and focus the Core business on Retail banking and small and medium sized business customers where we feel we have strong existing market credentials, customer relationships and expertise, whilst achieving significant operational efficiencies.

Those assets which are not consistent with our strategy and classified as part of the Non-core business will be actively managed to achieve the most appropriate asset value on an individual or portfolio basis or targeted for run down or exit. The need to invest in our IT platform and to increase resilience is an essential prerequisite to building a sustainable business.

The essence of our customer proposition is to deliver easy to understand, fair and transparently priced products that are easy to use. This will require us over time to improve our products, processes, digital offering and culture.

The Bank's revised plan, which runs from 2015-2019, accepted by the PRA, does not change the strategy. It looks to accelerate the deleveraging of the Non-core business, significantly improving, over the life of the plan, the Bank's resilience to a stress test as severe as the one run by the Bank of England in 2014.

Chief Executive Statement

"Over the course of 2014 the management team has continued to take significant steps to implement our strategy and to turn the Bank around. Our results reflect the progress we have made to date as we simplify and reshape the business to focus on our personal and small and medium sized business customers. The Co-operative Bank is stronger than a year ago but we are in the early stages of the turnaround and there is still much to do to transform the Bank into a sustainable business."

As we announced at the time of the Bank of England stress tests in December 2014, we now have a revised plan, accepted by the regulator, and designed to withstand a severe economic stress towards the end of the plan. The only material change from our previously announced strategy is the significant acceleration of the reduction in Risk Weighted Assets (RWA), primarily through reducing the Optimum portfolio, a closed book of residential mortgages, which is particularly susceptible to a severe economic stress. This will reduce our capital requirements over the longer term. We are progressing the reduction whilst current market conditions remain favourable. The Bank's regulators, FCA and PRA, understand the current situation of the Bank and have accepted the revised plan (1).

In the first year of implementing our plan, we focused on building capital and liquidity and the run down of our Non-core assets. At the end of 2014 our CET1 ratio stood at 13.0% (compared to 7.2% (restated) at the end of 2013), and I am pleased to report that we exceeded our target for reductions in Non-core assets. Our liquidity is also strong. However, in the short to medium term, based on the level of investment required and the continued unwind of our Fair Value Adjustments (FVAs) we expect to continue to be loss making for at least the next two years and therefore our CET1 ratio is expected to reduce before it improves again. Whilst the Bank is compliant with Individual Capital Guidance (ICG) at the end of 2014 as we have outlined previously, we only anticipate meeting ICG on a sustainable basis by the latter part of the planning period.

As we move into the second year of the turnaround, our focus continues to be on de risking the Bank and on making it more resilient. As part of this focus we are simplifying the business, reducing costs and strengthening the culture of the organisation. This is all with the aim of building a sustainable core bank differentiated by adherence to Co-operative principles and Values and Ethics.

We have made progress on improving day to day management, in beginning to embed cultural change across the organisation and in improving our governance. Although there is still considerable work ahead to simplify our product range and build the required resilience in the Bank, not least in the Bank's IT systems, we continue to make progress on embedding a revised risk management framework and in improving the Bank's controls. Our recent announcement to migrate the management of our IT infrastructure from The Co-operative Group to IBM will, when delivered, improve the resilience of our IT infrastructure and provide the foundation for the necessary transformation of our systems and the further development of our digital capability to better serve customers' future needs.

There is more to do in our retail business but over 2014 the majority of our customers have remained loyal and, as we drive down the underlying costs of the Core business, we continue our work to reshape the Bank as a more efficient and agile organisation. I am pleased that we have now begun to reinvest in our brand, which started with an advertising campaign that focused on our values and ethics, the factor that makes The Co-operative Bank different. We are also investing in our people and have begun the process of rolling out revised workplace values and ways of working, devised in conjunction with colleagues as we seek to combine pace, the ability to implement effectively and accountability whilst maintaining the service ethic and empathy for which we are well known. We have also started a process of talent identification and development and an important milestone for me personally was the relaunch of our graduate programme. These people related developments are critical to the future performance of the business but will take time to embed.

I would like to thank all our customers for their loyalty, our shareholders for their support and our colleagues for their continued hard work and dedication. The steps we are taking are building a stronger and better business for all our stakeholders. There is much more to do but I am confident that our approach to banking is as relevant in today's world as it ever was and that we can remain the bank of choice for anyone that shares the ethics and values that are at the heart of our business.

Financial Performance review

The financial performance of the business in 2014 remains dominated by the issues that came to light during 2013 including significant underinvestment in systems and processes. The statutory loss before taxation was £264.2m compared to a restated loss of £632.8m (after LME gain) in 2013. The main reasons for this change were significant reductions in the level of credit and conduct related charges. Credit impairments reduced from a statutory charge of £516.2m in 2013 to a release of £173.2m in 2014. The Bank continues to review products and practices, with total charges, including PPI, down from £411.5m in 2013 to £101.2m in 2014. This predominately comprises of £69.0m relating to previously identified breaches of the technical provisions of CCA, which are proving more complex than anticipated to address. It also includes a separate provision of £17.4m for packaged accounts. Prior year adjustments of £29.3m have affected the performance numbers, reflecting our ongoing drive to improve processes, procedures and accounting governance.

The Bank continues to be ahead of schedule in the disposal of Non-core assets with an overall reduction of these assets from £12.5bn at the beginning of the year to £10.3bn at year end. This has resulted in a corresponding reduction of £1.4bn of Risk Weighted Assets (RWAs) and contributed to an increased liquid asset ratio as well as the improved CET1 ratio.

At the end of 2014 the Bank's CET1 ratio stood at 13.0%, up from 7.2% (restated) as at December 2013, and exceeding previous guidance. The improvement in our CET1 ratio was driven by the £400m of capital raised in May 2014, the final £313m capital contribution from The Co-operative Group under the terms of the 2013 Liability Management Exercise, the write back of credit impairment provisions on Non-core assets and the speed and timing of the deleverage of those assets.

Simplifying the business

The task of simplifying the business and reducing underlying costs remains a key focus for the Bank and during 2014, our cost reduction programme has continued to deliver savings. This has been driven specifically through the reduction in the size of the Branch network, by reducing the numbers of employees in head office and by starting to improve the efficiency of the Bank's processes.

As we have restructured the business and improved processes, overall permanent staff numbers have fallen, with full-time equivalents standing at 5,711 at the year end, a reduction of 993. The reduction in underlying costs has been offset by the need to increase specialist and temporary resource in the short to medium term to support the Bank's transformation and the necessary remediation of systems and processes.

Performance of Non-core

The dedicated team within Co-operative Asset Management (CoAM) has taken advantage of better than originally expected economic conditions in the UK during 2014 and their own restructuring skills to reduce Non-core customer assets by £1.2bn since the half year and by a total of £2.2bn during 2014.

Under our revised plan, the focus is now on the reduction of our Non-core residential mortgage portfolio (Optimum). Optimum was particularly vulnerable to the Bank of England hypothetical severe stress and consumes significant capital. By advancing the timing of its reduction, the Bank will significantly improve its resilience to a severe economic downturn. Market conditions remain positive and we are optimistic that a meaningful reduction can be achieved in the early part of the plan. It should however be noted that the sale of Optimum has revenue implications which require further reduction in our cost base if we are to achieve our cost income ratio of below 60% in the longer term. Total RWAs are now targeted to fall below £7.5bn by the end of 2018.

The sale of the Illius portfolio and the announced sale of the clean energy assets at the end of 2014 clearly illustrate the Bank's readiness and ability to execute these plans, but all sales do remain vulnerable to some level of market risk.

Performance of the Core Bank

The performance of the Core Bank stabilised in the second half of the year as the ongoing uncertainty around the Bank diminished and we were able to begin reinvesting in the brand and our products as well as engaging with customers on our values and ethics. In the first six months of the year the Bank continued to face uncertainty surrounding reviews into past failings, and there was the need to raise additional capital which was completed in May. These events created a sustained and negative news flow which impacted our ability to retain and attract customers in the face of increased competition in the current account market. In the second half of the year the net outflow of current accounts reduced significantly and we were able to start our fightback by beginning to reinvest in the brand. The response to the Bank's advertising campaign launched in October and centred on our ethical stance was positive in terms of awareness and recommendation.

During 2014, the total number of current accounts decreased by 4% and the number of primary accounts, where the Bank provides the main banking service, also reduced by 2%, although the number increased marginally in the second half of the year. There remains considerable work ahead to re-establish the Bank's market share in a very competitive current account market and we are focused on developing our offering using the framework of our new Ethical Policy to guide us. The first step is the launch of a new overdraft proposition in 2015.

Our performance in mortgages was mixed. In the early part of the year, we were still recovering from our exit from the market in 2013 and were implementing the Mortgage Market Review. Throughout the second half of the year, after reviewing our processes, we became more competitive in the intermediary market, including launching the Bank's lowest ever two year fixed rate mortgage, and this has continued into early 2015. As a result 2014 was an improved year for new intermediary mortgage sales and at the beginning of 2015 the mortgage pipeline is significantly improved when compared with the early part of 2014. There is still more to do in our retail business in terms of margin improvement, process improvement, cost control and asset generation, as well as ensuring positive experiences and outcomes for our customers.

Significant investment and progress has been made in launching our digital offering and this investment and work will continue in 2015. Our new mobile app launched in March 2014 is evidence of this and now has more than 275,000 active users. Our improved internet banking service was launched in December and was rolled out to all customers in the first few weeks of 2015.

Having successfully protected our liquidity through the first half of the year, there has also been some managed reduction in high priced deposits during the second half. In the light of the planned deleveraging of the Non-core book we will continue to proactively manage liquidity in 2015. As a result of active management the Bank net interest margin has increased year on year by 0.15% to 1.19% largely driven by the reduced cost of deposits.

Good progress has been made on addressing underlying cost in the Core Bank as we continue our work to reshape the Bank as a smaller and more agile organisation. Direct Retail costs reduced by 10.2% over 2014 against 2013, largely driven by reduced headcount of 993 and a reduced number of branches and facilities. We closed 72 branches during 2014 and have announced a programme to close a further 57 branches later this year. This will leave a network of 165 branches which is still larger than it was before the merger with Britannia. Our aim is to provide branches, where we know they are well-used, in parallel with our digital and telephone channels. We will continue to invest in our digital channel, reflecting customers' changing preferences for how they do their day to day banking. As the use of digital channels is likely to become more prevalent, we expect to close a small number of additional branches in future years.

Developing our offering for small businesses remains important to the Bank and we are investing in people to lead this, but given the breadth of other current priorities, the refreshing of this proposition remains in development.

Values and ethics

Our values and ethics have always been an important factor that both underpins our business and distinguishes us in the marketplace. Led by Laura Carstensen, the new Chair of the Values and Ethics Committee, we began the work to renew our Ethical Policy in 2014 and bring it into line with what our customers care about today.

Over 74,000 customers and colleagues told us in our Ethical Poll in June that they wanted us to recommit to all our existing policy statements around the businesses with particular reference to organisations we will and won't lend to. They also made it clear that the way the Bank is run should be more visibly reflected in the Policy in areas beyond lending. As a result the expanded Ethical Policy announced in January 2015 covers the products and services offered to customers, the Bank's relationships with external stakeholders and suppliers and the workplace, culture and ways of working for colleagues in the Bank. We are also committing to return to our campaigning heritage by using our voice to stand up for underserved causes that are in line with our values and ethics.

The launch of the Policy is just the beginning. Over the coming months we will be developing our plans in some of the new areas, including the products and services we offer our customers and each year we will be reporting back on the progress we are making. We are still the only high street bank with a customer-led ethical policy and we must now build on the commitments we have made and bring them to life in the products and services we provide our customers every day and in the way we run the Bank.

Outlook

The management team continues to focus on turning around the Bank, making it more resilient and implementing the revised plan accepted by the PRA in December. There is still plenty of work ahead to deliver the change required. Throughout 2014 the Bank has benefited from improvements in the macroeconomic environment and the domestic outlook at least for now remains relatively benign. During 2015, we will continue deleveraging Non-core assets to build our resilience to a severe economic stress under the revised plan. We will also continue to invest in The Co-operative Bank brand. We are currently developing our product offering to win new customers to the Bank, using our expanded Ethical Policy as our framework. Under the leadership of our new Chairman, Dennis Holt, who took over from Richard Pym on 27 October 2014, the progress to renew the Board continues.

As outlined in the interim statement, the Board established a Committee to consider the feasibility and timing of an IPO. This has met on a couple of occasions to consider the options. Given that the business is still at an early stage of its recovery; and that the management team has a critical need to focus on implementing the revised plan, the Committee has concluded that the Bank is not in a position to undertake an IPO at this point in its journey but it will be an area that the Committee keeps under regular review.

Over 2014 we have taken some major steps forward but we have always been clear that the journey to reshape the business around our individual and small business customers would take time. Whilst the Bank is a Going Concern and stronger than it was, there remain fundamental issues to address in terms of improving resilience and bringing aspects of our business back within our risk appetite. However, alongside this work, the actions we have taken to strengthen the Bank now provide the platform to focus on what matters to our customers - restoring the brand, providing the products and services that best meet our customers' future needs and bringing to life the values and ethics that we share with them and that make us different. We continue to believe there is a market for a bank distinguished by its adherence to a customer led ethical policy and that there is value for all stakeholders in The Co-operative Bank fulfilling that need.

(1) For more information see page 26.

Detailed financial review

All amounts are stated in £m unless otherwise indicated

Capital

During 2014, the Bank has made progress toward improving the capital position and reducing the overall risk profile of the Bank. Completion of the £400m equity capital raising (£387m net of associated costs), together with the £313m of planned capital injections from The Co-operative Group (1), as well as ongoing deleveraging of RWAs, has resulted in a significant improvement in the capital position of the Bank.

(1) The capital injections were made by The Co-operative Banking Group Limited, a wholly owned subsidiary of the Co-operative Group Limited.

CRD IV fully loaded capital position

	As at 31 December 2014	As at 31 December 2013 (restated)	Change
Capital ratios			
CET 1 ratio	**13.0%**	7.2%	5.8%
Total capital	**15.0%**	8.9%	6.1%
RWAs (£bn)	**12.6**	15.1	(2.5)
Leverage ratio	**4.3%**	2.4%	1.9%

The £400m equity capital raising and The Co-operative Group CET1 capital injections of £50m in January 2014, £100m in June 2014 and £163m in December 2014 were the primary factors in the Bank's CET1 position increasing by £0.5bn to £1.6bn. The increase in CET1 has resulted in the Bank's fully loaded CRD IV CET1 ratio increasing by 5.8%, from 7.2% to 13.0%.

RWAs have decreased by £2.5bn since last year end. Non-core assets have been delevered in line with strategy and this is reflected in the above £1.4bn reduction in Non-core RWAs. Leverage ratio is 4.3%, an increase of 1.9% since last year end, reflecting both capital injections and ongoing balance sheet deleveraging activity.

For most of 2014 the Bank was not compliant with its Individual Capital Guidance (ICG), being the PRA's guidance as to the regulatory capital (Pillar 2a) it expects the Bank to hold above Pillar 1, where Pillar 1 is the minimum required under the Capital Requirements Regulation. On 31 December 2014 the contribution from The Co-operative Group helped push the Bank into ICG compliance, however due to the Bank's ongoing losses, this position should be regarded as a temporary situation. The Bank met the Pillar 1 capital requirement throughout the year.

The revised plan (2), which has been accepted by the PRA, anticipates that the Bank will meet the 7% CET1 ratio throughout the planning period and will sustainably meet ICG by the latter part of the planning period. The plan aims to build a sustainable Core Bank, and is designed to create a capital buffer by 2019 which would withstand a severe stress scenario equivalent to the 2014 Bank of England stress test.

(2) For more information see page 26.

Liquidity

Overview

The Bank raises the majority of its funding through accepting retail and corporate deposits. The Bank also maintains a range of funding programmes targeting wholesale investors.

The focus of the funding and liquidity strategy of the Bank has been to:

- Reduce retail fixed term deposits to match the reduction of balance sheet and reduce cost of liability base;
- Reduce the holding of investment grade bonds that were not eligible to be included in the liquid asset buffer (LAB). It also reduced reliance on short dated secured financing to fund such assets and so in turn reduced the amount of Treasury assets encumbered by the Bank;
- Substantially increase secondary liquidity by increasing the availability of mortgage collateral for funding;
- Maintain ratings of secured funding programmes, by the implementation of rating agency compliant back-up servicing arrangements to ensure market access; and
- Repay wholesale funding to the extent not required to support the Bank's liquidity position as conditions stabilise.

The Bank's deleveraging strategy will continue to reduce funding and liquidity requirements.

Credit rating

In April 2014, Moody's downgraded the Bank to Caa2 from Caa1. The current ratings are:

	Long term	Short term
Moody's	Caa2	NP
Fitch	B	B

The Bank's current credit ratings continue to result in:

i. sub-investment grade ratings on the Bank's senior debt in turn leading to a significant reduction in the demand for these types of instrument;
ii. a negative impact on the Bank's ability to access short term unsecured wholesale funding; and
iii. heightened collateral requirements within some clearing systems.

Liquidity portfolio

The Bank's liquidity resources as at 31 December 2014 were £12.1bn compared to £11.2bn as at 31 December 2013. The table below analyses the Bank's liquidity portfolio by product and by liquidity value. Primary liquidity consists of liquid assets that are eligible under BIPRU 12.7 (LAB) and secondary liquidity consists of all other liquid assets (including self-issued retained securitisations and whole loans).

Primary liquidity has decreased over the period by £424.4m and secondary liquidity has increased by c. £1.4bn.

	2014	2013	Change
Operational balances with central banks	**4,487.4**	5,076.3	(588.9)
Gilts	**1,246.7**	789.5	457.2
Central government and multilateral development bank bonds	**819.5**	1,112.2	(292.7)
Total primary liquidity	**6,553.6**	6,978.0	(424.4)
Total secondary liquidity	**5,566.8**	4,215.4	1,351.4
Total liquidity	**12,120.4**	11,193.4	927.0

Retail and commercial funding

The majority of the Bank's funding comes from retail and commercial accounts. As at 31 December 2014, customer deposits were £29.8bn compared to £33.0bn as at 31 December 2013.

Retail deposits reduced over the period by £2.2bn. This forms part of the Bank's strategy to reduce its fixed term retail deposits to match the reduction in the balance sheet and to reduce the cost of liabilities.

The total amount of the Bank's corporate deposits reduced by almost £1bn over the year. This was due to the maturing of term deposits placed before last year's credit rating downgrades.

	2014	2013	Change
Current accounts			
Retail	**3,479.3**	3,378.1	101.2
Corporate	**2,346.1**	2,298.9	47.2
Total current accounts	**5,825.4**	5,677.0	148.4
Instant access savings accounts			
Retail	**7,936.9**	8,097.2	(160.3)
Corporate	**584.0**	666.2	(82.2)
Total instant access saving accounts	**8,520.9**	8,763.4	(242.5)
Term deposits and bonds			
Retail	**7,675.6**	9,879.5	(2,203.9)
Corporate	**431.6**	1,344.9	(913.3)
Total term deposits and bonds	**8,107.2**	11,224.4	(3,117.2)
Individual savings accounts (ISA)			
Retail – ISA Fixed	**3,557.4**	3,853.1	(295.7)
Retail – ISA Demand	**2,745.9**	2,455.2	290.7
Total ISA accounts	**6,303.3**	6,308.3	(5.0)
Other deposits	**1,121.0**	1,028.3	92.7
Total customer deposits	**29,877.8**	33,001.4	(3,123.6)

Wholesale funding

The Bank uses wholesale funding to supplement retail and corporate customer deposits by raising debt to diversify funding sources. The Bank has a variety of wholesale funding sources outstanding, including securitisations, covered bonds, unsecured notes, bilateral facilities, and repurchase agreements.

The Bank has repaid bilateral facilities and repo funding during the course of the year to reduce liquidity as conditions stabilised. The Bank optionally redeemed the Silk Road Finance Number Two securitisation in September 2014 of c. £466m. The Bank has given notice for the optional redemption of the Silk Road Finance Number One securitisation in March 2015 of c. £1.3bn.

	2014	2013	Change
Preference shares, PSBs and subordinated debt	**196.4**	196.3	0.1
Secured funding	**2,521.8**	4,339.5	(1,817.7)
Repos	**500.6**	2,119.3	(1,618.7)

Market borrowing	**46.0**	56.6	(10.6)
MTNs	**832.9**	884.0	(51.1)
Total wholesale funding	**4,097.7**	7,595.7	(3,498.0)

The table does not include the Funding for Lending Scheme (FLS). The Bank accessed the FLS in the first half of 2013, drawing £900m of UK treasury bills. The Bank repaid £350m of its FLS liability in 2014. The remaining UK treasury bills remain available to the Bank until March 2017.

Figures are based on nominal values and accrued interest as at 31 December 2014 and 31 December 2013.

The table below analyses contractual maturities (as opposed to internally expected repayment dates).

	2014	2013	Change
Repayable in less than 1 month	**84.8**	2,010.3	(1,925.5)
Repayable between 1 and 3 months	**324.1**	67.8	256.3
Repayable between 3 and 12 months	**389.8**	157.2	232.6
Repayable between 1 and 5 years	**580.8**	1,800.8	(1,220.0)
Repayable in more than 5 years	**2,718.2**	3,559.6	(841.4)
Total	**4,097.7**	7,595.7	(3,498.0)

Total Bank financial performance

The 2014 financial results reflect the progress made in implementing the strategy to turn the Bank around with a statutory loss before taxation of £264.2m representing a significant improvement on the 2013 loss (restated) of £632.8m. However, the Bank is in the early stages of its turnaround and substantial work remains to transform it into a sustainable business.

The primary drivers of 2014 performance are:

- an overall net impairment write back of £171.7m compared to a 2013 loss of £512.1m, largely as a result of improved economic conditions;
- material reduction in charges for conduct and legal risk provisions of £101.2m compared to a charge in 2013 of £411.5m;
- a reduction in operating expenditure of £61.3m to £594.6m reflecting management actions to address the costs base of the Bank primarily focused on the improvement and simplification of Bank processes in addition to third party and ATM estate savings and branch rationalisation; and
- the non-recurrence of prior year items relating to intangible asset impairment (£148.4m), operating gains as a result of the Liability Management Exercise (LME) (£688.3m) and net gain on sale of Treasury assets (£40.8m).

The Bank's net interest margin has improved by 15bps on prior year to 1.19% largely driven by the reduced cost of deposits.

The Bank exceeded its target to reduce Non-core assets. Customer assets of £10.3bn at the end of 2014 is ahead of the target of c. £11.0bn. This continued deleverage has been achieved via a combination of formal trade sales, proactive rebanking of the Bank's Corporate CoAM clients and the natural run off of the Non-core book.

The numbers referenced and presented on these pages are on a management accounts basis. A reconciliation of these numbers to the statutory accounts basis is provided in the segmental information in note 4. 2013 comparatives have been restated as described in note 3.

Bank performance

	2014	2013 (restated)	Change
Net interest income	**480.4**	483.4	(3.0)
Gains/(losses) on asset sales	**(14.4)**	40.8	(55.2)
Non interest income	**128.1**	146.5	(18.4)
Operating income	**594.1**	670.7	(76.6)
Operating expenditure	**(594.6)**	(655.9)	61.3
Project costs	**(226.5)**	(164.7)	(61.8)
Impairment gains/(losses) on loans and advances	**171.7**	(512.1)	683.8
Operating result	**(55.3)**	(662.0)	606.7
FSCS levy	**(24.4)**	(24.1)	(0.3)
Share of post tax profits/(losses) from joint ventures	**0.6**	0.7	(0.1)
Intangible asset impairment	**-**	(148.4)	148.4
Conduct/legal risk	**(101.2)**	(411.5)	310.3
LME	**-**	688.3	(688.3)
Fair value amortisation	**(83.9)**	(75.8)	(8.1)
Loss before taxation	**(264.2)**	(632.8)	368.6
Net interest margin	**1.19%**	1.04%	0.15%
Cost income ratio (1)	**100.1%**	97.8%	2.3%

(1) Operating expenditure divided by operating income.

Charges in respect of the Financial Services Compensation Scheme (FSCS) levy are in line with prior year (restated) at £24.4m (2013: £24.1m restated). The unwind of the fair value adjustments associated with the merger of The Co-operative Bank and Britannia Building Society continues to impact the income statement with a charge of £83.9m incurred in the year (2013: £75.8m). Further information is included in note 40.

Operating Expenditure

	2014	2013	Change
Core direct costs	**(199.5)**	(222.0)	22.5

Non-core direct costs	**(26.1)**	(25.1)	(1.0)
Total direct costs	**(225.6)**	(247.1)	21.5
Operations and Central Costs	**(369.0)**	(408.8)	39.8
Total operating costs	**(594.6)**	(655.9)	61.3
of which: Staff Costs	**(250.6)**	(255.2)	4.6

Total operating costs reduced by £61.3m to £594.6m. Management actions have delivered £71.0m of sustainable savings in the underlying cost base compared to 2013. These break down into the following categories:

- process improvements and simplification of processes where the Bank has achieved savings of c. £20.0m;
- third party and ATM savings as a result of active management of supplier contracts coupled with a reduced ATM estate of c. £25.0m; and
- other cost reduction initiatives of c. £26.0m including savings arising from: branch rationalisation, new fraud detection and recovery processes.

These cost savings were partially offset by:

- activity relating to the separation of the Bank from The Co-operative Group c. £25.0m;
- marketing spend linked to the relaunch of the brand in October 2014 c. £8.0m;
- additional spend associated with specialist consultants and contractors c. £7.0m;
- c. £18.0m in relation to anti-money laundering, mortgage business review and numerous smaller items; and
- 2013 included c. £48.0m of one-off costs which have not recurred in 2014.

Staff costs have decreased year on year by £4.6m to £250.6m. Permanent staff numbers (full time equivalents) have fallen by 993 to 5,711 and direct pay has fallen by c. £19.0m which has been partially offset by cost increases as a result of additional short to medium term specialist contractor resource and increases in pension costs.

Project Costs

	2014	2013	Change
Operational projects	**(37.2)**	(33.7)	(3.5)
Remediation, integration and resiliency projects	**(140.1)**	(52.9)	(87.2)
Strategic projects and exceptional items	**(49.2)**	(78.1)	28.9
Total project expenditure	**(226.5)**	(164.7)	(61.8)

The Bank summarises its investment spend activity into three broad categories:

Operational projects relate to changes in the regulatory environment and smaller business led initiatives. Expenditure is broadly in line with prior year ensuring the regulatory and mandatory requirements of the Bank are met.

Remediation, integration and resiliency projects include IT remediation and resiliency as well as activity associated with Bank separation. In 2013 the Bank recognised provisions of £39.4m relating to separation from The Co-operative Group of which £21.6m has been utilised in 2014. Further provisions of £94.5m have been recognised in 2014. Included in this amount are provisions of £68.9m relating to the IT infrastructure contract with IBM announced in January 2015. The ten year contract has a total ongoing cost of £275.0m.

In addition, the Bank incurred costs of £19.1m regarding ongoing IT remediation, delivering against issues identified and agreed with the PRA and £14.4m towards embedding new systems and processes to address IT regulatory compliance.

Strategic projects and exceptional items include projects that are transformational in nature and deliver significant cost or income benefits to the business. Expenditure amounted to £49.2m (2013: £78.1m) reflecting investment to enhance capability across the organisation. Spend in this area focused on outsourcing of business processes (£14.3m), severance associated with organisational design changes (£12.7m) and rationalisation of the branch network (£6.2m). In addition to this, the Bank has invested in its Digital offering with total investment spend of £22.9m, of which £1.6m was expensed to the income statement. In addition the Bank spent £14.4m on a series of smaller initiatives.

Impairment losses

The 2014 net impairment write back of £171.7m compared to a charge of £512.1m in 2013 was primarily driven by the Non-core business with a 2014 net impairment write back of £168.2m (2013: charge of £476.3m).

Non-core assets have been disposed of at favourable prices and, together with a number of loan restructures, resulted in the release of previously recognised impairment provisions driving a net impairment write back of £104.6m (2013: charge of £177.4m). In addition, the Bank has booked revisions to valuations of collateral still held, due to an improvement in economic conditions, resulting in net impairment write backs of £62.3m (2013: charge of £65.4m).

Assets classified as in default during 2014 stabilised resulting in a charge of £28.4m (2013: charge of £195.9m). The improving economic conditions coupled with lower defaults have also favourably impacted the collective impairment provision with a net write back of £33.2m (2013: charge of £73.4m).

A more detailed analysis of impairments is provided in the credit risk section.

Conduct and legal risk

The Bank provided an additional £101.2m (2013: £411.5m) during the year in respect of conduct and legal risk. This predominantly comprises £69.0m relating to previously identified breaches of the technical provisions of CCA, £17.4m with regards to packaged accounts, and includes an additional net £15.2m for Mortgage related conduct risk and £5.0m PPI. The additional CCA provision reflects £44.5m of 2014 interest on non CCA compliant unsecured loans which will be refunded to the customer, £2.3m of mortgages related CCA provisions and £22.3m in respect of anticipated redress costs. The Bank reduced provisions held in relation to card security products provided via a third party, Affinion International Limited, by £10.0m.

Bank Balance Sheet

Summary balance sheet

	2014	2013 (restated)	Change
Cash and balances at central banks	**4,765.3**	5,418.8	(653.5)
Loans and advances to banks	**1,608.4**	1,594.4	14.0
Loans and advances to customers (1)	**25,700.8**	30,286.1	(4,585.3)
Investment securities & derivatives	**4,893.2**	5,055.2	(162.0)

Other assets	**615.2**	1,029.3	(414.1)
Total assets	**37,582.9**	43,383.8	(5,800.9)
Deposits by banks	**615.4**	2,757.5	(2,142.1)
Customer accounts	**29,877.8**	33,001.4	(3,123.6)
Debt securities and derivatives	**3,995.3**	4,746.2	(750.9)
Other borrowed funds	**196.4**	196.3	0.1
Other liabilities	**883.5**	913.9	(30.4)
Total liabilities	**35,568.4**	41,615.3	(6,046.9)
Total equity	**2,014.5**	1,768.5	246.0
Total liabilities & equity	**37,582.9**	43,383.8	(5,800.9)

(1) Includes loans and advances held for sale of £323.4m.

The Bank's customer asset base is made up predominantly of mortgages, corporate real estate loans and unsecured loans. In addition to these customer assets, the Bank holds liquid assets to meet its ongoing and potential future needs in the form of cash and balances at central banks coupled with investment securities.

To fund the assets on the balance sheet, the Bank relies heavily on customer accounts with funding generated from personal current accounts and customer investment products such as ISAs and fixed terms bonds.

Total assets have reduced by £5.8bn to £37.6bn. In addition to the reduction in loans and advances to customers, cash and balances at central banks has fallen by £0.7bn year on year as a result of liquidity management. Other assets have reduced to £0.6bn, a decrease of £0.4bn representing the sale of the Illius property portfolio coupled with the final instalment of The Co-operative Group's £0.3bn capital contribution.

Total liabilities have reduced by £6.0bn to £35.6bn reflecting a reduction of £3.1bn in customer balances, a reduction of deposits by banks of £2.1bn, and a reduction in debt securities and derivatives of £0.8bn as a result of reduction in wholesale funding requirements in line with asset contraction.

Business segment financial performance

Total Bank operating result

	2014	2013 (restated)	Change
Retail contribution	**341.5**	341.7	(0.2)
BaCB contribution	**47.5**	55.7	(8.2)
Core contribution exluding Treasury/other	**389.0**	397.4	(8.4)
Treasury/other contribution	**(51.9)**	(16.4)	(35.5)
Core contribution result	**337.1**	381.0	(43.9)

Non-core contribution result	**203.1**	(469.5)	672.6
Operations and Central Costs	**(369.0)**	(408.8)	39.8
Project costs	**(226.5)**	(164.7)	(61.8)
Operating result	**(55.3)**	(662.0)	606.7

The Core business (Retail and BaCB excluding Treasury/other) contribution is slightly down on prior year at £389.0m (2013: £397.4m) as a result of a reduction in income, partially offset by net impairment write backs and lower direct costs.

Treasury/other delivered a contribution loss of £51.9m (2013: £16.4m) reflecting the change in both the asset and liability mix of the Treasury balance sheet and allocation of liquidity costs.

The Non-core contribution of £203.1m represents a significant improvement on prior year (2013: £469.5m loss) driven primarily by net impairment write backs of £168.2m compared to 2013 impairment charges of £476.3m.

The detailed commentary regarding the drivers behind the results are included in the following sections.

Core

Core contribution

	2014	2013 (restated)	Change
Net interest income	**431.8**	487.2	(55.4)
Gains/(losses) on asset sales	**(2.1)**	40.8	(42.9)
Non-interest income	**103.4**	110.8	(7.4)
Net income	**533.1**	638.8	(105.7)
Direct costs	**(199.5)**	(222.0)	22.5
Impairment gains/(losses) on loans and advances	**3.5**	(35.8)	39.3
Contribution result	**337.1**	381.0	(43.9)
Net interest margin	**1.60%**	1.60%	-
Assets	**25,476.2**	28,568.2	(3,092.0)
Liabilities	**33,391.0**	39,418.7	(6,027.7)

The Core Bank contribution was down £43.9m on 2013. This is mainly as a result of a reduction in net interest income of £55.4m across all Core business segments coupled with the non-recurring prior year asset sales in Treasury. However, this was partially offset by a reduction in direct costs of £22.5m mainly arising in the Retail business coupled with a favourable movement of £39.3m on impairment charges (£3.5m net write back in 2014, 2013: £35.8m charge).

Retail

Retail contribution

	2014	2013 (restated)	Change
Net interest income	**396.3**	428.1	(31.8)
Non-interest income	**105.2**	123.7	(18.5)
Net income	**501.5**	551.8	(50.3)
Direct costs	**(161.9)**	(180.3)	18.4
Impairment gains/(losses) on loans and advances	**1.9**	(29.8)	31.7
Contribution result	**341.5**	341.7	(0.2)
Net interest margin	**2.52%**	2.49%	0.03%
Customer assets	**14,611.4**	16,790.9	(2,179.5)
Customer liabilities	**25,562.3**	27,899.3	(2,337.0)

2013 comparatives have been restated as described in note 3.

2014 Retail contribution has remained broadly stable at £341.5m (2013: £341.7m) with reduced income offset by lower direct costs and net impairment write backs.

Mortgage book performance was mixed. In the second half of 2013, the Bank prioritised its liquidity needs over originating new business and as a result, new mortgage applications were severely impacted in the second half of 2013 and early part of 2014.

As the Bank became more competitive in its intermediary products, year on year mortgage applications through intermediaries more than doubled to £1,960.1m. Moreover, intermediary mortgage completions improved to £941.0m (2013: £737.6m), of which £810.4m were completed in the second half of 2014.

However, redemption rates increased in the year on higher margin standard variable rate (SVR) mortgages and combined with challenges in the origination of direct to customer mortgages, Retail customer lending decreased 13.0% to £14,611.4m reducing the net interest income of the Retail division.

Maintaining strong levels of liquidity was a focus for the first half of 2014. In the second half of 2014, actions were taken to address excess liquidity across the Bank via customer pricing of fixed term deposits. As a result, Retail customer liabilities reduced to £25,562.3m.

In addition, the Bank's internal cost of funding reduced year on year. Customer liabilities receive less benefit from a lower cost of internal funding and overall this has negatively impacted Retail net interest income due to the net liability position of the balance sheet. The net impact of the above is to decrease Retail Bank total net interest income by £31.8m to £396.3m. Despite this reduction in income, net interest margin has marginally increased due to the mix of assets and liabilities.

The UK current account market has experienced increased competition in 2014. The uncertainty regarding the Bank, coupled with the Bank's decision not to significantly market in the first half of 2014, has resulted in a net 4% reduction in total current accounts to 1.4m. The outflow of total current accounts reduced significantly in the second half of the year. However there remains considerable work ahead to re-establish the Bank's market position in a very competitive market.

2014 impairment improved £31.7m to a net write back of £1.9m (2013: £29.8m charge). This predominantly reflects the release of historical provisions associated with an unsecured debt sale. This credit is offset by 2014 impairment charges which are lower than 2013 due to lower balances in arrears, primarily driven by favourable economic conditions.

Business and Commercial Banking (BaCB)

Business and Commercial Banking contribution

	2014	2013 (restated)	Change
Net interest income	**46.1**	69.5	(23.4)
Non-interest income	**14.9**	14.9	-
Net income	**61.0**	84.4	(23.4)
Direct costs	**(15.1)**	(23.7)	8.6
Impairment gains/(losses) on loans and advances	**1.6**	(5.0)	6.6
Contribution result	**47.5**	55.7	(8.2)
Net interest margin	**6.29%**	7.80%	(1.51%)
Customer assets	**620.0**	844.9	(224.9)
Customer liabilities	**2,837.0**	3,479.0	(642.0)

The 2013 comparatives have been restated as described in note 3.

The BaCB business 2014 contribution result of £47.5m (2013: £55.7m) represents a £8.2m reduction on prior year.

Customer liabilities reduced £642.0m to £2,837.0m reflecting fixed term deposit outflows as a result of the continuing impact of Bank credit downgrades. In addition, customer assets decreased £224.9m to £620.0m (2013 £844.9m) largely as a result of out of cycle maturities, including repayment of The Co-operative Group balances.

Net interest income has reduced £23.4m largely as a result of the reduction in customer balances outlined above. Consequently, the net interest margin has decreased 151bps to 6.29% (2013: 7.80%).

BaCB reported a net impairment write back of £1.6m mainly due to favourable economic conditions.

Treasury/Other

Treasury/other business contribution

	2014	2013 (restated)	Change
Net interest income	**(10.6)**	(10.4)	(0.2)

Gains/(losses) on asset sales	**(2.1)**	40.8	(42.9)
Non-interest income	**(16.7)**	(27.8)	11.1
Net Income	**(29.4)**	2.6	(32.0)
Direct costs	**(22.5)**	(18.0)	(4.5)
Impairment gains/(losses) on loans and advances	**-**	(1.0)	1.0
Contribution result	**(51.9)**	(16.4)	(35.5)
Net interest margin	**(0.10)%**	(0.08)%	(0.02%)
Assets	**10,244.8**	10,932.4	(687.6)
Liabilities	**4,991.7**	8,040.4	(3,048.7)

The 2013 comparatives have been restated as described in note 3.

Net interest income reduced due to a change in asset and liability mix of the Treasury balance sheet and the implementation of a revised policy on distributing the cost of holding liquidity. However, this reduction was offset by the impact of a review of hedging accounting methodologies applied by the Bank.

Treasury continued to reduce assets not eligible for the liquid asset buffer (LAB), resulting in an asset portfolio consisting materially of highly liquid gilts, multilateral development banks and cash. Due to its current credit ratings, the Bank is required to maintain collateral postings within central payment systems. These assets typically consist of lower yielding government bonds and Treasury bills thereby further impacting net interest income. The Bank repaid £350m of its Funding for Lending Scheme (FLS) liability at the end of 2014.

The allocation policy for the cost of holding the Bank's LAB was changed in 2014, resulting in Treasury absorbing the cost of holding liquid assets above the liquidity risk appetite (LRA) amount directly attributable to products (as opposed to allocating out the entire LAB cost). The impact of this change was a reduction in net interest income for Treasury of £12.2m.

A review of hedge accounting methodologies (see note 3) resulted in a £3.6m increase in net interest income in 2014 and a prior period reduction of £14.6m.

Non-interest income increased £11.1m when compared to 2013 primarily due to the hedge accounting restatement, noted above (see note 3), which resulted in a profit after restatement of £2.5m (2013: £9.8m loss) on cross currency micro hedging. Due to deleveraging of the balance sheet in 2014, the Bank paid the maximum FLS fee, which is included in non-interest income.

Non-core

Non-core balance sheet

	2014	2013 (restated)	Change
Corporate CoAM	**3,930.1**	5,646.1	(1,716.0)
Optimum	**6,822.9**	7,326.1	(503.2)
Illius	**-**	162.2	(162.2)

Assets	**10,753.0**	13,134.4	(2,381.4)
Corporate CoAM	**557.4**	831.0	(273.6)
Liabilities	**557.4**	831.0	(273.6)
Customer assets	**10,253.0**	12,473.4	(2,220.4)
Customer liabilities	**557.4**	831.0	(273.6)

The Bank exceeded its target in the reduction of Non-core assets. These assets have a higher proportional risk weighting compared to Core Bank assets and therefore deleverage mitigates the exposure to credit risk in this area. Non-core total assets decreased by £2,381.4m to £10,753.0m. The majority of this reduction is in the Corporate CoAM Business Unit (£1,716.0m) where the Bank has a focused team actively working to deleverage the balance sheet.

In addition, the Bank's Non-core residential mortgage portfolio's (Optimum) total assets reduced by £503.2m to £6,822.9m as customers continued to pay down their mortgages. The Bank's revised plan requires a reduction in Optimum assets. Optimum was particularly vulnerable to the Bank of England's hypothetical severe stress and an acceleration in timing of its reduction will significantly improve the Bank's resilience to a severe economic downturn. A disposal of the Bank's Optimum assets has revenue implications which require further reduction in the Bank's cost base if the Bank is to achieve its longer term cost income ratio target of below 60%.

The Illius business (a closed residential property portfolio) was disposed of in the year. The transaction resulted in £162.2m of assets being sold at a marginal loss of £1.2m after transaction costs. The Illius business contributed a total loss for the year of £6.5m (2013: £10.1m loss).

Non-core liabilities have reduced by £273.6m to £557.4m in line with expectations. As the Bank continues its Non-core deleveraging strategy customers have chosen to migrate their accounts to other financial institutions.

Non-core contribution

	2014	2013 (restated)	Change
Net interest income	**48.6**	(3.8)	52.4
Gains/(losses) on asset sales	**(12.3)**	-	(12.3)
Non-interest income	**24.7**	35.7	(11.0)
Net income	**61.0**	31.9	29.1
Direct costs	**(26.1)**	(25.1)	(1.0)
Impairment gains/(losses) on loans and advances	**168.2**	(476.3)	644.5
Contribution result	**203.1**	(469.5)	672.6

The 2013 comparatives have been restated as described in note 3.

The 2014 contribution is a significant improvement on prior year at £203.1m (2013: loss of £469.5m) primarily driven by net impairment write backs in the year of £168.2m. These are associated with assets being disposed of at favourable prices resulting in the write back of previously recognised impairment provisions. In addition, the Bank has revised valuations of assets still held.

Optimum is part of the Non-core business and the mortgage book is closed for new business. Net interest income for the Non-core Bank has improved during the year to £48.6m (2013: loss of £3.8m) primarily as a result of the Optimum portfolio being charged a lower cost of funds in line with the Bank's reduced cost of internal funding.

Non-core fee related income is down on prior year as a result of lower asset balances across the business and will continue to fall as the Bank deleverages the asset base.

Principal Risks and Uncertainties

Regulatory position

In December 2014 the Bank submitted a revised plan to the PRA. The revised plan was accepted by the PRA and runs from 2015-2019. Once delivered, it will help the Bank to comply with FCA and PRA regulatory requirements and expectations.

The following section summarises the Bank's position in relation to deficiencies against regulatory requirements and expectations. These deficiencies have existed for some time, and will continue for some years to come, while the Bank executes its plan.

Capital

The Bank meets its Pillar I capital requirements under normal economic conditions. This is the minimum required under the Capital Requirements Regulation. However, the Bank has insufficient capital to withstand a severe stress.

The Bank's revised plan is expected to remediate this position towards the end of the plan period (mainly through Risk Weighted Asset (RWA) reduction to reduce risks that the Bank is exposed to, and cost reduction to mitigate ongoing losses).

The PRA provides Individual Capital Guidance (ICG) for each bank. This represents guidance on the capital (Pillar 2a) a firm should hold over Pillar 1. Although the Bank was temporarily above ICG at 31 December 2014, the Bank has insufficient capital to sustainably meet its ICG until the later years of its plan.

The Bank's plan remediates this issue by 2018.

Capital Requirements Regulations (CRR)

The Bank is not currently compliant with all of the requirements to model credit risk internally.

The Bank plans to remediate this issue during 2015.

Solo-consolidation

Until its expiry in September 2014, the Bank had regulatory approval to operate under a 'solo-consolidation' permission, which allowed it to be regulated for prudential purposes as though the Bank and specified solo-consolidated subsidiaries formed a single legal entity. In March 2015, the Bank was granted a new permission to apply solo-consolidation, though with respect to a smaller number of subsidiaries. The Bank and its subsidiaries do not have the processes in place to comply with regulatory reporting obligations resulting from this change, or with large exposure requirements in respect of exposures to certain FCA-authorised subsidiaries. The Bank intends to address these issues to a timetable set by the regulators. The Bank has already acted to ensure its FCA-authorised subsidiaries comply with capital requirements on an individual basis.

Technology

As indicated previously, the Bank's infrastructure is in need of an upgrade in numerous respects. Across the Bank's IT infrastructure there are varying levels of resilience and recoverability and whilst a basic level of resilience to a significant data centre outage is in place, the Bank does not currently have a proven end-to-end disaster recovery capability.

The migration of IT infrastructure to an IBM platform (announced on 23 January 2015) is expected to deliver proven end to end disaster recovery capability by the end of 2016.

The Bank has received written confirmation from the FCA that the technology issue detailed above constitutes a breach of the FCA's Threshold Conditions (1). The FCA is closely supervising the firm as it works towards restoring compliance with the Appropriate Resources (non-financial resources) Threshold Condition on this issue. The FCA is not currently proposing further immediate supervisory intervention or the immediate exercise of any additional regulatory powers as a result of this assessment. The FCA reserves the right to take action in the future in relation to this breach. The PRA's general policy is not to communicate its assessment of its position in relation to the PRA Threshold Conditions. However, both the PRA and FCA are closely monitoring the position of the Bank and the Bank remains in continual dialogue with both regulators.

(1) Threshold Conditions are set out in Schedule 6 of the Financial Services and Markets Act 2000 as amended by the Financial Services and Markets Act 2000 (Threshold Conditions) Order 2013. Threshold Conditions set out the minimum standards to be met relating to financial and non-financial resources, including capital, risk management, liquidity and technology. The Threshold Conditions differ depending on whether a firm is PRA-regulated or not.
The Bank is regulated by both the PRA and the FCA, and certain of the Bank's subsidiaries may in future also be regulated on an individual basis by the FCA.

Background

The Bank faced an extremely difficult and unprecedented situation following its June 2013 announcement of a significant shortfall in CET1 of £1.5bn. Since then, elements of the uncertainty around the Going Concern status of the Bank have been removed with the successful completion of the two capital raising exercises - the LME in December 2013 and the equity capital raising in May 2014 together with the receipt of The Co-operative Group's £333m capital contribution.

In December 2014, following the Bank's failure of the Bank of England stress tests, the PRA accepted a revised plan. The overarching strategy of the Bank remains the same, however the Bank has committed to an earlier deleverage of the Optimum portfolio than that contemplated by the original plan. This will have an impact on the Bank's income which will need to be offset by additional cost savings to enable the achievement of the cost income target by the end of the plan period.

Overall, the turnaround is still in its early stages and there are significant challenges in its execution. The Bank has a large number of remediation and redress programmes to implement along with substantial re-engineering of its operating model to reduce costs and improve efficiency and a very large and complex IT remediation programme. A failure to successfully implement or a delay in implementing the Bank's strategy and plans may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory requirements both in respect of capital and more generally (see previous page for more information).

The Bank's ability to implement its plan is also influenced by external factors which may mean underpinning assumptions relating to economic or market conditions may be incorrect and negatively impact the plan (for example interest rates may not rise in accordance with assumptions underpinning the plan). Many of these are similar to those faced by other financial institutions, for example, deterioration in general economic conditions, instability of global financial markets and the management of credit risk, interest rate risk, currency risk and market risk and risks from regulatory change and an increasing regulatory enforcement and litigious environment.

The table below outlines how the Bank's Risk Management Framework (RMF) categorises the key financial and non-financial risks to which the Bank is exposed. The crystallisation of any of these risks could result in an adverse effect on the Bank's business, financial condition operating results, reputation and prospects. The RMF is the Board approved segmentation of the risks that the Bank faces into ten Principal Risks to allow the Bank to identify, assess, manage, monitor and report on its risks across the business. Details of how these risks are managed can be found in the risk management section.

Many of these risks are not peculiar to the Bank but are common across all banks. More detail on those more idiosyncratic risks can be found below:

Principal Risks	Definition	Why this is important and how it is managed
Credit risk	The current or prospective risk to earnings and/or capital arising from a borrower's failure to meet the terms of any contract with the Bank or the various subsidiaries of the Bank or such borrower's failure to perform as agreed.	**Managing this risk is a fundamental part of what a bank does.** The Bank's exposure to this risk is reducing as the higher risk lending is deleveraged, however along with all other banks, the Bank remains exposed to macro-economic, market wide risks such as issues with the housing market and interest rate changes.
Liquidity and funding risk	The risk that the Bank's resources will prove inadequate to meet its liabilities as they contractually fall due or as a result of any contingent or discretionary cash outflows that may occur in a stress. It arises from the mismatch of timings of cash flows generated from the Bank's assets and liabilities (including derivatives). Should additional liquidity be required during a time of stress this is likely to result in higher than anticipated funding costs which will negatively impact on retained earnings and therefore capital resources.	**The Bank is reliant on its retail deposit base as a major source of funding** and given the relative size of the Bank's retail deposit base as compared with other sources of funding, the Bank is particularly exposed to liquidity risks as a loss of confidence by customers may result in the loss of a high proportion of the Bank's funding.
Market risk	The risk that the value of assets and liabilities, earnings and/or capital may change as a result of changes in market prices of financial instruments. The majority of the Bank's market risk arises from changes in interest rates which is managed and hedged in line with the market risk policy to minimise earnings volatility.	**The treasury team manages interest rate risk.** More information can be found in the risk management disclosures. The success of the Bank's current deleverage strategy is particularly susceptible to market risk.
Operational risk (including legal risk)	The risk of loss resulting from inadequate or failed internal processes, people and systems or external events. This encompasses the effectiveness of risk management techniques and controls to minimise these losses. Legal risk including litigation is also managed within this risk type.	**The Bank is subject to a number of specific issues in this area due to a lack of investment in systems and processes which has led to increased operational risk.** **In particular:** **The Bank's IT system has been underinvested for a considerable period of time.** The Bank needs to urgently and significantly improve and re-engineer its

		existing IT platform as the existing infrastructure is unsuitable and inherently fragile. There are also concerns about its resilience as the Bank's IT disaster recovery plan is not proven end to end. In January 2015, the Bank entered into an Enterprise Services (ES) contract with IBM in order to address this risk, however until that work is completed the Bank is exposed to a higher rise of an IT failure causing material disruption to the Bank's products and services. There are considerable execution risks in a project of this scale and complexity. The Bank's regulators are fully aware of the steps the Bank is taking to address these operational risks as discussed on page 26. **Many of the Bank's business, operational, reporting and financial processes rely on significant manual intervention** which is inefficient and increases the risk of errors in the Bank's data and financial reporting. The Bank is subject to high levels of model risk which occurs as a direct result of weaknesses in the design or use of a model. **The Bank's systems of control have been weak** and although the foundations of more robust controls, including the revised and updated RMF, have been laid, this is taking more time than anticipated and significant work to embed across the organisation. These include the need to enhance general IT controls, including logical access and controls over the management of financial and customer data. Poor systems and manual processes, many of which have not been integrated following the Bank's merger with the Britannia in 2009 exacerbate this risk. Until the risk framework is fully embedded there is increased risk that inadequate risk management could lead to exposures outside the Bank's risk appetite, unanticipated losses and regulatory censure. **The Bank is in the process of separating from The Co-operative Group.** Currently, and into the medium term, the Bank depends on The Co-operative Group to provide a number of services including critical functions such as IT (until the ES arrangement with IBM described above becomes operational), personnel, assets and to on-supply certain services, data and assets by third party suppliers. The Bank also has significant counterparty exposure to The Co-operative Group. The ongoing separation project is complex and may be

		more costly than currently contemplated. The Bank faces legal, financial and reputational risk where legal proceedings are brought against it. Liability for damages may be incurred by the Bank where third parties are harmed by the conduct of the Bank's business. The Bank does not have a documented right to occupy a number of its main places of business which if unresolved could lead to disputes, additional cost and operational disruption.
Reputational risk	The risk associated with an issue which could in some way be damaging to the reputation of the Bank. Underlying issues amongst others arising as a result of: (i) the Bank's strategic decisions or business performance; (ii) an operational failure; or (iii) external perception. This may result in a requirement to hold additional liquidity in anticipation of a stress scenario, which is likely to negatively impact retained earnings over time and therefore capital resources.	**The Bank considers that its reputation as an ethically led organisation is critical to the success of the plan.** Generically, there is a risk that this reputation may be undermined. Specifically, the Bank's change in ownership structure and the necessity to make significant cost savings which will include inter alia branch closures and staff reductions increase this risk. The Bank will continue to rely on the Co-operative brand and therefore carries the risk that its brand will be damaged as a result of matters relating to The Co-operative Group. The Co-operative Bank trade mark belongs to the Bank. Please see the Corporate Governance Report on page 40 for a fuller explanation of the principles governing the Bank's right to use the trademark and the circumstances in which this could be challenged or removed.
Strategic and business risk	The risk arising from changes to the Bank's businesses and the environment in which it operates, specifically the risk of not being able to carry out the Bank's business plan and desired strategy. This may result in the Bank having to hold additional capital and/or liquidity. This risk is covered by many areas of capital in Pillar II, specifically execution, concentration and liquidity risk.	**The Bank's plan to focus on becoming a smaller Core Bank is unproven and is in the early stages of implementation. The Bank does not have a track record in successful execution of the large scale change necessary.** The plan involves concurrent transformational change, with a large component relating to IT, which may result in additional investment cost and delays to the plan. Any delay would require ongoing regulatory acceptance of these issues for a longer period of time which might not be forthcoming and could be withdrawn if the plan is not executed in line with regulatory expectations. In order to meet the plan accepted by the PRA, the Bank must deleverage its Non-core assets, in particular the Optimum portfolio, in accelerated time scales.

		Additional Tier 2 capital is contemplated by the Bank's revised plan. Further additional equity and/or debt capital may be required, beyond that contemplated currently, because of increased capital requirements (applicable to the Bank or banks generally), actual costs and losses exceeding those estimated in the Bank's plan or if the Bank does not deliver on its plan as anticipated. The Bank may be unable to raise any Tier 2 or other forms of capital it may need on favourable terms, when needed, or at all.
People risk	People risk is the risk associated with the recruitment, employment and management of individuals within the Bank. A significant portion of the Bank's cost base is staff costs and so managing this resource within budget is key to cost reduction and therefore to retained earnings. This risk is captured within the operational risk framework.	**The Bank continues to be subject to increased risk in this area.** The Bank continues to suffer an elevated risk of being unable to retain and recruit suitably qualified personnel. This increases execution risk in the plan and reduces historical corporate knowledge.
Regulatory risk	The risk of fines, public censure, limitation on business, requirements for legal or operational restructuring, or restitution costs arising from the failure to understand, interpret, implement and comply with UK and EU regulatory requirements.	**Along with the wider banking industry, the Bank must comply with multiple regulatory changes** which may add complexity to an already difficult technology, operational and prudential change programme. There is also a risk that changes to regulatory requirements affect the Bank's ability to successfully implement its plan. **The regulatory position of the Bank is described on page 26.** At the end of 2014, the Bank met its ICG, however this is a temporary position and the Bank will not sustainably meet its ICG until the later years of its Plan. The PRA has accepted this position. The Bank is under intense regulatory scrutiny and expects such scrutiny to continue. The Bank is also the subject of multiple regulatory and other investigations and enquiries into events at the Bank and circumstances surrounding them, including enforcement investigations by the FCA and PRA. These investigations and inquiries (see note 36 for more details) are likely to result in: significant expense which may include damages, fines and other penalties; even greater scrutiny from regulators; further regulatory action or litigation; significant resource drain; further adverse publicity and reputational damage.

Conduct risk	The risk that the Bank's behaviour, offerings or interactions will result in unfair outcomes for customers.	**The Bank is exposed to the inherent risks relating to the miss-selling of financial products**, acting in breach of regulatory principles or requirements and giving negligent advice or other conduct determined by the Bank or the regulators to be inappropriate, unfair or non-compliant with applicable law or regulations. Any failure to manage these risks adequately could lead to further significant provisions, costs and liabilities and/or reputational damage. The Bank's approach to provisions for historic miss-selling issues such as PPI, interest rate swaps and packaged accounts is based on the views and requirements of the regulator. Any change in the regulator's current approach, such as an extension of the period covered by the requirement for proactive contact with customers, could have a material impact. The Bank is continuing its programme of a structured risk based assessment, of which the primary focus is the discovery and remediation of existing and new conduct and legal issues. While much work has been undertaken and progress has been made in identifying conduct issues, no assurance can be given that further issues will not be identified, or that the already identified issues may not require further provision. Projects to remediate these issues are underway however are costly, complicated and require significant data extracts and IT support to implement. Delays or failure to successfully implement redress to customers increases the costs to the Bank and may lead to regulatory sanction. The Bank has initiated a redress programme in respect of various breaches of mortgage conduct of business rules. It is also the subject of a skilled persons review into potential detriment to its mortgage customers arising from, amongst other matters, arrears handling. The outcome of the review is uncertain but could potentially lead to enforcement investigations by the FCA. The Bank continues to be exposed to the risks of non-compliance with the Consumer Credit Act (CCA). While the Bank has identified certain instances where its documentation or processes have not been fully compliant with the technical requirements, there may be other instances of non-compliance which have not yet been identified. Until remediation of the issues

		already identified is complete, the Bank remains in breach of the technical requirements of the Act and will be unable to enforce interest charges on the affected products. The consequences of non-compliance with the CCA can include interest and default charges paid by a customer in prior periods being required to be refunded and the customer agreement not being enforceable by the Bank without a court order until the breach is remedied.
Pension risk	The risk to the Bank's capital and company funds from the Bank's exposure to scheme liabilities (to the extent liabilities are not met by scheme assets) and risks inherent in the valuation of scheme liabilities and assets.	**The Bank participates in two defined benefit pension schemes, both of which are currently in deficit and there is a risk that this will worsen over time:** • The Pace scheme, whose sponsoring employer is The Co-operative Group. The Bank is a participating employer in this scheme. • The Britannia scheme, now closed, whose sponsoring employer is CFSMS, guaranteed by the Bank. • Refer to note 35 for a more detailed discussion of the accounting for these schemes. • The Bank has agreed to a share of the deficit funding up to July 2015 as described in note 35 and a liability for this has been recognised on the balance sheet. Once the Banks's share of Pace liabilities has been agreed, the Bank will account for the scheme on a defined benefit basis. The Pace scheme is not currently sectionalised and operates on a 'last man standing' basis. The Bank's obligation to Pace would increase significantly if another large employer in the scheme were to become insolvent. There is uncertainty over how much the Bank will need to pay in the event of sectionalisation of the scheme. The Bank is in consultation in respect of closure of the defined benefit section of the scheme.

Statement of Directors' responsibilities in respect of the Annual Report and Accounts and the financial statements

The Directors are responsible for preparing the Annual Report and Accounts and the consolidated financial statements of The Co-operative Bank plc and its subsidiaries (the Bank) and parent company financial statements for The Co-operative Bank (the Company) in accordance with applicable law and regulations.

Company law requires the Directors to prepare Bank and Company financial statements for each financial year. Under that law they have elected to prepare the Bank and the Company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and applicable law.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Bank and Company and of their income statement for that year. In preparing each of the Bank and Company financial statements, the Directors are required to:

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

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Bank's and Company's transactions and disclose with reasonable accuracy at any time the financial position of the Bank and Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Bank and Company and to prevent and detect fraud and other irregularities.

The Directors are also responsible for preparing, in accordance with applicable laws and regulations, a Strategic Report, Directors' Report and Corporate Governance Statement that complies with that law and those regulations. The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Bank's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The Directors consider the Annual Report and Accounts and financial statements, taken as a whole, to be fair, balanced and understandable and provide the information necessary for shareholders to assess the Bank and Parent Company's performance, business model and strategy.

Disclosure of information to the Auditor

So far as the Directors are aware, there is no relevant Audit information of which the Bank's Auditor is unaware, and the Directors have taken all steps that they ought to have taken as Directors in order to make themselves aware of any relevant Audit information and to establish that the Bank's Auditor is aware of that information.

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and income statement of the Company and of the undertakings included in the consolidation taken as a whole; and
- the Directors' Report includes a fair review of the development and performance of the business and the position of the issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

By Order of the Board

Dennis Holt

Chairman

26 March 2015

The Bank income statement

For the year ended 31 December 2014

All amounts are stated in £m unless otherwise indicated

	2014	Restated 2013
Interest receivable and similar income	**1,051.8**	1,245.6
Interest expense and similar charges	**(706.8)**	(930.7)
Net interest income	**345.0**	314.9
Fee and commission income	**197.3**	219.9
Fee and commission expense	**(74.9)**	(72.1)
Net fee and commission income	**122.4**	147.8
Net trading (expense)/income	**(2.9)**	3.8
Other operating income	**2.4**	30.6
Operating income	**466.9**	497.1
Operating expenses		
Operating expenses	**(852.6)**	(847.3)
Provision for customer redress	**(52.3)**	(307.0)
Intangible asset impairment	**-**	(148.4)
Total operating expenses	**(904.9)**	(1,302.7)
Operating loss before impairment losses	**(438.0)**	(805.6)
Impairment gains/(losses) on loans and advances	**173.2**	(516.2)
Operating loss pre Liability Management Exercise	**(264.8)**	(1,321.8)
Profit from Liability Management Exercise	**-**	688.3
Operating loss post Liability Management Exercise	**(264.8)**	(633.5)
Share of post-tax profits from joint ventures	**0.6**	0.7
Loss before taxation	**(264.2)**	(632.8)

Income tax	**39.0**	(144.5)
Loss for the financial year	**(225.2)**	(777.3)
Attributable to:		
Equity shareholders	**(226.6)**	(778.2)
Non-controlling interests	**1.4**	0.9
	(225.2)	(777.3)
Loss per share (basic and fully diluted)	**(61.48)p**	(211.12)p

In 2013, £194.5m was disclosed separately on the face of the income statement as a deduction from interest receivable and similar income for conduct redress on certain loans. Similarly in 2013, £185.1m was disclosed separately on the face of the income statement as a deduction from fees and commission income.

As the Bank is not legally entitled to interest income and similar income in respect of customers affected by certain breaches of the technical requirements of the Consumer Credit Act (CCA), £104.5m of interest income collected in 2013 has been excluded from interest receivable and similar income and the line item has been re-presented. The remaining deductions of £90.0m of interest income and £185.1m of fee and commission income have been re-presented as charges within provisions for customer redress, which is what these amounts related to in 2013.

In total, £101.2m (2013: £411.5m) of conduct and legal provisions have been recognised during 2014. Further details are disclosed in note 33.

EPS for 2013 has been re-presented as described in note 14.

Comparative figures have been restated as described in note 3.

The Bank statement of comprehensive income

For the year ended 31 December 2014

All amounts are stated in £m unless otherwise indicated

				Restated		
	Equity shareholders	**Non-controlling interests**	**Total**	Equity shareholders	Non-controlling interests	Total
	2014	**2014**	**2014**	2013	2013	2013
(Loss)/Profit for the financial year	**(226.6)**	**1.4**	**(225.2)**	(778.2)	0.9	(777.3)
Other comprehensive (expense)/income that may be recycled to profit and loss:						
Changes in cash flow hedges						
Net changes in fair value recognised directly in equity	**43.1**	**(0.1)**	**43.0**	(39.9)	(0.7)	(40.6)

Income tax	**(6.4)**	**-**	**(6.4)**	9.3	0.2	9.5
Transfers from equity to income or expense	**11.5**	**-**	**11.5**	(13.7)	-	(13.7)
Income tax	**(2.3)**	**-**	**(2.3)**	3.2	-	3.2
Changes in available for sale assets						
Net changes in fair value recognised directly in equity	**63.8**	**-**	**63.8**	(32.7)	-	(32.7)
Income tax	**(15.7)**	**-**	**(15.7)**	7.6	-	7.6
Transfers from equity to income or expense	**(12.5)**	**(0.3)**	**(12.8)**	(24.8)	-	(24.8)
Income tax	**3.1**	**0.1**	**3.2**	5.6	-	5.6
Revaluation of equity shares	**-**	**-**	**-**	0.1	-	0.1
Income tax	**-**	**-**	**-**	0.1	-	0.1
Other comprehensive income/(expense) for the financial year, net of income tax	**84.6**	**(0.3)**	**84.3**	(85.2)	(0.5)	(85.7)
Total comprehensive (expense)/income for the financial year	**(142.0)**	**1.1**	**(140.9)**	(863.4)	0.4	(863.0)

The 2013 comparatives have been restated as described in note 3.

The Bank balance sheet

At 31 December 2014

All amounts are stated in £m unless otherwise indicated

		Restated	Restated
	2014	2013	2012
Assets			
Cash and balances at central banks	**4,765.3**	5,418.8	5,433.0
Loans and advances to banks	**1,608.4**	1,594.4	1,904.1
Loans and advances to customers	**25,377.4**	30,286.1	33,327.1
Fair value adjustments for hedged risk	**148.5**	106.3	354.2
Investment securities - loans and receivables	**18.1**	23.6	295.0
Investment securities - available for sale	**3,167.5**	2,732.4	3,789.4
Investment securities - fair value through income or expense	**1,236.9**	1,743.4	1,845.2

Investment securities - held for trading	**-**	-	960.2
Derivative financial instruments	**470.7**	555.8	818.8
Non-current assets classified as held for sale	**387.3**	-	-
Equity shares	**2.8**	5.8	5.7
Investments in joint ventures	**5.3**	4.7	3.9
Investment properties	**2.1**	164.1	173.0
Property, plant and equipment	**67.5**	115.2	113.4
Intangible assets	**103.7**	110.7	263.2
Amounts owed by other Co-operative Group undertakings	**-**	-	56.8
Other assets	**187.6**	480.9	70.3
Prepayments and accrued income	**12.2**	16.5	14.9
Current tax assets	**0.6**	-	172.6
Deferred tax assets	**21.0**	25.1	162.5
Total assets	**37,582.9**	43,383.8	49,763.3
Liabilities			
Deposits by banks	**615.4**	2,757.5	3,612.0
Customer accounts	**29,614.0**	32,463.3	35,884.4
Customer accounts - capital bonds	**263.8**	538.1	888.1
Debt securities in issue	**3,443.6**	4,207.6	4,716.2
Derivative financial instruments	**551.7**	538.6	967.6
Other borrowed funds	**196.4**	196.3	1,258.6
Amounts owed to other Co-operative Group undertakings	**-**	-	190.0
Other liabilities	**157.8**	202.9	104.0
Accruals and deferred income	**16.0**	54.1	20.1
Liabilities directly associated with non-current assets classified as held for sale	**7.9**	-	-
Provisions for liabilities and charges	**617.5**	549.7	137.9
Current tax liabilities	**0.3**	4.2	-
Deferred tax liabilities	**84.0**	103.0	121.4
Total liabilities	**35,568.4**	41,615.3	47,900.3
Capital and reserves attributable to the Bank's equity holders			
Ordinary share capital	**22.6**	12.5	410.0
Share premium account	**1,736.9**	1,359.8	8.8

Retained earnings	**(273.1)**	(46.4)	1,326.6
Available for sale reserve	**24.6**	(14.1)	30.0
Capital redemption reserve	**410.0**	410.0	-
Cash flow hedging reserve	**59.0**	13.1	54.2
	1,980.0	1,734.9	1,829.6
Non-controlling interests	**34.5**	33.6	33.4
Total equity	**2,014.5**	1,768.5	1,863.0
Total liabilities and equity	**37,582.9**	43,383.8	49,763.3

The 2013 and 2012 comparatives have been restated as described in note 3.

Approved by the Board on 26 March 2015

Dennis Holt, Chairman

Niall Booker, Chief Executive

The Bank statement of cash flows

For the year ended 31 December 2014

All amounts are stated in £m unless otherwise indicated

		Restated
	2014	2013
Cash flows used in operating activities		
Loss before taxation	**(264.2)**	(632.8)
Adjustments for:		
Decrease in prepayments and accrued income	**4.3**	4.7
(Decrease)/increase in accruals and deferred income	**(38.1)**	13.4
Interest payable in respect of other borrowed funds	**22.8**	96.0
Effect of exchange rate movements	**0.5**	(0.6)
Fair value movement on investment properties	**4.5**	8.0
Impairment (gains)/losses on loans and advances	**(170.9)**	517.3
Movements on investment impairments	**(20.0)**	(18.5)
Depreciation and amortisation	**40.0**	33.9
Impairment of intangible assets	**7.6**	142.0
Interest amortisation	**6.0**	(4.2)

Fair value movements and amortisation of investment securities	**(206.2)**	142.1
Impairment of property, plant and equipment	**14.7**	21.2
(Gain)/loss on disposal of property, plant, equipment and software	**(0.2)**	0.5
Non-cash effect of LME transaction	**-**	(688.3)
Loss on disposal of investment property	**1.2**	-
Unwind of fair value adjustments arising on transfer of engagements	**97.5**	52.1
Preference dividend	**-**	5.4
	(500.5)	(307.8)
Decrease in deposits by banks	**(2,142.1)**	(854.5)
Decrease in customer accounts and capital bonds	**(3,123.6)**	(3,863.2)
Decrease in debt securities in issue	**(764.0)**	(603.0)
Decrease in loans and advances to banks	**105.3**	54.5
Decrease in loans and advances to customers	**5,073.6**	2,941.8
Decrease in amounts owed by other Co-operative Group undertakings	**-**	(47.6)
Increase in amounts owed to other Co-operative Group undertakings	**-**	58.8
Net movement of other assets and other liabilities	**(236.2)**	95.8
Income tax received	**4.3**	45.0
Net cash flows used in operating activities	**(1,583.2)**	(2,480.2)
Cash flows from investing activities		
Purchase of tangible and intangible fixed assets	**(74.9)**	(55.7)
Proceeds from sale of property, plant and equipment	**8.3**	1.7
Proceeds from sale of investment property	**156.5**	1.3
Purchase of investment securities	**(2,279.0)**	(4,425.3)
Proceeds from sale and maturity of investment securities	**2,580.0**	6,681.2
Net cash flows from investing activities	**390.9**	2,203.2
Cash flows from financing activities		
Interest paid on other borrowed funds	**(22.8)**	(83.9)
Dividends paid to non-controlling interests	**(0.2)**	(0.2)
Preference share dividends paid	**-**	(5.9)
Capital Commitment received from the Co-operative Group	**313.0**	-
Costs incurred relating to the May 2014 Capital Raising	**(12.8)**	-
Cash proceeds relating to the May 2014 Capital Raising	**400.0**	145.0

Net cash flows from financing activities	**677.2**	55.0
Decrease in cash and cash equivalents	**(515.1)**	(222.0)
Cash and cash equivalents at the beginning of the financial year	**6,092.2**	6,314.2
Cash and cash equivalents at the end of the financial year	**5,577.1**	6,092.2
Cash and balances with central banks	**4,707.5**	5,352.6
Held for sale	**9.1**	-
Loans and advances to banks	**745.5**	634.6
Short term investments	**115.0**	105.0
	5,577.1	6,092.2

The cash flows differ from the Bank balance sheet movements as these movements include the non-cash unwinds of the fair value adjustments arising on the Britannia Building Society merger.

Following the change in the ownership of the Bank, amounts owed to and by Co-operative Group undertakings are classified as third party balances.

The 2013 comparatives have been restated as described in note 3.

The Bank statement of changes in equity

For the year ended 31 December 2014

All amounts are stated in £m unless otherwise indicated

	Attributable to equity holders of the Bank								
	Share capital	**Share premium**	**Available for sale reserve**	**Cash flow hedging reserve**	**Capital redemption reserve**	**Retained earnings**	**Total**	**Non-controlling interest**	**Total equity**
2014									
Balance at the beginning of the year (as restated)	**12.5**	**1,359.8**	**(14.1)**	**13.1**	**410.0**	**(46.4)**	**1,734.9**	**33.6**	**1,768.5**
Total comprehensive (expense)/ income for the year	**-**	**-**	**38.7**	**45.9**	**-**	**(226.6)**	**(142.0)**	**1.1**	**(140.9)**
Transactions with owners recorded directly in equity:									
Issuance of new share capital	**10.1**	**377.1**	**-**	**-**	**-**	**-**	**387.2**	**-**	**387.2**

Dividend	**-**	**-**	**-**	**-**	**-**	**(0.1)**	**(0.1)**	**(0.2)**	**(0.3)**
Balance at the end of the year	**22.6**	**1,736.9**	**24.6**	**59.0**	**410.0**	**(273.1)**	**1,980.0**	**34.5**	**2,014.5**
2013									
Balance at the beginning of the year (as restated)	410.0	8.8	30.0	54.2	-	1,326.6	1,829.6	33.4	1,863.0
Total comprehensive (expense)/ income for the year	-	-	(44.1)	(41.1)	-	(778.2)	(863.4)	0.4	(863.0)
Cancellation of share capital	(410.0)	-	-	-	410.0	-	-	-	-
Issuance of new share capital	12.5	777.5	-	-	-	-	790.0	-	790.0
Transfer of retained earnings to share premium	-	594.8	-	-	-	(594.8)	-	-	-
Transaction costs	-	(21.3)	-	-	-	-	(21.3)	-	(21.3)
Dividend	-	-	-	-	-	-	-	(0.2)	(0.2)
Balance at the end of the year (as restated)	12.5	1,359.8	(14.1)	13.1	410.0	(46.4)	1,734.9	33.6	1,768.5

During the year a securitisation vehicle was closed and a dividend payment of £0.1m (2013: £nil) was made to its respective holding company. This amount was subsequently paid out to charitable organisations.

The 2013 comparatives have been restated as described in note 3.

Notes to the Bank financial statements

For the year ended 31 December 2014

All amounts are stated in £m unless otherwise indicated

1. Basis of preparation and significant accounting policies

1.1. Basis of preparation

Both the Company financial statements and the Bank financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), and as adopted by the European Union (EU).

On including the parent company financial statements within the Bank's Annual Report and Accounts, the Company is taking advantage of the exemption in Section 408 of the Companies Act 2006 not to present its individual income statement and related notes that form a part of these approved financial statements.

The financial statements have been prepared under the historic cost convention as modified by the revaluation of available for sale financial assets, derivative contracts, investment properties and certain other financial assets and financial liabilities held at fair value. The Bank applies the recognition, measurement and disclosure requirements of IFRS in issue that are endorsed by the EU and are effective for accounting periods beginning on or after 1 January 2014.

The financial statements comprise all audited sections of the accounts. Where indicated, the risk management section on pages 85 to 130 and capital management section on pages 131 to 137 form part of the audited accounts.

Standards and interpretations issued and effective

In preparing this consolidated financial information, the Bank has adopted the following pronouncements during the year that are new or revised:

- IFRIC 21 (Levies (2013))

This interpretation gives guidance on the recognition of a liability to pay a levy that is accounted for in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets. A levy is an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation other than outflows of resources covered by other standards, fines or other penalties that are imposed for breaches of the regulation. The obligating event that gives rise to a liability to pay a levy is the activity that triggers the payment of the levy, as identified by the legislation. The Bank adopted this interpretation from 1 January 2014, when recognising the Financial Services Compensation Scheme (FSCS) Levy. The impact of the application has been to increase brought forward reserves at 1 January 2013 by £24.8m as the FSCS Levy will be recognised annually on 1 April, rather than the date upon which the Bank’s share of the levy is calculated as a proportion of the total market protected deposit, being 31 December.

- IFRS 10 (Consolidated Financial Statements (2011))

This new standard introduces a single consolidation model for all entities based on control, irrespective of the nature of the investee. It supersedes both IAS 27 (Consolidated and Separate Financial Statements (2008)) except where IAS 27 still applies as noted below, and Amended SIC 12 (Consolidation: Special Purpose Entities (2004)). It aims to provide transparency in identifying off-balance sheet, parent subsidiary relationships, using a consistent basis for determining the existence and thus consolidation of those underlying entities being controlled by the reporting entity. The amendment to IFRS 10 has not had a material impact on the 2014 financial statements of the Bank.

- IFRS 11 (Joint Arrangements (2011))

This new standard establishes principles for financial reporting by parties to a joint arrangement. It supersedes both IAS 31 (Interests in Joint Ventures (2010)) and Amended SIC 13 (Jointly Controlled Entities: Non-Monetary Contributions by Venturers (2007)). Recognition criteria now distinguish between joint operations and joint ventures on their relative ‘rights and obligations’ scope. A joint operation interest is accounted for between assets, liabilities, revenue and expense, whilst a joint venture is restricted to equity accounting. The amendment to IFRS 11 has not had a material impact on the financial statements of the Bank.

- IFRS 12 (Disclosure of Interests in Other Entities (2011))

This new standard applies to entities that have an interest in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity. It aims to provide disclosure transparency on the reporting entity’s risks associated with its interests in other entities, in conjunction with IFRS 10’s application which determines the existence of such entities. A number of unconsolidated securitisation holding companies have been identified where the Bank is considered the sponsor of such entities. Disclosure has been made in note 2 in relation to such entities.

- Amended IAS 27 (Consolidated and Separate Financial Statements (2011))

This amendment occurs as a direct consequence of IFRS 10’s issuance, which now acts as the new single authority on consolidation requirements. IAS 27’s scope has therefore reduced and focuses more specifically on separate financial information accounting bases. Under IAS 27, an entity shall therefore prepare its separate financial information using one of two bases; either at cost or in accordance with IFRS 9 (or IAS 39 if an entity has not yet adopted IFRS 9). The amendment to IAS 27 has no material impact on the financial statements of the Bank.

- Amended IAS 28 (Investments in Associates and Joint Ventures (2011))

This amendment occurs as a direct consequence of IFRS 10's issuance, which now acts as the new single authority on consolidation requirements. IAS 27's scope has therefore reduced and focuses more specifically on separate financial information accounting bases. Under IAS 28, an entity shall therefore prepare its separate financial information using one of two bases; either at cost or in accordance with IFRS 9 (or IAS 39 if an entity has not yet adopted IFRS 9). The amendment to IAS 28 has no material impact on the financial statements of the Bank.

- Amendments to IAS 32 (Offsetting Financial Assets and Financial Liabilities)

The current offsetting model in IAS 32 requires an entity to offset a financial asset and financial liability only when the entity currently has a legally enforceable right of set-off and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously. This amendment clarifies the position when offsetting financial assets and financial liabilities. The legal right of set-off must be available today and legally enforceable for all counterparties in the normal course of business, as well as in the event of default, insolvency or bankruptcy. The amended disclosures requires more extensive disclosures than are currently required. The disclosures focus on quantitative information about recognised financial instruments that are offset in the balance sheet, as well as those recognised financial instruments that are subject to master netting or similar arrangements irrespective of whether they are offset. The amendment to IAS 32 has no material impact on the financial statements of the Bank.

- Amendment to IAS 36 (Recoverable Amount Disclosures for Non-financial Assets (2013))

This amendment changes the disclosure requirements of IAS 36 when the recoverable amount is based on fair value less costs of disposal. The amendment removes the requirement to disclose the recoverable amount when a cash generating unit (CGU) contains goodwill or indefinite life intangible assets where there has been no impairment. In addition, the amendment requires additional information about the fair value measurement when the recoverable amount of impaired assets is based on fair value less cost of disposal. The new amendment requires detailed disclosure of how the fair value less costs of disposal has been measured when an impairment loss has been recognised or reversed. The amendment to IAS 36 has no material impact on the financial statements of the Bank.

- Amendment to IAS 39 (Novation of derivatives and continuation of hedge accounting (2013))

This amendment allows hedge accounting to continue where a derivative, which has been designated as a hedging instrument, is novated to effect clearing with a central counterparty as a result of laws or regulation, if specific conditions are met. The amendment to IAS 39 has no material impact on the financial statements of the Bank.

Standards and interpretations issued but not yet effective

At the date of authorisation of these financial statements, the Bank has not applied the following new and revised IFRSs, that have been issued but are not yet effective and, in some cases, not yet adopted by the EU.

- IFRS 9 (Financial Instruments (2014))

This new standard was issued in July 2014 and supersedes IAS 39 Financial Instruments: Recognition and Measurement. The standard includes requirements for recognition and measurement, impairment, de-recognition and general hedge accounting. The standard also supersedes IFRS 9 (2009), IFRS 9 (2010) and IFRS 9 (2013).

Due to the short period of time which has elapsed since the issue of the standard, the Bank has not yet estimated the financial effects, although it is expected that IFRS 9 will have a significant impact for the Bank, in line with the wider industry. The standard is mandatory for years beginning on or after 1 January 2018 but is available for early adoption subject to EU endorsement.

- Amendments to IFRS 10 (Consolidated financial statements) and IAS 28 (Investments in associates and joint ventures (2014))

These amendments address an inconsistency between the requirements in IFRS 10 and those in IAS 28 in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The main consequence of the amendments is that a full gain or loss is recognised when a transaction involves a business (whether it is housed in a subsidiary or not). A partial gain or loss is recognised when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary.

The amendments are mandatory for years beginning on or after 1 January 2016 but are available for early adoption subject to EU endorsement. The impact to the Bank of the amendments is likely to be immaterial.

- Amendment to IFRS 11 (Joint arrangements: on acquisition of an interest in a joint operation (2014))

This amendment adds new guidance on how to account for the acquisition of an interest in a joint operation that constitutes a business. The amendments specify the appropriate accounting treatment for such acquisitions.

The amendment is mandatory for years beginning on or after 1 January 2016 but is available for early adoption subject to EU endorsement. The impact to the Bank of the amendment is likely to be immaterial.

- IFRS 15 (Revenue from Contracts with Customers (2014))

This standard was issued in May 2014 and is a converged standard from the IASB and FASB on revenue recognition. IFRS 15 specifies how and when an IFRS reporter will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. This standard supercedes IAS 18 (Revenue) and a number of revenue related Interpretations.

The standard will be effective for annual reporting years beginning on or after 1 January 2017 subject to EU endorsement. The impact to the Bank of the amendments is likely to be immaterial as income from IAS 39 financial instruments is outside the scope of IFRS 15, however, the Bank has not yet finalised its estimation of the financial effects.

- Amendment to IAS 16 (Property, plant and equipment) and IAS 38 (Intangible assets: on depreciation and amortisation (2014))

In this amendment the IASB has clarified that the use of revenue based methods to calculate the depreciation of an asset is not appropriate because revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. The IASB has also clarified that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset.

The standard is mandatory for years beginning on or after 1 January 2016 but is available for early adoption subject to EU endorsement. The impact to the Bank of the amendments is likely to be immaterial.

- Amendments to IAS 27 (Separate financial statements: on the equity method (2014))

These amendments allow entities to use the equity method to account for investments in subsidiaries, joint ventures and associates in their separate financial statements.

The standard is mandatory for years beginning on or after 1 January 2016 but is available for early adoption subject to EU endorsement. The impact to the Bank of the amendments is likely to be immaterial.

- Amendments to IAS 1 (Presentation of Financial Statements)

The narrow-focus amendments to IAS 1 Presentation of Financial Statements clarify, rather than significantly change, existing IAS 1 requirements. In most cases the proposed amendments respond to overly prescriptive interpretations of the wording in IAS 1. The impact to the Bank of the amendments is likely to be immaterial.

Other standards and interpretations have been issued but these are not considered to be relevant to the Bank’s operations.

The Bank intends complying with standards from the date they become effective.

1.2. Financial Reporting Council

The following disclosures were made in the 2013 Annual Report and Accounts as a result of enquiries by the Conduct Committee of the Financial Reporting Council.

- The PRA's assessment of the Bank's capital requirements which were disclosed in the Bank's 4 November 2013 prospectus. Due to the specific circumstances of the Bank similar updated disclosures were included in the 2013 Annual Report and Accounts.
- Clarification of the nature of the acquisition fair value adjustment made in respect of loans acquired in the merger with the Britannia Building Society.
- Comparative fair value disclosures for loans and advances at 31 December 2012 using the revised valuation methodologies applied at 31 December 2013.
- Recognition of the investment in the new core IT banking system as an intangible asset of the Bank as at 31 December 2012 by way of a prior period adjustment and disclosure of the rationale for this change in treatment.

The disclosures have been presented in the 2014 Annual Report and Accounts where relevant.

1.3. Going Concern

a. Introduction

These financial statements are prepared on a Going Concern basis. The Directors have a reasonable expectation that the Bank will have the resources to continue in business for the foreseeable future, taking into account the matters referred to below.

The assessment of the appropriateness of using the Going Concern basis of accounting has been subject to a thorough process involving analysis and discussion by management, Executive and Board Committees and the Board, in line with our governance processes, and discussion with the PRA and FCA. This analysis included a particular focus on the 12 month period ending 31 March 2016.

Following the capital shortfall identified in 2013, and the subsequent successful capital raising exercises, the Bank is now in the early stages of its turnaround.

The completion of the capital raising exercises removed elements of uncertainty around the Going Concern status of the Bank. However, whilst important steps, these are not in themselves sufficient to recapitalise the Bank in the long term. There continue to be material uncertainties around the Bank's ability to continue as a Going Concern which relate to the implementation of the plan as discussed in (e) below. In particular, the Bank needs ongoing regulatory acceptance of the Bank's position until the IT platform is remediated and the Bank has rebuilt its capital strength to be able to withstand a significant stress.

The 2015-2019 plan was reviewed and accepted by the PRA following the Stress Test Results (Stress Test) announced on 16 December 2014. This plan has been designed to enable the Bank to withstand a stress of the severity of the Stress Test by the end of the plan period and involves reshaping and restructuring the business as a core relationship bank.

b. The plan

The Co-operative Bank is a recognised brand and continues to maintain a loyal customer base. Our strategy is to reshape the business as a core relationship bank providing straightforward business banking and retail banking services to individuals and SMEs. Restructuring the business, including a reduction in head office costs, to drive a significant reduction of the cost base is an important part of the overall strategy.

A key element of the reshaping of the business is the reduction in the Non-core banking business and assets, which currently carry the majority of the Risk Weighted Assets of the Bank. Reducing the Risk Weighted Assets of the Bank will improve its CET1 and leverage ratios.

The revised plan, accepted by the PRA, accelerates the reduction in RWAs via expediting deleverage of the Optimum portfolio.

c. Capital

Following receipt of the final component of the £313m Capital Contribution on 31 December 2014, the Bank met the Individual Capital Guidance (ICG) for total capital set by the PRA at the end of the year, however it is not forecast to sustainably remain compliant for most of the duration of the 2015-2019 planning period. The PRA has reviewed and accepted the 2015-2019 plan as revised following the Bank of England Stress Testing announcements.

Total CRD IV capital resources as at 31 December 2014 are £1.9bn (31 December 2013 £1.3bn) with Core Tier 1 capital after regulatory deductions of £1.6bn (31 December 2013 restated £1.1bn). The Bank's CET1 ratio stands at 13.0% (31 December 2013 restated 7.2%) on a CRD IV end point basis.

d. Liquidity

Since 31 December 2013, the liquid asset ratio has increased to 17.4% as at 31 December 2014 (31 December 2013 restated: 16.1%). This liquid asset ratio increase is due to a reduction in total assets, despite a decrease in primary liquidity. The Bank continues to maintain a liquidity position above regulatory minima and in excess of its internal risk appetite.

During the period to 31 December 2014, the Bank has actively managed a reduction in customer deposits with a reduction in customer assets. Within the aggregate customer deposit reduction in the period to 31 December 2014, Core Retail customer deposits decreased by £2.2bn. The Bank has also repaid bilateral facilities and repo funding during the course of the year, and optionally redeemed the Silk Road Finance Number two securitisation in September 2014 of £500m.

e. Risks and uncertainties

Key risks associated with successful execution of the plan include:

1. On 20 December 2013, the Bank began the process of separating its operations from its former parent, the Co-operative Banking Group Limited, and its ultimate former parent, The Co-operative Group, with both of which it shares premises, systems and services. The work is complex and time consuming and despite forecasting that separation costs will be higher than originally envisaged, there remains a risk that the costs of executing these separation plans may increase. The potential misalignment of Group and Bank's objectives may also make separation slower and more costly than anticipated;
2. The Bank participates in The Co-operative Group's defined benefit pension scheme (Pace). As long as the Bank remains a participating employer in Pace, the Bank could be 'last man standing' in the event of the failure of one or more of the other participating employers meaning that some or all of Pace's liabilities would need to be borne by the Bank. In addition, a material difference to current estimates of the funding of the pension scheme, or the Bank being forced to pay for a greater proportion than currently envisaged, could cause the Bank to require further capital in addition to that referred to above;
3. The Bank's IT system has been underinvested for a considerable period of time. The Bank needs to urgently and significantly improve and re-engineer its existing IT platform as the existing infrastructure is unsuitable and inherently fragile. There are also concerns about its resilience as the Bank's IT disaster recovery plan is not proven end to end. The Bank has entered into, in January 2015, an Enterprise Services (ES) contract with IBM in order to address this risk, however until that work is completed the Bank is at risk of an IT failure causing material disruption to Bank's products and services. The required improvement and re-engineering of the Bank's IT platform and operational process is necessary and significant in scale, complexity and cost in common with any programme of this scale it carries a significant level of execution risk. Any delays in, or failure by, the Bank to deliver the re-engineering of the Bank's IT platform may result in ongoing risk of technology failure, significant additional investment costs, subject the Bank to further regulatory scrutiny or sanction and impact the Bank's ability to deliver its strategy. The Bank's regulators are fully aware of the steps the Bank is taking to address these operational risks;
4. More generally, the ability of the Bank to achieve the results set out in the 2015-2019 plan. In this respect particular challenges include (but are not limited to): ability to achieve the targeted cost savings; ability to retain customers and deposits; the timing and quantum of impacts to capital from the asset reduction exercise; meeting its planned improvements in net interest margin; the ability of the Bank to generate sufficient Core Bank asset growth; a possible further deterioration in the quality of the Bank's asset portfolio; unplanned costs from (for example) conduct risk matters, regulatory investigations, IT investment and the ability to maintain the Bank's access at an appropriate cost to liquidity and funding;
5. The ability of the Bank to raise additional non-CET1 capital assumed in the plan; and
6. To move forwards with its plan, the Bank requires the regulators' ongoing acceptance of its inability to meet regulatory requirements and expectations, including ICG. To the extent this is

not forthcoming or to the extent that the Bank does not perform in line with its Business plan or regulatory capital requirements are increased for any reason, additional CET1 capital may be required over and above that included in that plan in order for the Bank to remain a Going Concern, and the PRA or FCA could exercise their powers under the Banking Act of 2009.

f. Conclusion

The Directors have concluded that, despite lower than expected losses and higher CET1 for the year ended 31 December 2014, the risks set out above, and their consequential effects, represent a material uncertainty which may cast doubt upon the Bank's ability to continue as a Going Concern. The Bank may, therefore, be unable to continue realising its assets and discharging its liabilities in the normal course of business. Nevertheless, after making enquiries and considering the current forecasts, in particular those for the period up to and including 31 March 2016, the Directors have a reasonable expectation that the Bank will have adequate resources to continue in business over this period. For these reasons, they continue to adopt the Going Concern basis in preparing these financial statements. This set of financial statements does not include the adjustments that would result if the Bank was unable to continue as a Going Concern.

1.4. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods, inclusive of assets recognised where the Bank is subject to the substantial risks and rewards of those assets.

1. Business combinations

On 1 August 2009, The Co-operative Bank plc merged with Britannia Building Society, with Britannia transferring their engagements to the Bank. This business combination has been accounted for applying the requirements of IFRS 3 (Business Combinations (2004)).

The consideration transferred was valued by reference to the members' interests acquired. Financial assets and liabilities which, following the Bank's accounting policies, would be carried at amortised cost, were brought onto the balance sheet at their fair value at acquisition and were subsequently carried at amortised cost using the effective interest rate method. The income statement includes the results of the engagements transferred from Britannia since the date of acquisition.

2. Basis of consolidation

a. Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists whenever the Company is exposed to, or has rights to, variable return from its involvement in an entity and has the ability to affect those returns through its power over the entity. In assessing control, potential voting rights that presently are exercisable are taken into account. The financial information of subsidiaries is included in the consolidated financial information from the date that control commences until the date that control ceases.

The financial information has been prepared using uniform accounting policies and is based on the same accounting period as the Company.

Intra-group balances and transactions, and any unrealised gains and losses arising from intra-group transactions, are eliminated in preparing the consolidated financial information.

Special Purpose Entities (SPEs) are entities that are created to accomplish a narrow and well defined objective; for the Bank this includes:

- various securitisation transactions in which mortgages were sold to SPEs. The equity of these SPEs is not owned by the Company; and
- Covered Bond Limited Liability Partnerships created in order to act as a guarantor for the issue of covered bonds.

An SPE is consolidated if, based on an evaluation of the substance of its relationship with the Bank and the SPE's risks and rewards, the Company concludes that it controls the SPE.

The following circumstances may indicate a relationship in which, in substance, the Company controls and consequently consolidates an SPE:

- the activities of the SPE are being conducted on behalf of the Company according to its specific business needs so that the Bank obtains benefits from the SPE's operation;

- the Company has the decision making powers to obtain the majority of the benefits of the activities of the SPE;
- the Company has the rights to obtain the majority of the benefits of the SPE and therefore may be exposed to the risks incidental to the activities of the SPE; or
- the Company retains the majority of the residual or ownership risks related to the SPE or its assets in order to obtain benefits from its activities.

The above circumstances apply to all Company SPEs. Consequently the Company consolidates each SPE.

The assessment of whether the Company has control over an SPE is carried out at inception. No further assessment of control is carried out unless changes in the structure or terms of the SPE or additional transactions between the Bank and the SPE occur.

b. Interests in joint ventures

A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement, have rights to the net assets of the arrangement.

Those parties are called joint venturers. The Bank's interests in joint ventures are accounted for using the equity method. The consolidated financial information includes the Bank's share of the income and expenses and equity movements of equity accounted investees, after adjustments to align the accounting policies with those of the Bank.

c. Interests in unconsolidated structured entities

Unconsolidated structured entities are unconsolidated entities that have been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity. The Bank does not consolidate structured entities where the Bank does not control the structured entity. The Bank acts as a sponsor for certain unconsolidated securitisation vehicle holding companies which the Bank neither owns nor controls. The Bank has determined itself a sponsor of unconsolidated securitisation vehicle holding companies if the Bank does not have a material ongoing interest in the entity, but it may act to protect its reputation in relation to the structured entity. No income has been received from unconsolidated structured entities during the year (2013: £nil). The carrying value of all assets transferred to unconsolidated structured entities during the year is £nil (2013: £nil).

3. Revenue recognition

a. Interest income and expense

Interest income and expense is recognised on an EIR basis, inclusive of directly attributable incremental transaction costs and fees including arrangement and broker fees, valuation and solicitor costs, discounts and premiums where appropriate.

The EIR basis spreads the interest income and expense over the expected life of each instrument. The EIR is the rate that, at the inception of the instrument, exactly discounts expected future cash payments and receipts through the expected life of the instrument back to the initial carrying amount. When calculating the EIR, the Bank estimates cash flows considering all contractual terms of the instrument (for example, prepayment options) but does not consider assets' future credit losses except for assets acquired at a deep discount.

For assets acquired at a value significantly below the carrying value in the acquiree's financial information because they have incurred loss, expectations of future loss are higher than at origination, and interest spreads have widened because of deteriorating market conditions, the calculation of EIR is the same as shown above with the exception that the estimates of future cash flows include credit losses.

Early redemption charges are recognised on a cash basis as received.

b. Fees and commissions

Fee and commission income is predominantly made up of arrangement and other fees relating to loans and advances to customers that are included in the effective interest calculation.

Commitment fees received are deferred and included in the EIR calculation upon completion or taken in full at the date the commitment period expires and completion does not occur.

All other fee and commission income, such as loan closure fees or arrears fees, not included in the effective interest calculation, is recognised on an accruals basis as the service is provided.

Fees and commissions payable to introducers in respect of obtaining lending business, where these are direct and incremental costs related to the issue of a financial instrument, are included in interest income as part of the effective interest rate.

4. Financial instruments (excluding derivatives)

a. Recognition

The Bank initially recognises loans and advances when they are advanced to customers. Deposits, debt securities issued and other borrowed funds are recognised on the date at which they are originated.

Regular way purchases and sales of financial assets are recognised on the trade date at which the Bank commits to purchase or sell the asset. All other financial assets and liabilities are initially recognised on the trade date at which the Bank becomes a party to the contractual provisions of the instrument.

b. Derecognition

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial assets expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

When a financial asset is derecognised in its entirety, the difference between the carrying amount and the sum of the consideration received (including any new asset obtained less any new liability assumed), and any cumulative gain or loss that had been recognised in other comprehensive income, is recognised in the income statement.

When available for sale financial assets are derecognised, the cumulative gain or loss, including that previously recognised in reserves, is recognised in the income statement.

A financial liability is derecognised when the obligation is discharged, cancelled or expires. Any difference between the carrying amount of a financial liability derecognised and the consideration paid is recognised through the income statement.

c. Financial assets

i. Overview

The Bank classifies its financial assets (excluding derivatives) as either:

- loans and receivables;
- available for sale; or
- financial assets at fair value through profit or loss.

ii. Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and the Bank does not intend to sell immediately or in the near term. These are initially measured at fair value plus transaction costs that are directly attributable to the financial asset. Subsequently, these are measured at amortised cost using the effective interest rate method. The amortised cost is the amount advanced less principal repayments, plus or minus the cumulative amortisation using the EIR method of any difference between the amount advanced and the maturity amount less impairment provisions for incurred losses.

Loans and receivables mainly comprise loans and advances to banks and customers (except where the Bank has elected to carry the loans and advances to customers at fair value through income or expense as described in accounting policy (4.c) iv. below) and assets reclassified from available for sale (see below).

The Bank has a number of facility agreements with multiple counterparties, which form a single contractual relationship. The Bank considers these arrangements to be single financial instruments and accounts for these accordingly within loans and advances or customer deposits respectively.

iii. Available for sale

Available for sale financial assets are debt securities and equity shares that are not held for trading and are intended to be held for an indefinite period of time. These are initially recognised on their trade date, measured at fair value based on current bid prices where quoted in an active market. Where the debt securities and equity shares are unlisted the fair values are based on valuation techniques including discounted cashflow analysis, with reference to relevant market rates, and other commonly used valuation techniques. Movements in fair value are recorded in equity as they occur. On disposal, gains and losses recognised previously in equity are transferred to the income statement. In exceptional circumstances, for instance where the market in the securities has become inactive, the Bank has reclassified such assets as loans and receivables.

Any transfer back from loans and receivables, upon reclassification, would be measured at fair value based on current bid prices where quoted in an active market. Where there is no active market or the debt securities or equity shares are unlisted the fair values are based on valuation techniques including discounted cashflow analysis, with reference to relevant market rates, and other commonly used valuation techniques.

iv. Financial assets at fair value through profit or loss

These are:

- Financial assets designated at fair value through profit or loss

Financial assets designated at fair value are assets which have been designated to eliminate or significantly reduce a measurement and recognition inconsistency or where management specifically manages an asset or liability on that basis, eg capital bonds.

These assets are measured at fair value based on current bid prices where quoted in an active market. Where there is no active market or the securities are unlisted the fair values are based on valuation techniques including discounted cashflow analysis, with reference to relevant market rates, and other commonly used valuation techniques. Gains and losses arising from changes in the fair value are brought into the income statement within trading income as they arise.

- Financial assets held for trading

Financial assets held for trading are assets which have been principally acquired for the purpose of selling or repurchasing in the near term, or they form part of a portfolio of identified financial instruments that are managed together for which there is evidence of a recent pattern of short term profit taking. These financial assets are recognised on the date of trade, when the Bank enters into contractual arrangements with counterparties to purchase or sell financial instruments, and are normally derecognised when sold. Measurement is initially at fair value, with transaction costs taken to the income statement. Subsequently their fair values are remeasured, and gains and losses from changes therein are recognised in the income statement within trading income.

d. Financial liabilities

i. Overview

Financial liabilities are contractual obligations to deliver cash or another financial asset. Financial liabilities are recognised initially at fair value, net of directly attributable transaction costs.

Financial liabilities, other than derivatives and capital bonds, are subsequently measured at amortised cost.

Capital bonds within customer accounts have been designated at fair value through profit or loss upon initial recognition in the balance sheet. Changes in fair value are recognised through the income statement.

The capital bonds are economically hedged using equity linked derivatives, which do not meet the requirements for hedge accounting. Recording changes in fair value of both the derivatives and the related liabilities through the income statement most closely reflects the economic reality of the transactions. In doing so this accounting treatment eliminates a measurement inconsistency that would otherwise arise from valuing the capital bonds at amortised cost and the derivatives at fair value.

ii. Other borrowed funds

Borrowings are recognised initially at fair value, which equates to issue proceeds net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the borrowings using the EIR method.

The Bank classifies capital instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instruments. The Bank's preference shares were classified as financial liabilities as they carried the right to a fixed non-cumulative preferential dividend and were subsequently presented in other borrowed funds. The dividends on these preference shares were recognised in the income statement as interest expense on an amortised cost basis using the EIR method.

As part of the LME on 20 December 2013, all the preference shares were transferred to The Co-operative Group (via the Banking Group). The Co-operative Group waived its rights to income and capital under the preference shares. Accordingly, the preference shares have been extinguished as financial liabilities in the 2013 balance sheet even though they have not been redeemed.

iii. Perpetual subordinated bonds

Perpetual subordinated bonds were carried at their nominal value plus any premium and a fair value adjustment for hedged risk where items were designated as part of a fair value hedge relationship. Interest payable on perpetual subordinated bonds was recognised in the income statement using the EIR method.

The perpetual subordinated bonds were cancelled and, therefore, extinguished as financial liabilities on 20 December 2013 as part of the LME.

5. Impairment provisions

a. Assessment

i. Objective evidence

At the balance sheet date, the Bank assesses its financial assets not at fair value through profit or loss, for objective evidence of an impairment loss.

Objective evidence that financial assets are impaired can include significant financial difficulty of the borrower, a breach of contract, such as default or delinquency in interest or principal payments, the granting by the Bank to the borrower, for economic and legal reasons relating to the borrower's financial difficulty, a concession that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy or other financial reorganisation, or the disappearance of an active market for a security.

The Bank considers evidence for impairment for loans and advances at both a specific asset and collective level.

ii. Forbearance

The Bank operates a policy of forbearance which mitigates against borrower default. All such cases are included within its provisioning methodology.

- Residential secured mortgages

Loans under forbearance are subject to a specific identified impairment assessment.

- Unsecured retail business

Irrespective of forbearance, impairment is charged in accordance with the identified past due and unidentified loss event approaches described on page 102.

- Corporate business

All accounts subject to forbearance which are in default and on the watchlist are individually assessed for impairment.

For further information on the Bank's approach to forbearance, its management and execution, see the risk management section on page 104.

b. Scope

i. Individual accounts

All secured loans and advances are assessed for impairment using a range of criteria graded for levels of risk. Accounts at risk of impairment are monitored and impaired where they display clear indicators of underperformance.

All corporate loans on watchlist, or in default, are individually assessed for impairment.

Loans and advances that do not meet the criteria for individual impairment are collectively assessed for impairment (incurred but not yet reported) by grouping together loans and advances of similar risk characteristics.

ii. Collective accounts

a. Retail

When assessing collective impairment for secured retail loans, the Bank estimates incurred losses on mortgages based on the borrower's external credit score or where the loan is specifically identified as being subject to forbearance.

When assessing collective impairment for unsecured retail loans, the Bank estimates losses on loans with delinquency greater than a pre-determined trigger point. In addition, the Bank makes provision on all loans arising from fraud and loans transferred to debt collection agencies. In respect of unsecured loans, the Bank uses statistical modelling of historical trends of probability of default, timing of recoveries and the amount of loss incurred.

The model's results are adjusted for management's judgement as to whether current economic and credit conditions are such that actual losses are likely to differ from those suggested by historical modelling. Once impaired, accounts are subjected to higher levels of impairment according to both their relevant stage of delinquency, i.e. the number of days in arrears, and their consequent likelihood of ultimately being charged off. Default rates, loss rates and future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

b. Corporate

All loans other than those to which a specific provision has been applied are included in the corporate collective calculation. The collective provision applied is to multiply the drawn balance of the loan by an estimated propensity for the loan to default (PD) during a loss emergence period by the estimated Loss Given Default (LGD). A 100% propensity to default is applied for all commercial real estate loans where the indexed loan-to-value (LTV) is greater than 100% and to those loans which are due to contractually expire in the next 12 months and the indexed LTV is greater than 65%. All other PDs are based on recently observed loan migration experience or regulatory PDs where these are deemed to be more appropriate. Loans which are on watchlist will therefore have a higher PD than those cases in the live book.

c. Measurement

The amount of the loss is the difference between:

- the asset's carrying amount; and
- the present value of estimated future cash flows (discounted at the asset's original or variable EIR for amortised cost assets and at the current market rate for available for sale assets).

Where the debt is secured, the assessment reflects the expected cash flows from the realisation of the security, net of cost to realise, whether or not foreclosure or realisation of the collateral is probable.

d. Impairment of financial assets carried at amortised cost

The amount of the impairment loss on assets carried at amortised cost is recognised immediately through the income statement and a corresponding reduction in the value of the financial asset is recognised through the use of an allowance account.

A write off is made when all or part of a claim is deemed uncollectable or forgiven after all the possible collection procedures have been completed and the amount of loss has been determined. Write offs are charged against previously established provisions for impairment or directly to the income statement.

Any additional recoveries from borrowers, counterparties or other third parties made in future periods are offset against the write off charge in the income statement once they are received.

Provisions are released at the point at which it is deemed that, following a subsequent event, the risk of loss has reduced to the extent that a provision is no longer required.

e. Impairment of financial assets classified as available for sale

Available for sale assets are assessed at each balance sheet date to see whether there is objective evidence of impairment. In such cases, any impairment losses are recognised by transferring the cumulative loss that has been recognised directly in equity to income or expense.

When a subsequent event causes the amount of impaired loss on available for sale investment securities to decrease, and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through the income statement.

However, any further recovery in fair value of an impaired available for sale equity security is recognised directly in equity.

6. Offsetting

Financial assets and financial liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to do so and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

7. Sale and repurchase agreements

Securities sold subject to repurchase agreements (repos) are reclassified on the balance sheet as pledged assets when the transferee has the right by contract or custom to sell or repledge the assets. The liability to the transferee is also included on the balance sheet, in deposits by banks. The difference between sale and repurchase price is accrued over the life of the agreements using the EIR method.

Securities purchased under agreements to re-sell (reverse repos) are classified as loans and advances to banks on the balance sheet, as appropriate.

8. Derivative financial instruments and hedge accounting

a. Derivatives used for asset and liability management purposes

Derivatives are used to hedge interest and exchange rate exposures related to non-trading positions. Instruments used for hedging purposes include swaps, forward rate agreements, futures, options and combinations of these instruments. The Bank also uses equity derivatives to hedge the equity risks within its capital bonds.

Derivative financial instruments are stated at fair value based on quoted market prices in active markets and, where these are not available, using valuation techniques such as discounted cashflow models. Further information is provided in note 40. All derivatives are carried as assets when the fair value is positive and liabilities when the fair value is negative. The gain or loss on re-measurement to fair value is recognised immediately in the income statement except where derivatives qualify for cash flow hedge accounting.

Where hedge accounting is applied, the Bank formally documents the relationship between the hedging instrument(s) and hedged item(s) including the risk management objective and strategy in undertaking the hedge transaction together with the method used to assess effectiveness of the hedging relationship.

The Bank makes an assessment, both at the inception of the hedge relationship as well as on an ongoing basis, as to whether the hedging instruments are expected to be ‘highly effective’ on offsetting the changes in fair value or cash flows of the respective hedged items during the period for which the hedge is designated, and whether the actual results of each hedge are within a range of 80% to 125%.

i. Cash flow hedges

Where derivatives are designated as hedges of the exposure to variability in cash flows of a recognised asset or liability, or a highly probable forecast transaction, the portion of the fair value gain or loss on the derivative that is determined to be an effective hedge is recognised directly in equity. The ineffective part of any gain or loss is recognised in the income statement immediately.

The accumulated gains and losses recognised in equity are reclassified to the income statement in the periods in which the hedged item will affect profit or loss. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss recognised at that time remains in equity until the forecast transaction is eventually recognised in the income statement.

When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was recognised in equity is immediately reclassified to the income statement.

ii. Fair value hedges

Where a derivative is designated as the hedging instrument to hedge the change in fair value of a recognised asset or liability or a firm commitment that could affect profit or loss, changes in the value of the derivative are recognised immediately in the income statement together with changes in the fair value of the hedged item that are attributable to the hedged risk.

Fair values are based on quoted market prices in active markets or, where these are not available, using valuation techniques such as discounted cash flow models. If the derivative expires or is sold, terminated, or exercised, or no longer meets the criteria for fair value hedge accounting, or the designation is revoked, then hedge accounting is prospectively discontinued. Any adjustment up to that point, to a hedged item for which the EIR method is used, is amortised to income or expense as part of the recalculated EIR of the item over its remaining life.

iii. Fair value hedge accounting for a portfolio hedge of interest rate risk

As part of its risk management process the Bank identifies portfolios whose interest rate risk it wishes to hedge. The portfolios may comprise only assets, only liabilities or both assets and liabilities. The Bank analyses each portfolio into repricing time periods based on expected repricing dates, by scheduling cash flows into the periods in which they are expected to occur. Using this analysis, the Bank decides the amount it wishes to hedge and designates as the hedged item an amount of assets or liabilities from each portfolio equal to this.

The Bank measures monthly the change in fair value of the portfolio relating to the risk that is being hedged. Provided that the hedge has been highly effective, the Bank recognises the change in fair value of each hedged item in the income statement with the cumulative movement in its value being shown on the balance sheet as a separate item, fair value adjustment for hedged risk, either within assets or liabilities as appropriate. If the hedge no longer meets the criteria for hedge accounting, this amount is amortised to the income statement over the remaining average useful life of the hedge item.

The Bank measures the fair value of each hedging instrument and this is included in derivative financial instruments in either assets or liabilities as appropriate, with the change in value recorded in the income statement.

Any hedge ineffectiveness is recognised in the income statement as the difference between the change in fair value of the hedged item for the hedged risk and the change in fair value of the hedging instrument.

b. Embedded derivatives

A derivative may be embedded in another instrument, known as the host contract. Where the economic characteristics and risks of an embedded derivative are not closely related to those of the host contract (and the host contract is not carried at fair value through income or expense), the embedded derivative is separated from the host and held on-balance sheet at fair value.

Movements in fair value are recognised in the income statement, whilst the host contract is accounted for according to the relevant accounting policy for that particular asset or liability.

c. Derivatives used for trading purposes

Derivatives entered into for trading purposes include swaps, forward rate agreements, futures, options and combinations of these instruments. Derivatives used for trading purposes are measured at fair value and any gains or losses are included in the income statement. The use of derivatives and their sale to customers as risk management products as appropriate, is an integral part of the Bank's trading activities.

9. Financial guarantee contracts

Financial guarantees, in respect of intra-group funding and the pension deficit in respect of the

Britannia Pension Scheme, are treated as insurance contracts in accordance with IFRS 4 (Insurance Contracts (2004)). In accordance with the standard, the recognised insurance liability is assessed based on the current estimate of forecast future cash flows. If this highlights that the liability is inadequate, the liability is increased and the corresponding charge taken through the income statement.

10. Property, plant and equipment

The Bank recognises assets where it is exposed substantially to all the risks and rewards of those assets.

Acquired computer software licences are capitalised on the basis of cost incurred to acquire and bring the software to use.

Items of property, plant and equipment are stated at cost less any accumulated depreciation and impairment losses. Depreciation is provided on a straight line basis at the following rates, which are estimated to write down the assets to realisable values at the end of their useful lives.

Freehold and long leasehold land and buildings	40–50 years
Freehold and leasehold improvements	10–40 years
Short leasehold buildings	life of lease
Equipment:	
Computer	3–7 years
Furniture and equipment	3–10 years

All items of property, plant and equipment are reviewed for indications of impairment on a regular basis and at each balance sheet date. If impairment is indicated, the asset's recoverable amount (being the greater of fair value less cost to sell and value in use) is estimated. Value in use is calculated by discounting the future cash flows generated from the continuing use of the asset.

If the carrying value of the asset is less than the recoverable amount, an impairment charge is recognised in the income statement.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment, and are recognised net within operating expenses in the income statement.

11. Intangible assets

The Bank recognises intangible assets where it is exposed substantially to all the risks and rewards of those assets.

a. Computer software

Computer software is stated at cost less cumulative amortisation and impairment and comprises computer software together with the costs of development of the software.

Acquired computer software licences are capitalised on the basis of cost incurred to acquire and bring the software to use.

Costs that are directly associated with the internal production of software products that will generate future economic benefit are capitalised. Only costs which meet the definition of development costs under IAS 38 (Intangible Assets) are capitalised, with costs being capitalised only if the asset can be reliably measured, will generate future economic benefits and there is an ability to use the asset. Expenditure that is not directly attributable to the development of such assets is recognised in the income statement in the period to which it relates.

The expenditure capitalised includes direct employee costs and an appropriate portion of relevant direct overheads. Amortisation is charged to the income statement on a straight line basis to allocate the cost over the estimated useful life up to a maximum of seven years.

b. Other intangible assets

Other intangible assets are stated at cost less cumulative amortisation and impairment. Amortisation is charged on a straight line basis over the useful life of the asset. For core systems, a review of the asset's useful life is carried out and a maximum useful life of up to ten years is applied.

c. Impairment

Intangible assets are assessed for indications of impairment at least annually. If impairment is indicated, the asset's recoverable amount (being the greater of fair value less cost to sell and value in use) is estimated. Value in use is calculated by discounting the future cash flows generated from the continuing use of the asset. If the carrying value of the asset is less than the greater of the value in use and the fair value less costs to sell, an impairment charge is recognised to this value in the income statement. Irrespective of whether there is any indication of impairment, intangible assets in the course of construction are tested for impairment at least annually.

12. Goodwill

All business combinations are accounted for by applying the purchase method. Goodwill represents amounts arising on acquisition of subsidiaries, associates and joint ventures and represents the difference between the cost of the acquisition and the fair value of the identifiable assets, liabilities and contingent liabilities acquired.

If a business combination is achieved without transfer of consideration, the amount of goodwill is calculated by reference to the fair value of the Bank's interest in the acquiree using a valuation technique. The technique involves assessing the future net cash flow of the acquiree and then discounting using a rate that reflects current market assessment of the time value of money and risks specific to the acquiree.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is not amortised but is tested for impairment on an annual basis. Where impairment is required, the amount is recognised in the income statement and cannot be subsequently reversed.

13. Leases

a. Overview

The Bank enters into leases for land and buildings and operating leases for vehicles and equipment.

Leases for land and buildings are split between leases for the land and leases for the buildings for accounting purposes only. The leases are separately assessed as to whether they are finance or operating leases.

The Bank's policy is to provide for the minimum future lease payments on buildings that it does not currently use, net of expected rental income from sub-leases. The Bank provides for dilapidation where an obligation exists to make good dilapidation or other damage, or return the asset to the configuration that existed at the inception of the lease.

b. Assets leased to customers

All leases of assets to customers are finance leases. Income from assets leased to customers is credited to the income statement based on a pattern reflecting a constant periodic rate of return on the net investment in the lease.

c. Assets leased from third parties

i. Finance leases

Finance lease assets are initially recorded at the lower of fair value and the present value of the minimum lease payments, and subsequently in accordance with the relevant policy for the underlying asset. An equal liability is recorded in other liabilities. Interest is allocated to the lease payments so as to record a constant periodic rate of charge on the outstanding liability.

ii. Operating leases

Operating lease payments are charged to the income statement on a straight line basis over the term of the lease and the asset is not recognised on the balance sheet.

14. Investment property

Property held for long term rental yields that is not occupied by the Bank, or property held for capital appreciation, is classified as investment property. Investment property comprises freehold land and buildings. It is carried at fair value. Fair value is based on current prices in an active market for similar properties in the same location and condition. No depreciation is provided on these properties. Any gain or loss arising from a change in fair value is recognised in the income statement.

If the Bank takes occupancy of an investment property, it is reclassified as property, plant and equipment and its fair value at the date of reclassification becomes its cost for subsequent accounting purposes. Similarly, transfers to the investment property portfolio are made when occupancy by the Bank ceases and the property meets the criteria of an investment property under IAS 40. Prior to such a transfer the property is measured at fair value with any gain or loss recognised in the income statement.

15. Cash and cash equivalents

Cash and cash equivalents comprises cash balances and balances with a maturity of three months or less from the acquisition date, which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Overdrafts that are repayable on demand and form an integral part of the Bank's cash management are included as a component of cash and cash equivalents for the purpose of the cash flow statement.

16. Income tax

a. Overview

Tax for the year comprises current and deferred tax, which is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in the statement of comprehensive income. In addition, estimated amounts receivable from tCG for tax losses surrendered and changes in that estimate are recorded as an adjustment to the tax expense.

b. Current tax

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

c. Deferred tax

Deferred tax is provided using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided for is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised and is supported by the Board's approved revised plan.

Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

17. Pension costs

a. Co-operative Pension Scheme

The Bank participates in The Co-operative Pension Scheme (Pace). Pace is a hybrid scheme, consisting of a defined benefit section and a defined contribution section. There is currently insufficient information available to consistently and reliably identify the Bank's share of its liability in respect of this multi-employer scheme. For this reason the pension costs in respect of Pace are accounted for on a defined contribution basis in accordance with IAS 19 Employee Benefits (revised 2011). Pension costs are recognised as an expense in the Bank's income statement. See note 35 for further details.

b. Britannia Pension Scheme

The Britannia scheme is a hybrid scheme, consisting of a defined benefit section and a defined contribution section. In 2009, following the transfer of engagements of Britannia Building Society, CFSMS, a Co-operative Group subsidiary, became principal employer of the scheme. The Bank and three wholly owned subsidiaries (Platform, WMS and Britannia International) are participating employers in this multi-employer scheme.

Following the separation of the Bank from the wider Co-operative Group, the Britannia scheme is now accounted for on a defined benefit basis within the accounts of the Bank. See note 35 for further details.

Accordingly, the Bank recognises the fair value of the scheme assets less the present value of the scheme's estimated obligations, discounted at a high quality corporate bond rate, less an asset restriction that reflects the Bank's inability to access the surplus in the scheme.

18. Foreign currency

The functional and presentational currency for the Bank is pound sterling. Transactions in foreign currencies are translated at the foreign exchange rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to sterling at the foreign exchange rate ruling at that date. Foreign currency differences arising on translation are recognised in the income statement, except for foreign currency differences arising on translation of available for sale equity instruments or a qualifying cashflow hedge, which are recognised directly in the statement of comprehensive income. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair values are translated to sterling at the exchange rates prevailing at the dates the values were determined.

19. Investments in Bank undertakings

Investments in subsidiaries are initially measured at fair value which equates to cost and subsequently valued at cost less impairment.

20. Provisions for liabilities and charges

A provision is recognised in the balance sheet if the Bank has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

In the case of restructuring provisions, a constructive obligation arises when a plan is sufficiently detailed and is formalised. Restructuring provisions include only direct expenditure arising from the restructuring plan which is both necessary and for restructuring and not associated with the Bank's ongoing activities.

Provisions are recognised for discounts on performing loans identified for disposal at the balance sheet date which will be sold post year end at a loss.

21. Share premium

Share premium is the amount by which the fair value of the consideration received exceeds the nominal value of shares issued. Expenses and commissions paid on the issue of shares are written off against the share premium of the same issue.

22. Assets held for sale

Non-current assets and disposal groups (including both the assets and liabilities of the disposal groups) are classified as held for sale when their carrying amounts will be recovered principally through sale, they are available for sale in their present condition and their sale is highly probable. Non-current assets held for sale and disposal groups are measured at the lower of their carrying amount and fair value less cost to sell, except for those assets and liabilities that are not within the scope of the measurement requirements of IFRS 5 Non-current Assets Held for Sale and Discontinued Operations such as deferred taxes, financial instruments, investment properties, insurance contracts and assets and liabilities arising from employee benefits. These are measured in accordance with the accounting policies described above. Immediately before the initial classification as held for sale, the carrying amounts of the asset (or assets and liabilities in the disposal group) are measured in accordance with applicable IFRSs. On subsequent remeasurement of a disposal group, the carrying amounts of the assets and liabilities noted above that are not within the scope of the measurement requirements of IFRS 5 are remeasured in accordance with applicable IFRSs before the fair value less costs to sell of the disposal group is determined.

2. Critical judgements and estimates

The preparation of financial information requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

The judgements and assumptions that are considered to be the most important to the portrayal of the Bank's financial condition are those relating to loan impairment provisions, conduct risk and legal provisions, deferred tax, pensions, hedge accounting, separation, effective interest rate (EIR) and interest recognition relating to breaches of technical requirements of the Consumer Credit Act.

a. Loan impairment provisions

i. Overview

The loan portfolios are reviewed on a regular basis to assess for impairment. In determining whether an impairment provision should be recorded, judgements are made as to whether there is objective evidence that a financial asset or portfolio of financial assets is impaired as a result of loss events that occurred after recognition of the asset and by the balance sheet date.

The calculation of impairment loss includes expectations of levels of future cash flows, and is based on both the likelihood of a loan or advance being written off and the estimated loss on such a write off.

The changes in impairment provisions for all books of business result from management review of assumptions, with respect to the determination and operational alignment of: The probability of the possession of collateral given default (PPD); treatment of forbearance; length of loss emergence periods; timing of impairment recognition and the formalising of charge off policy.

Further explanation of the treatment of forborne balances is included in the Bank's risk management disclosures.

The section below explains the methodology for loan impairment for both the Core (unsecured and secured residential) and Non-core (Corporate and Optimum) segments. Only the critical elements of judgement are discussed in detail.

ii. Collective provisions

Loans which have not been individually impaired are assessed for collective impairment. Collective provisions cover losses which have been incurred but not yet identified on loans subject to individual assessment and for homogeneous groups of loans that are not considered individually significant. Typically retail lending portfolios are assessed for impairment on a collective basis as the portfolios generally consist of large pools of homogenous loans.

a) Core

i) Unsecured and secured residential

The Bank's collective provision for unsecured and secured retail personal advances is £108.3m (2013: £164.7m). Loans are identified as impaired by taking account of the stage of the debt's delinquency, the product type and the regularity of payments made whilst in arrears. The provision is calculated using assumed probabilities of default (PD) and a loss given default (LGD) for unidentified impairment.

The provision rates reflect the likelihood that the debt will be written off or charged off at some point in the future. The PD and LGD parameters are based on historical experience and are subject to regular review.

A key estimate within the unsecured models is the probability that impaired accounts move to a default status during the outcome period. The model uses historical actual data over a defined period of time to arrive at an average probability of accounts moving to default. If the maximum PD had been used for each category of arrears and for each product, this would increase the collective provision by £5.8m for all of the unsecured portfolios.

A key estimate of the secured impairment model provisioning is forced sales discount. The forced sales discount is an average and is calculated using historical actual data over a defined outcome period. If the maximum forced sales discount for the outcome period was used to calculate the provision across the secured portfolios excluding Optimum it would increase by £6.8m.

There were no significant changes made to the collective provision methodology in 2014.

b) Non-core

i) Corporate

The Bank's collective provision against corporate loans in the Non-core division has decreased to £16.7m (2013: £40.0m).

The collective provision is calculated using factors such as observed default rates and LGD. As assessment is made of the likelihood of the loan becoming recognised as impaired in the loss emergence period and for loans that are impaired the likelihood of them moving to default over the outcome period. The calculation of the collective provision relies heavily on assumed probabilities of default.

There were no significant changes to the collective provision methodology in 2014 except for i) utilising property collateral for non-CRE customers when assessing their loss rates, and ii) the introduction of explicit discounting in assessing the proceeds of property sales.

The strategic deleveraging of the Bank's Non-Core assets in 2014 has been the primary reason for the reduction in the collective provision.

The impact of increasing the default rates by 10% is an increase of the collective by £2.1m. The impact of increasing other parameters that affect the loss rate by 10% is not significant.

ii) Optimum collective

In addition to the above, collective provisions of £12.4m (2013: £9.4m) are held in the Optimum segment of the Non-core business.

A key estimate is the collateral value. A 10% decrease to the indexed collateral value used in the model would increase the provision by £22.1m.

There were no significant changes made to the collective provision methodology in 2014.

Further explanation of collective loan impairment method is included in the Bank's risk management disclosures.

iii) Individual provisions

Individual provisions are recorded for loans which are assessed for impairment on an individual basis. Loans considered as individually significant are typically corporate loans.

a) Core

i) Unsecured and secured residential

Individual provisions for unsecured and secured residential lending total £4.5m (2013: £10.7m). There were no significant changes made to the provision methodology in 2014.

Sensitivities to the key estimates within the secured residential individual impairment model are disclosed in the risk management section.

b) Non-core

i) Corporate

The Bank's impairment provision on corporate loans totals £386.8m (2013: £698.4m). The provision has decreased reflecting improving macro economic factors and the Bank's strategic deleverage of Non-core assets.

The determination of individual impairment provisions requires the exercise of considerable management judgement involving matters such as economic conditions and the resulting trading performance of the customer and the value of security held, for which there may not be a readily accessible market. In particular, significant judgement is required by management in assessing the borrower's cash flows and debt servicing capability together with the realisable value of collateral. The actual amount of the future cash flows and their timing may differ from the assumptions made for the purposes of determining the impairment provision and consequently these provisions can be subject to change over time. A key estimate within the provision is collateral valuation. A 10% decrease in collateral values would increase the provision by £47.3m.

For further information on credit risk and impairment, see the Bank's risk management disclosures.

ii) Optimum individual

The Bank's individual impairment provision on Optimum mortgages is £9.5m (2013: £26.1m). Mortgage accounts are identified as impaired and provided for on an individual basis by taking account of the stage of the debt's delinquency.

There were no significant changes made to the provision methodology in 2014. The decrease in the provision reflects the improving quality of the loan book and improved House Price Index (HPI) values.

b. Conduct risk and legal provisions

i. Overview

The Bank has identified a number of conduct risk and legal issues against which it has raised provisions, based on management's best estimate of the total potential costs to the Bank.

Significant components of the conduct risk and legal provision are potential customer redress in relation to Payment Protection Insurance (PPI), interest rate swaps and breaches of the technical requirements of the Consumer Credit Act (CCA). The Bank has also made provision for conduct provisions which are individually less significant.

The calculation of these conduct and legal provisions requires significant judgement by management in determining appropriate assumptions. Other than relating to PPI and Interest Rate Hedging, the Bank is at an early stage of calculating and processing redress to customers and therefore the provisions have a high degree of sensitivity to changes in actual as opposed to forecast outcomes. This is due to a number of factors such as assumption made to compensate for incomplete historical data, or that the Bank has further work still to do to complete its review of all past products for possible compliance or conduct breaches. Consequently, eventual outcomes could vary significantly from current estimates which represent the Bank's best estimates based on currently available information. Key assumptions made in the estimation of provisions include basis of redress, operating costs of resolving redress, level of complaints, Bank uphold rates, proactive contact and response rates and the Financial Ombudsman Service referral and uphold rates.

Where reasonably possible changes in estimates can be reliably quantified, these are discussed in each section below.

ii. Payment Protection Insurance (PPI)

A provision of £73.6m (2013: £133.8m) has been recorded in respect of potential customer redress relating to past sales of PPI. The provision is in respect of the total expected cost of carrying out this work and paying compensation, making total provisions raised to date of £352m (2013: £347m).

The most significant factors behind the £5m increase are the calculation of single premium PPI redress based on full redress rather than redress based on an equivalent regular premium PPI and the application of further guidance from Financial Ombudsman Service in relation to late fees.

There are a number of key assumptions within the calculation of the current provision. The key assumptions within the calculation of the current provision are complaint volumes, uphold rates, administration costs, proactive response rate and retrospective redress.

The current position, expected movement in position and baseline sensitivities of the key estimates are outlined below:

Description of estimate	Current position	Future expected	Sensitivity on current position
Number of inbound valid (1) complaints	83,000	19,000	1,000 = £1.4m

Number of proactive mailings	41,000	9,000	1,000 = £1.5m
Response rate to proactive mailings	62%	70%	1% = £1.3m
Average uphold rate per valid (1) complaint	64%	63%	1% = £0.5m
Average redress per upheld complaint	£3,181	£2,015	£100 = £1.6m

(1) Valid complaints excludes those complaints for which no PPI policy exists.

These assumptions remain subjective, in particular due to the uncertainty associated with future claims levels. The resulting provision represents the best estimate of all future expected costs of PPI redress. However, it is possible the eventual outcome may differ from the current estimate and if this were to be material an adjustment to the provision will be made. The provision also includes an estimate of the Bank's claims handling costs and those costs associated with claims that are subsequently referred to the Financial Ombudsman Service.

iii. Interest rate hedging past business review

The Bank previously voluntarily agreed to participate in the FCA's Interest Rate Hedging (IRH) Past Business Review (PBR).

A provision of £14.8m (2013: £33.0m) for potential interest rate swap mis-selling has been recorded. The decrease in the provision reflects the utilisation of the provision in the period.

Calculations on redress have been performed based upon the latest guidance from both the FCA and a Skilled Person (as defined by the FCA). The final redress method has not, however, been confirmed in all cases.

There are a number of key assumptions within the calculation of the current provision. The key assumptions within the calculation of the current provision are the population of in scope swaps and the methodology to calculate redress provision. A potential change in overall outcomes, whilst considered unlikely, could increase the provision by £2.0m.

iv. Breaches of the technical requirements of the Consumer Credit Act (legal provision)

An amount of £169.4m (2013: £109.5m) has been provided regarding interest refunds following identification of breaches of the technical requirements of the CCA.

The increase in the provision reflects further interest chargeable on affected loans in accordance with relevant loan agreements which requires redressing, an updated estimate of the costs which will be incurred in delivering redress and an additional provision in relation to a further cohort of loans that have been identified as being non-compliant with the CCA. The provision will continue to increase in line with interest charged until the issue is resolved.

Assumptions for provisioning purposes are that the payment profile of loans was as per those agreed at drawdown. The provision covers all interest accrued during non-compliance to the end of December 2014.

Within the provision, operating costs of £17.6m are based upon the latest view of delivery timeframes.

v. Other conduct/compliance related provisions

Other conduct/compliance related provisions include the following:

- £17.8m (2013: £29.0m) for potential customer redress relating to the processing of first payments on certain mortgages;
- £24.0m (2013: £31.0m) relating to potential customer redress in relation to mortgage early redemption charges;
- £14.9m (2013: £26.1m) for alleged failings in the introduction of third party sales of card and identification protection products (as part of an industry wide review announced by the FCA on 27 January 2015);
- £20.0m (2013: £22.0m) relating to potential customer redress due to mortgage customer detriment;

- £34.8m (2013: £19.0m) for potential customer redress in relation to arrears fees and charges;
- £17.4m (2013: £nil) relating to packaged accounts;
- £15.0m (2013: £15.0m) relating to provision for potential conduct issues incurred but not identified;
- £7.0m (2013: £13.0m) relating to potential customer redress and other costs in relation to mortgage documentation;
- £15.2m (2013: £nil) relating to cost of mortgage redress; and
- £12.2m (2013: £10.9m) of other conduct provisions.

Key assumptions include basis of redress, operating costs of resolving redress, the level of complaints, uphold rates, proactive contact and response rates and Financial Ombudsman Service referral and uphold rates. The above provisions have a significant range of highly judgemental outcomes, the most significant of which reside within the provision for customer redress due to mortgage customer detriment and the provision for packaged accounts. Given the Bank is still in the process of identifying the population of affected customers it carries the inherent risk of forecasting for subjective final outcomes. A reasonably possible change by doubling the numbers of customers who have experienced detriment and increasing redress payments, could increase the provision for customer redress by £10.8m. Increasing the average number of fees in scope for redress for closed accounts over a longer period of time by circa 20% could increase the provision for packaged accounts by £3.6m.

c. Deferred tax

The Bank has recognised a deferred tax asset of £21.9m (2013: £25.1m restated) which includes £0.9m (2013: £nil) within a disposal group classified as held for sale. The Bank has recognised a deferred tax liability of £84.0m (2013: £103.0m restated). Deferred tax has been calculated using a tax rate of 20%.

The deferred tax asset relates to temporary differences arising on consolidation adjustments where the recoverability is not dependent on the future performance of the Bank and temporary differences in subsidiaries that are forecast to make taxable profits. The Bank has not recognised a deferred tax asset in respect of any other trading losses, capital losses or temporary differences as doubt exists over the availability of sufficient future taxable profits.

The Bank reviewed the deferred tax asset position of individual subsidiaries in the year and concluded that a deferred tax asset should be recognised in those subsidiaries which are forecast to make taxable profits against which other temporary differences can be offset under IAS 12 (Income Taxes). This, together with other deferred tax assets and liabilities previously unrecognised as at 31 December 2013, has resulted in the restatement of deferred tax assets as at 31 December 2013 of £25.1m and deferred tax liabilities of £10.5m (net increase in opening retained earnings as at 1 January 2014 of £14.8m).

d. Pensions

i. Defined contribution accounting for the Pace scheme

The Bank participates in Pace. Pace is a hybrid scheme, consisting of a defined benefit section and a defined contribution section. There is currently insufficient information available to consistently and reliably identify the Bank's share of its liability in respect of this multi-employer scheme. For this reason defined benefit accounting is not possible and pension costs in respect of Pace are accounted for on a defined contribution basis in accordance with IAS 19 Employee Benefits (revised 2011). Pension costs are recognised as an expense in the Bank's income statement.

A provision of £2.9m (2013: £nil) has been recognised in relation to the annual deficit funding which the bank has agreed to pay. This covers the period to July 2015. A further agreement on deficit funding may be reached at that point if the overall liability position has not been resolved by this point. See note 35 for further details.

ii. Defined benefit accounting for the Britannia scheme

The Britannia scheme is a hybrid scheme, consisting of a defined benefit section and a defined contribution section. In 2009, following the transfer of engagements of Britannia Building Society, CFSMS, a Co-operative Banking Group subsidiary, became principal employer of the scheme. The Bank and three wholly owned subsidiaries (Platform Funding Limited, WMS and Britannia International) are participating employers in this multi-employer scheme. This scheme is now closed.

Following further operational separation of the Bank from the wider Co-operative Group, the Britannia scheme was recognised on the Bank's balance sheet during 2014 and is now accounted for on a defined benefit basis.

The next full (triennial) actuarial funding valuation of the Britannia Pension Scheme, with effective date 5 April 2014, is currently ongoing. The deadline for agreement of funding position and contributions (ie the completion of the valuation) is 5 July 2015.

Further information on the financial implications of accounting for the Britannia scheme on a defined benefit basis is disclosed in note 35.

e. Hedge accounting

The Bank reviewed its hedge accounting methodology in the year and concluded that the method for calculating hedge ineffectiveness should be revised to better align with industry practices under IAS 39 (Financial Instruments: Recognition and Measurement). This has resulted in the recognition of an accounting loss in the year and a restatement of prior years (decrease of opening retained earnings as at 1 January 2014 of £9.3m).

These changes will result in additional accounting volatility in future financial periods, although this merely represents changes in the timing of recognition of profit or loss and not in the overall economic value of the hedge itself.

f. Interest recognition (CCA)

During 2013, technical breaches of the CCA were identified resulting in the Bank not being legally entitled to the interest on the loans subject to a breach. The Bank anticipates redressing customers and rectifying loan documentation throughout 2015, at which point the Bank becomes compliant with the CCA and the Bank can start recognising interest on the loans again.

The interest recognised on unsecured lending subject to a CCA breach was previously recognised within the interest income line, with an equal deduction for the amount recognised directly below interest income presented on the Income Statement. The presentation will be amended for the year and this income has not been recognised.

g. Separation provision

During November 2013, the Bank publically announced its intention to separate from The Co-operative Group. The Bank has recognised a provision of £112.3m (2013: £39.4m) in relation to separation costs which are eligible to be provided for under IAS 37 (Provisions, Contingent Liabilities and Contingent Assets).

The separation provision represents the costs directly related to the Bank's obligation to separate from The Co-operative Group. The calculation of the separation provision requires significant judgement by management in determining appropriate assumptions. Key assumptions include the day rate which will be paid to contract staff as part of the separation of Enterprise Services Programme and the overall time it will take to achieve separation. A reasonably possible change in overall estimates of cost for key separation provision judgements could increase the provision by £12.0m.

h. Effective Interest Rate and Fair Value adjustments

When calculating the EIR to apply to an asset or liability held at amortised cost, the Bank estimates future cash flows considering all contractual terms of an instrument. In most cases, the future cash flows arising from an asset or liability will be dependent on a number of variables, such as the proportion of mortgage customers who do not switch product after a discount period ends, or future interest rates set by the market. Therefore, it follows that management is required to apply significant judgement in creating assumptions about the value of these variables in the future.

In calculating the EIR adjustment to apply to mortgage balances, the most significant assumption in terms of impact and volatility is the assumed standard variable rate which will be in effect at the end of a fixed rate product term. This is determined with reference to expected Bank of England base rate rises, with a proportion of future increases assumed to pass through to the Bank's standard variable rate. As a measure of the sensitivity of this input, a 0.5% increase in the assumed standard variable rate in place at the end of all fixed rate products would result in a £5.2m (39%) increase in the EIR adjustment required to the loans and advances to customers balance as at 31 December 2014.

On the merger of the Bank and Britannia Building Society in August 2009 an exercise was undertaken to fair value the respective assets and liabilities of Britannia Building Society. These fair value adjustments are unwound on an EIR basis over the effective lives of the assets and liabilities. Management is required to apply significant judgement in determining the EIR assumptions which underpin the unwind profile of the fair value adjustments. The most significant assumption in terms of impact and volatility in determining the unwind profile for fair value adjustments is the remaining average lives of the related instruments.

The most significant fair value adjustment is that made to the Leek debt securities, which were valued below par upon merger. This adjustment has been unwinding towards the call date of the underlying Leek debt securities. As a measure of the remaining lives on these instruments, if the Leek notes were to be redeemed one month earlier than the call date, the Leek notes fair value adjustment would decrease by £13.1m (3.4%) as at 31 December 2014, resulting in an additional expense of £13.1m in the year to 31 December 2014.

3. Restatement

Hedge accounting

In accordance with its Accounting Volatility Management Strategy, the Bank elects to make use of different hedge accounting techniques in order to eliminate (as far as possible) any profit or loss generated purely through the implementation of accounting standards (as opposed to actual economic losses).

The Bank applies two types of hedge accounting: cash flow hedge accounting and fair value hedge accounting. These hedging methodologies are used on both a micro basis (one underlying asset or liability hedged by one derivative) and a macro basis (a portfolio of assets or liabilities hedged by a combination of derivatives).

The Bank has reviewed its hedge accounting strategies and the interpretations applied to hedge accounting in accordance with IAS 39 and best practice. Based on this review, the Bank has amended its calculation of hedge ineffectiveness resulting from these models and retrospectively restated prior year results for the change in methodology. The result of this change in policy is that the Bank now accounts for additional sources of accounting hedge ineffectiveness through the income statement (accounting hedge ineffectiveness may occur even though the hedge is economically perfect).

The effect of the change, together with a £2.2m credit tax adjustment related to hedge accounting, was to reduce retained earnings by £9.3m. This included a £7.0m increase to the opening balance at 1 January 2013. In 2013 the adjustments were a £14.6m charge to net interest income, a £9.8m charge to other operating income and a tax credit of £8.1m. The adjustment to the cashflow hedging reserve below includes a tax charge of £5.6m, giving a net tax credit of £2.5m.

IFRIC 21 Levies

The interpretation addresses the accounting for a liability to pay a levy if that levy is within the scope of IAS 37. It also addresses the accounting for a liability to pay a levy whose timing and amount is uncertain.

The guidance provided by IFRIC 21 has led to a change in the timing for the recognition of Financial Services Compensation Scheme (FSCS) levies that impact the Bank.

The FSCS provided compensation to consumers following the collapse of a number of deposit takers. The compensation paid out to consumers is currently funded through loans from the Bank of England and HM Treasury. In order to repay the loan principal, which is not expected to be recovered, the FSCS levies participating financial institutions.

The ultimate FSCS levy to the industry as a result of the collapses cannot currently be estimated reliably as it is dependent on various uncertain factors, including the potential recoveries of assets by the FSCS and changes in the level of protected deposits and the population of FSCS members at the time.

In previous years, the Bank recognised the FSCS levy in accordance with IAS 37 on the basis that the obligating event was being a deposit taker on the 31 December preceding the FSCS scheme year, so that in the 31 December 2013 ARA, an estimated provision in respect of the 2014/15 levy was recognised. IFRIC 21 clarified that the obligating event that gives rise to a liability to pay a levy is the event that triggers the payment of the levy, and this is the case even if the levy is calculated by reference to revenue generated in the previous period. As FSCS can only raise a levy within its scheme year, under IFRIC 21 the Bank should only recognise a provision in the scheme year itself. As such, the 2014/15 levy should be recognised in the Bank's 2014 ARA.

IFRIC 21 is applicable for accounting periods beginning on or after 1 January 2014. The change has been applied retrospectively and the comparatives restated accordingly.

The effect of the restatement was to reduce provisions and increase retained earnings by £26.3m, being a reduction in provisions of £24.8m and a credit to the income statement of £1.5m.

Corporate interest fair value

An interest fair value asset was recorded at the time of the merger of the Bank with the Britannia Building Society in 2009. This asset has been unwound in line with the expected behavioural lives of the assets. The Bank has reviewed the methodology and modelling of the unwind of this asset and has concluded that £23.7m of unwind related to 2013 in line with the impairment position and expected unwind profile at that point. This resulted in a £23.7m reduction in retained earnings.

Effective Interest Rate (EIR)

The Bank has reviewed its EIR models and methodologies in accordance with accounting standards and best practice. Based on this review, the Bank has amended its calculations and retrospectively restated prior years. This has resulted in a reduction in retained earnings and loans and advances to customers of £12.4m.

Deferred Tax Asset (DTA) recognition in subsidiaries

The Bank has reviewed its methodology for DTA recognition across all of the companies and has concluded that a DTA should be recognised in two of the Bank's subsidiaries, Platform Funding Limited (PFL) in 2013 and 2014, and Mortgage Agency Services Number Five Limited (MAS5) in 2013. No DTA has been recognised in MAS5 in 2014 due to the likelihood of an Optimum deleverage. All of the business of MAS5 relates to Optimum. This restatement, together with the restatement of other deferred tax positions previously unrecognised as at 31 December 2013, has resulted in a total restatement of DTA as at 31 December 2013 of £25.1m and deferred tax liabilities of £10.5m. The net impact is £14.6m, being a £12.1m increase in retained earnings and a £2.5m tax credit included in the hedge accounting adjustment of £9.3m.

Provisions for customer redress (CCA)

Included in the net interest income adjustment is the provision for customer redress, previously reported as part of net interest income. This has been re-presented, leading to an adjustment to the net interest income line of £104.5m. In addition, provisions for conduct redress in 2013 of £90.0m, £185.1m and £31.9m included within net interest income, fee and commission income and operating expenses respectively, have been aggregated and disclosed separately on the face of the income statement.

The effect of the prior year restatements on the Bank are:

Balance Sheet

	1 January 2013 (as reported)	Adjustments	**1 January 2013 (restated)**	31 December 2013 (as reported)	Adjustments	**31 December 2013 (restated)**

Assets						
Loans and advances to customers	33,339.5	(12.4)	**33,327.1**	30,322.2	(36.1)	**30,286.1**
Fair value adjustments for hedged risk	354.2	-	**354.2**	107.6	(1.3)	**106.3**
Deferred tax assets	159.6	2.9	**162.5**	-	25.1	**25.1**
Liabilities						
Debt securities in issue	4,713.7	2.5	**4,716.2**	4,195.3	12.3	**4,207.6**
Deferred tax liabilities	121.4	-	**121.4**	92.5	10.5	**103.0**
Provisions for liabilities and charges	162.7	(24.8)	**137.9**	576.0	(26.3)	**549.7**
Reserves						
Retained earnings	1,304.3			(39.4)		
Adjustment for EIR accounting		(12.4)			(12.4)	
Corporate fair value adjustment		-			(23.7)	
Deferred tax adjustment		2.9			12.1	
Adjustment for FSCS levy		24.8			26.3	
Adjustment for hedge accounting (1)		7.0			(9.3)	
	1,304.3	22.3	**1,326.6**	(39.4)	(7.0)	**(46.4)**
Cash flow hedging reserve	63.7	(9.5)	**54.2**	14.9	(1.8)	**13.1**

(1) The 2013 adjustment for hedge accounting includes a £2.5m credit relating to deferred tax.

As part of the reserves restatement deferred tax assets have been recognised.

Income statement

The hedge accounting and effective interest rate (EIR) restatement gives rise to a restated presentation of items within net interest income. The IFRIC 21 levies restatement gives rise to a restated presentation of items within operating expenses.

The impact of the restatements is shown below:

	31 December 2013 (as reported)	Restated	Re-presented	31 December 2013 (restated)
Net interest income – on loans and advances to customers	1,275.0	(23.7)	(104.5)	1,146.8
Net interest income – on financial instruments hedging assets	(114.4)	(14.6)	-	(129.0)
Other operating income	40.4	(9.8)	-	30.6
FSCS levies	(25.6)	1.5	-	(24.1)
Operating loss	(586.9)	(46.6)	-	(633.5)
Loss for the year before taxation	(586.2)	(46.6)	-	(632.8)
Income tax	(161.8)	17.3	-	(144.5)

The total impact of the IFRIC 21 levy adjustment as at 31 December 2013 is a reduction in the FSCS provision of £26.3m to £13.3m, and the charge of £1.5m. The cumulative impact on reserves is an increase of £26.3m.

4. Segmental information

The Bank is managed as two divisions – Core and Non-core. Core represents activity consistent with the strategy and risk appetite of the Bank. This includes Retail, Business and Commercial Banking (BaCB), Treasury and Other segments. Non-core business lines include activities not aligned with the current strategy of the Bank which are targeted for run down or exit.

Revenues are attributed to the segment in which they are generated. Transactions between the reportable segments are on normal commercial terms and internal charges and transfer pricing adjustments have been reflected in each segment.

Further detail of the components of the Core and Non-core segments is provided on page 14.

	Core					**Non-core**				
	Retail	**BaCB**	**Treasury**	**Other (1)**	**Total Core**	**Corporate CoAM**	**Optimum**	**Illius**	**Total Non-core**	**Total**
2014										
Net interest income	**396.3**	**46.1**	**(24.0)**	**13.4**	**431.8**	**9.3**	**43.2**	**(3.9)**	**48.6**	**480.4**
Losses on asset sales	**-**	**-**	**(2.1)**	**-**	**(2.1)**	**(11.1)**	**-**	**(1.2)**	**(12.3)**	**(14.4)**
Non-interest income	**105.2**	**14.9**	**(16.7)**	**-**	**103.4**	**17.2**	**4.7**	**2.8**	**24.7**	**128.1**
Operating income	**501.5**	**61.0**	**(42.8)**	**13.4**	**533.1**	**15.4**	**47.9**	**(2.3)**	**61.0**	**594.1**
Direct costs	**(161.9)**	**(15.1)**	**(13.3)**	**(9.2)**	**(199.5)**	**(18.8)**	**(3.1)**	**(4.2)**	**(26.1)**	**(225.6)**

Impairment gains on loans and advances	**1.9**	**1.6**	**-**	**-**	**3.5**	**152.6**	**15.6**	**-**	**168.2**	**171.7**
Contribution result	**341.5**	**47.5**	**(56.1)**	**4.2**	**337.1**	**149.2**	**60.4**	**(6.5)**	**203.1**	**540.2**
Operations and central costs										**(369.0)**
Project Costs										**(226.5)**
Operating result										**(55.3)**
PPI, conduct and legal risk provisions										**(101.2)**
Share of post-tax profits from joint ventures										**0.6**
Financial Services Compensation Scheme Levies										**(24.4)**
Fair value amortisation										**(83.9)**
Loss before taxation										**(264.2)**
Income tax										**39.0**
Loss for the financial year										**(225.2)**

Unity Trust Bank operates in the social economy and commercial banking sectors and is consolidated into the Bank's results on the basis of control. On 14 January 2014, it was announced that the Bank is in discussions with the Board of Unity Trust Bank about a potential sale of its 26.7% shareholding. Discussions continue but remain at an early stage and any decision on a changed ownership structure would be subject to regulatory approval. Unity Trust Bank plc is registered in England and operates in the UK.

	Core					Non-core				
	Retail	BaCB	Treasury	Other (1)	Total Core	Corporate CoAM	Optimum	Illius	Total Non-core	Total
2013 Restated										
Net interest income	428.1	69.5	(19.2)	8.8	487.2	16.6	(14.3)	(6.1)	(3.8)	483.4
Gains on asset sales	-	-	40.8	-	40.8	-	-	-	-	40.8
Non-interest income	123.7	14.9	(30.0)	2.2	110.8	29.3	5.7	0.7	35.7	146.5
Operating income	551.8	84.4	(8.4)	11.0	638.8	45.9	(8.6)	(5.4)	31.9	670.7
Direct costs	(180.3)	(23.7)	(11.2)	(6.8)	(222.0)	(18.2)	(2.2)	(4.7)	(25.1)	(247.1)

Impairment losses on loans and advances	(29.8)	(5.0)	-	(1.0)	(35.8)	(446.8)	(29.5)	-	(476.3)	(512.1)
Contribution result	341.7	55.7	(19.6)	3.2	381.0	(419.1)	(40.3)	(10.1)	(469.5)	(88.5)
Operations and central costs										(408.8)
Project Costs										(164.7)
Operating result										(662.0)
Intangible asset impairment										(148.4)
PPI, conduct and legal risk provisions										(411.5)
Share of post-tax profits from joint ventures										0.7
Financial Services Compensation Scheme Levies										(24.1)
Liability Management Exercise										688.3
Fair value amortisation										(75.8)
Loss before taxation										(632.8)
Income tax										(144.5)
Loss for the financial year										(777.3)

(1) The 2013 comparatives have been restated as described in note 3.

	2014	Restated 2013
Net interest income		
Total interest margin for reportable segments	**480.4**	483.4
Gains on asset sales	**1.6**	5.4
Interest fair value unwind	**(89.0)**	(69.4)
Provision for customer redress claims	**(48.0)**	(104.5)
Net interest income	**345.0**	314.9

Non-interest income		
Total non-interest income for reportable segments	**128.1**	146.5
(Losses)/gains on asset sales	**(16.0)**	35.4
Interest fair value unwind	**9.8**	0.3
Non-interest income	**121.9**	182.2
Comprising:		
Net fee and commission income	**122.4**	147.8
Net trading income	**(2.9)**	3.8
Other operating income	**2.4**	30.6
	121.9	182.2
Operating expenses		
Total direct costs for reportable segments	**(225.6)**	(247.1)
Interest fair value unwind	**(4.7)**	(6.7)
Operations and central costs	**(369.0)**	(408.8)
Project costs	**(226.5)**	(164.7)
Re-presentation of fraud costs	**-**	4.1
Provision for customer redress claim	**3.5**	-
Impairment re-classification	**(1.5)**	-
Provision for conduct risk	**(4.4)**	-
Financial Services Compensation Scheme Levies	**(24.4)**	(24.1)
Operating expenses	**(852.6)**	(847.3)
Interest fair value unwind		
Total interest unwind for reportable segments	**(83.9)**	(75.8)
Interest margin unwind	**89.0**	69.4
Non-interest income unwind	**(9.8)**	(0.3)
Operating expenses unwind	**4.7**	6.7
Interest fair value unwind	**-**	-

Impairment gains/(losses) on loans and advances

Total impairment gains/(losses) on loans and advances for reportable segments	**171.7**	(512.1)
Re-presentation of fraud costs	**-**	(4.1)
Impairment re-classification	**1.5**	-
Impairment gains/(losses) on loans and advances	**173.2**	(516.2)

The above table reconciles information used for management purposes, as disclosed in the detailed financial review with the statutory disclosures.

The 2013 comparatives have been restated as described in note 3.

They have also been re-presented in respect of costs, including fraud costs, to reflect the way these are now managed and reported within the Bank.

2014

	Core					**Non-core**				
	Retail	**BaCB**	**Treasury**	**Other**	**Total Core**	**Corporate CoAM**	**Optimum**	**Illius**	**Total Non-core**	**Total**
Segment assets	**14,611.4**	**620.0**	**9,729.4**	**515.4**	**25,476.2**	**3,930.1**	**6,822.9**	**-**	**10,753.0**	**36,229.2**
Unallocated assets										**1,069.8**
Total assets for reportable segments										**37,299.0**
Statutory adjustments										**283.9**
Bank total assets										**37,582.9**

2014

	Core					**Non-core**				
	Retail	**BaCB**	**Treasury**	**Other**	**Total Core**	**Corporate CoAM**	**Optimum**	**Illius**	**Total Non-core**	**Total**
Segment liabilities	**25,562.3**	**2,837.0**	**4,523.3**	**468.4**	**33,391.0**	**557.4**	**-**	**-**	**557.4**	**33,948.4**
Unallocated liabilities										**1,109.8**
Total liabilities for reportable segments										**35,058.2**
Statutory adjustments										**510.2**
Bank total liabilities										**35,568.4**

2013 (as restated)

	Core	Non-core

	Retail	BaCB	Treasury	Other	Total Core	Corporate CoAM	Optimum	Illius	Total Non-core	Total
Segment assets	16,790.9	844.9	10,491.4	441.0	28,568.2	5,646.1	7,326.1	162.2	13,134.4	41,702.6
Unallocated assets										1,557.9
Total assets for reportable segments										43,260.5
Statutory adjustments										123.3
Bank total assets										43,383.8

2013 (as restated)

	Core					Non-core				
	Retail	BaCB	Treasury	Other	Total Core	Corporate CoAM	Optimum	Illius	Total Non-core	Total
Segment liabilities	27,899.3	3,479.0	7,645.5	394.9	39,418.7	831.0	-	-	831.0	40,249.7
Unallocated liabilities										603.8
Total liabilities for reportable segments										40,853.5
Statutory adjustments										761.8
Bank total liabilities										41,615.3

Unallocated assets are non-customer assets and liabilities that are not allocated to a particular segment. Statutory adjustments mainly relate to the reallocation of provisions, accruals and prepayments and the gross up of mark-to-market values.

The 2013 comparatives have been restated as described in note 3.

7. Net Interest income

	2014	Restated 2013
Interest receivable and similar income		
On financial assets not at fair value through profit or loss:		
On loans and advances to customers	**1,052.6**	1,146.8
On loans and advances to banks	**24.1**	29.7
On investment securities	**75.8**	122.5

	1,152.5	1,299.0
On financial assets at fair value through profit or loss:		
Net interest expense on financial instruments hedging assets	**(119.7)**	(129.0)
Net interest income on financial instruments not in a hedging relationship	**19.0**	75.6
	1,051.8	1,245.6

The comparatives have been restated as described in note 3.

Included within interest receivable is £3.2m (2013: £14.2m) relating to profit on sale of investment securities – available for sale.

Interest income accrued on impaired financial assets during the year was £37.9m (2013: £43.5m). Interest due to unwinding of discount on impairment provisions relating to impaired financial assets amounted to £10.9m (2013: £10.7m).

	2014	Restated 2013
Interest expense and similar charges		
On financial liabilities not at fair value through profit or loss:		
On customer accounts	**(405.2)**	(484.3)
On bank and other deposits	**(247.8)**	(267.0)
On subordinated liabilities	**(22.8)**	(79.1)
On perpetual secured debt	**-**	(40.2)
	(675.8)	(870.6)
On financial liabilities at fair value through profit or loss:		
Net interest expense on financial instruments hedging liabilities	**(21.4)**	(24.1)
Net interest expense on financial instruments not in a hedging relationship	**(9.6)**	(36.0)
	(706.8)	(930.7)

The 2013 comparatives have been restated as described in note 3.

The Bank’s perpetual secured debt was extinguished on 20 December 2013 as part of the LME. The associated interest expense was therefore £nil during the year (2013: £40.2m).

Interest expense on bank and other deposits includes interest expense on deposits by banks and on debt securities in issue. It also includes fair value unwind on debt securities in issue of £109.2m (2013: £91.3m), further details of which are provided in note 40.

8. Net fee and commission income/(expense)

	2014	2013
Fee and commission income		
On items not at fair value through profit or loss	**197.2**	219.6
On trust or fiduciary activities that result from holding or investing in assets on behalf of others	**0.1**	0.3
	197.3	219.9

	2014	2013
Fee and commission expense		
On items not at fair value through profit or loss	**(74.8)**	(71.8)
On items at fair value through profit or loss	**(0.1)**	(0.3)
	(74.9)	(72.1)

11. Operating expenses

	2014	Restated 2013
Operating Expenses		
Staff costs	**304.1**	274.6
Administrative expenses	**296.7**	280.4
Depreciation of property, plant and equipment	**13.3**	16.4
Amortisation of intangible fixed assets	**26.7**	24.2
Impairment of property, plant and equipment	**6.3**	11.3
Impairment of brand intangible fixed assets	**3.1**	2.0
(Profit)/loss on sale of property, plant and equipment	**(0.2)**	0.5
Operating lease rentals	**25.6**	27.4
Financial Services Compensation Scheme Levies	**24.4**	24.1
Property provisions for liabilities and charges provided in the year	**2.1**	16.3
Other provisions for liabilities and charges provided in the year	**24.7**	35.0
Direct expenses from investment properties that generated rental income in the period	**3.6**	4.0
Direct expenses from investment properties that did not generate rental income in the period	**0.2**	0.1

The following items are included in operating expenses, which have been incurred outside the ordinary course of business:

	2014	2013
Investment, integration and rationalisation costs	**40.7**	71.3
Bank separation costs	**72.9**	39.4
Costs incurred in bid for Lloyds Banking Group branches	**-**	10.4
Impairment of property, plant and equipment	**8.4**	9.9
	122.0	131.0
Total operating expenses	**852.6**	847.3

Included within investment, integration and rationalisation costs is £4.5m (2013: £2.9m) of impairment of intangible fixed assets.

The Bank separation costs included in the table above are the net impact of a charge of £94.5m (2013: £39.4m) and a utilisation of £21.6m (2013: £nil).

The 2013 comparatives have been restated as described in note 3.

12. Staff costs

	2014	2013
Wages and salaries	**180.6**	190.3
Social security costs	**16.0**	14.6
Pension costs:		
Defined benefit plans	**4.9**	0.2
Defined contribution plans	**26.1**	28.5
Other staff costs	**76.5**	41.0
	304.1	274.6

Average number of employees

The average number of persons working for the Bank during the year is as follows:

	No. of employees 2014	No. of employees 2013
Full time	**4,772**	5,646
Part time	**1,630**	1,880

	6,402	7,526

Employees of the Bank were employed by CFS Management Services Limited (CFSMS) until 20 December 2013 and staff costs recharged to the Bank. At the beginning of 2014, the majority of the Bank employees had their employment contracts transferred from CFSMS to The Co-operative Bank plc. The transfer was required to support the legal separation of the Bank from The Co-operative Group. This transfer took place under the Transfer of Undertakings (Protection of Employment) Regulations 2006.

13. Income tax

	2014	2013 (restated)
Current tax		
Current year	**(22.3)**	(9.9)
Prior year	**7.8**	22.8
Total current tax	**(14.5)**	12.9
Deferred tax		
Current year	**(24.5)**	(13.3)
Write off of prior year deferred tax asset	**-**	148.2
Prior year	**-**	(3.3)
Total deferred tax	**(24.5)**	131.6
Total tax (credit)/charge	**(39.0)**	144.5

In addition to the above, included within other comprehensive income is a current tax charge of £12.5m (2013: tax credit of £13.3m restated) and a deferred tax charge of £8.7m (2013: tax credit of £12.5m restated).

Further information on deferred tax is presented in note 34. The tax on the Bank's loss before taxation differs from the theoretical amount that would arise using the corporation tax rate in the UK as follows:

	2014	2013 (restated)
Loss before taxation	**(264.2)**	(632.8)
Tax calculated at a rate of 21.49% (2013: 23.25%)	**(56.8)**	(147.1)
Effects of:		
Unrecognised deferred tax	**22.7**	115.9
Discount of group relief debtor	**(9.7)**	56.9

Adjustments to tax charge in respect of prior periods	**7.7**	19.5
Expenses not deductible for tax purposes	**(4.4)**	25.1
Change in rate of deferred tax	**1.8**	29.9
Other differences	**(1.8)**	0.4
Depreciation of capital expenditure not qualifying for capital allowances	**1.5**	2.5
Write off of prior year deferred tax asset	**-**	148.1
Non-taxable income	**-**	(116.3)
Difference in the tax rate at which current year group relief is expected to be recoverable	**-**	9.6
	(39.0)	144.5

The comparatives for 2013 have been restated as described in Note 3. This results in an increase in unrecognised deferred tax of £2.0m and a decrease in the write off of prior year deferred tax assets of £9.4m. Amounts receivable from The Co-operative Group for tax losses surrendered and changes in that amount are recorded as an adjustment to the tax expense.

14. Earnings per share

Basic earnings per share is calculated by dividing the net loss attributable to equity shareholders of the Bank by the weighted average number of ordinary shares in issue during the year.

	2014	Restated 2013
Loss attributable to equity shareholders of the Bank	**(226.6)**	(778.2)
Ordinary shares in issue (millions)		
At the beginning of the year	**250.0**	8,200.0
Shares cancelled	**-**	(8,200.0)
Issue of new ordinary shares	**200.5**	250.0
Issue of bonus shares	**1.0**	-
At the end of the year	**451.5**	250.0
Weighted average number of ordinary shares in issue (millions)	**368.6**	368.6
Basic losses per share (expressed in pence per share)	**(61.48)p**	(211.12)p

201.5m new shares were issued as part of the capital raising completed in May 2014 (see note 39 for details).

The 2013 weighted average number of shares has been adjusted for the 2013 cancellation of 8.2bn ordinary shares and the 2014 bonus share issue as required by IAS 33 (Earnings per share). 8.2bn of ordinary shares were cancelled in 2013 as part of the LME.

15. Non-current assets held for sale

a) Non-current assets classified as held for sale

	Non-current assets	Disposal group	**2014**	2013
Property, plant and equipment	9.1	41.0	**50.1**	-
Intangible assets	-	0.3	**0.3**	-
Loans and advances to customers	-	323.4	**323.4**	-
Cash and cash equivalents	-	9.1	**9.1**	-
Other receivables	-	4.4	**4.4**	-
	9.1	378.2	**387.3**	-

b) Liabilities directly associated with non-current assets classified as held for sale

	Disposal group	**2014**	2013
Other liabilities, accruals and deferred income	6.6	**6.6**	-
Current tax liabilities	1.0	**1.0**	-
Provision for liabilities and charges	0.3	**0.3**	-
	7.9	**7.9**	-

The non-current assets presented as held for sale relate to two transactions which are expected to complete in 2015 and have been approved by management:

i) The sale of a significant proportion of the ATM estate, in accordance with a sale agreement signed in November 2014. The ATMs are to be migrated to the purchaser on a phased basis with the Bank retaining the risks and rewards of ownership up to the point of transfer of each individual ATM; and
ii) The sale of Britannia House.

No impairment losses or gains were recognised on classification of Britannia House or ATMs as held for sale assets.

The disposal groups relate to three transactions which are highly likely to complete in 2015 and have been approved by the Board:

i) The proposed sale of Western Mortgage Services Limited (WMSL) shares or business as part of the Bank’s outsourcing of its mortgage processing services for all its residential mortgages. This proposed transaction was announced by the Bank on 11 November 2014;
ii) The sale of Southside Regeneration Limited (SRL) as part of a larger deleveraging deal; and

iii) The completion of a renewable energy asset portfolio sales contract which was exchanged during December 2014, under which the underlying borrowers cannot reasonably withhold consent.

No impairment losses or gains were recognised on classification as disposal groups.

Except for the renewable energy asset portfolio which is included in Corporate CoAM, all of the above disposal groups and held for sale assets are included within the Other Core segment in note 4.

16. Cash and balances at central banks

	2014	2013
Cash in hand	**218.0**	274.9
Balances with the Bank of England other than mandatory reserve deposits	**4,489.5**	5,077.7
Included in cash and cash equivalents	**4,707.5**	5,352.6
Mandatory reserve deposits with the Bank of England	**57.8**	66.2
	4,765.3	5,418.8

Mandatory reserve deposits are not available for use in the Bank’s day-to-day operations, are non-interest bearing and are not included in cash and cash equivalents.

17. Loans and advances to banks

	2014	2013
Items in course of collection from other banks	**63.3**	105.1
Placements with other banks	**682.2**	529.5
Included in cash and cash equivalents	**745.5**	634.6
Other loans and advances to banks	**862.9**	959.8
	1,608.4	1,594.4

18. a) Loans and advances to customers

	Classified as held for sale (1)	**Not classified as held for sale**	**Total 2014**	Restated 2013
Gross loans and advances	**323.4**	**25,917.3**	**26,240.7**	31,238.5

Less: allowance for losses	**-**	**(539.9)**	**(539.9)**	(952.4)
	323.4	**25,377.4**	**25,700.8**	30,286.1

(1) See note 15 for details of the loans and advances classified as held for sale. No loans and advances were classified as held for sale at 31st December 2013.

Loans and advances to customers include £182.7m (2013: £134.2m) of financial assets at fair value through profit or loss designated at initial recognition to eliminate or significantly reduce a measurement or recognition inconsistency, and £3.9m of financial assets held for trading (2013: nil). Of these, £78.4m (2013: £62.9m) are secured by real estate collateral.

Loans and advances to customers include £7,899.6m (2013: £10,111.9m) securitised under the Bank's securitisation and covered bond programmes. The Bank remains exposed to substantially all of the risks and rewards of ownership of these assets. Included within the Bank's deposits by banks are £10.1m (2013: £500.3m) of loans from external third parties and within the Bank's debt securities in issue are £2,876.5m (2013: £3,703.4m) of fixed and floating rate notes, all secured on these mortgage assets.

Loans and advances to customers have been restated as detailed in note 3.

Concentration of exposure

The Bank's exposure is virtually all within the UK. Further information on the concentration of exposure is included within the risk management disclosures.

Allowance for losses on loans and advances

	Core		**Non-core**		
	Individual	**Collective**	**Individual**	**Collective**	**Total**
2014					
At the beginning of the year	**10.7**	**167.8**	**724.5**	**49.4**	**952.4**
Balances with debt collection agencies	**-**	**39.6**	**-**	**-**	**39.6**
Release against profits for the year	**(1.5)**	**(3.3)**	**(147.3)**	**(20.3)**	**(172.4)**
Amounts written off	**(4.6)**	**(89.9)**	**(174.4)**	**-**	**(268.9)**
Unwind of discount allowance	**(0.1)**	**(4.2)**	**(6.6)**	**-**	**(10.9)**
Interest charged on impaired loans	**-**	**-**	**0.1**	**-**	**0.1**
At the end of the year	**4.5**	**110.0**	**396.3**	**29.1**	**539.9**

	2014
Net impairment credit shown in income statement	**(173.2)**
Amounts recovered against amounts previously written off	**2.3**
Provision against fair value adjustment for hedged risk	**(1.5)**
Release against profits shown above	**(172.4)**

The net impairment credit in the Bank's income statement is £173.2m (2013 charge: £516.2m). This includes amounts recovered by the Bank of £2.3m (2013: £1.1m) against amounts previously written off.

The impairment charge also includes a provision of £1.5m (2013: £9.8m) made against fair value adjustments for hedged risk during the year (as shown in the fair value adjustments for hedged risk tables).

Core provisions are analysed in further detail below:

	Core						
	Retail		BaCB		Other (1)		Total
	Individual	Collective	Individual	Collective	Individual	Collective	Core
2014							
At the beginning of the year	**2.8**	**161.9**	**0.5**	**5.3**	**7.4**	**0.6**	**178.5**
Balances with debt collection agencies	**-**	**39.6**	**-**	**-**	**-**	**-**	**39.6**
(Release)/charge against profits	**(1.3)**	**(0.1)**	**1.3**	**(3.1)**	**(1.5)**	**(0.1)**	**(4.8)**
Amounts written off	**(0.5)**	**(89.9)**	**(0.4)**	**-**	**(3.7)**	**-**	**(94.5)**
Unwind of discount allowance	**-**	**(4.2)**	**-**	**-**	**(0.1)**	**-**	**(4.3)**
At the end of the year	**1.0**	**107.3**	**1.4**	**2.2**	**2.1**	**0.5**	**114.5**

(1) 'Other' relates to Unity Trust Bank.

A review of the Bank's relationships with debt collection agencies in 2014 concluded that the Bank had substantially retained all of the risks and rewards associated with such relationships. The related gross receivables of £41.4m and associated allowance of £39.6m have therefore been recognised as at 31 December 2014. The comparative information has not been adjusted on the grounds of materiality. Had the comparative information been adjusted, the net loans and advances to customers balance and total equity would have increased by £1.8m and £1.8m respectively.

Non-core provisions are analysed in further detail below:

	Non-core				
	Corporate		Optimum		Total
	Individual	Collective	Individual	Collective	Non-core
2014					
At the beginning of the year	**698.4**	**40.0**	**26.1**	**9.4**	**773.9**
(Release)/charge against profits	**(129.0)**	**(23.3)**	**(18.3)**	**3.0**	**(167.6)**
Amounts written off	**(176.1)**	**-**	**1.7**	**-**	**(174.4)**
Unwind of discount allowance	**(6.6)**	**-**	**-**	**-**	**(6.6)**
Interest charged on impaired loans	**0.1**	**-**	**-**	**-**	**0.1**

At the end of the year	**386.8**	**16.7**	**9.5**	**12.4**	**425.4**

	Core		Non-core		
	Individual	Collective	Individual	Collective	Total
2013 restated					
At the beginning of the year	9.4	175.2	434.8	23.6	643.0
Charge against profits for the year	2.4	38.0	441.3	25.8	507.5
Amounts written off	(0.9)	(41.8)	(145.1)	-	(187.8)
Unwind of discount allowance	(0.2)	(3.6)	(6.9)	-	(10.7)
Interest charged on impaired loans	-	-	0.4	-	0.4
At the end of the year	10.7	167.8	724.5	49.4	952.4

	2013
Net impairment charge shown in income statement	516.2
Amounts recovered against amounts previously written off	1.1
Provision against fair value adjustment for hedged risk	(9.8)
Charge against profits shown above	507.5

Core provisions are analysed in further detail below:

	Core						
	Retail		BaCB		Other (1)		Total
	Individual	Collective	Individual	Collective	Individual	Collective	Core
2013							
At the beginning of the year	2.7	173.3	0.3	1.1	6.4	0.8	184.6
Charge/(release) against profits for the year	0.6	32.9	0.6	5.3	1.2	(0.2)	40.4
Amounts written off	(0.5)	(40.7)	(0.4)	(1.1)	-	-	(42.7)
Unwind of discount allowance	-	(3.6)	-	-	(0.2)	-	(3.8)
At the end of the year	2.8	161.9	0.5	5.3	7.4	0.6	178.5

(1) ‘Other’ relates to Unity Trust Bank.

The overall write back of impairment is largely due to improved credit conditions and the strategic disposal of Non-core assets at favourable prices.

Non-core provisions are analysed in further detail below:

	Non-core				
	Corporate		Optimum		Total
2013	Individual	Collective	Individual	Collective	Non-core
At the beginning of the year	426.9	20.5	7.9	3.1	458.4
Charge against profits for the year	417.8	19.5	23.5	6.3	467.1
Amounts written off	(139.8)	-	(5.3)	-	(145.1)
Unwind of discount allowance	(6.9)	-	-	-	(6.9)
Interest charged on impaired loans	0.4	-	-	-	0.4
At the end of the year	698.4	40.0	26.1	9.4	773.9

Loans and advances to customers include finance lease receivables:

	2014	2013
Gross investment in finance leases may be analysed as follows:		
No later than one year	**14.3**	18.4
Later than one year and no later than five years	**47.8**	55.4
Later than five years	**51.0**	53.6
	113.1	127.4
Unearned future finance income on finance leases	**(30.4)**	(32.7)
Net investment in finance leases	**82.7**	94.7
The net investment in finance leases may be analysed as follows:		
No later than one year	**9.0**	12.8
Later than one year and no later than five years	**33.1**	39.2
Later than five years	**40.6**	42.7
	82.7	94.7

There are no unguaranteed residual values for any of the finance leases.

The Bank enters into finance lease and hire purchase arrangements with customers in a wide range of sectors including transport, retail and utilities. The accumulated allowance for uncollectible minimum lease payments receivable is £nil (2013: £0.6m).

18. b) Fair value adjustments for hedged risk

The Bank has entered into interest rate swaps that protect it from changes in interest rates on the floating rate liabilities that fund its portfolio of fixed rate mortgages. Changes in the fair values of these swaps are offset by changes in the fair values of the fixed rate mortgages.

	2014	Restated 2013
Gross fair value adjustments for hedged risk	**196.8**	153.1
Less: impairment provision	**(48.3)**	(46.8)
	148.5	106.3

The comparatives have been restated as described in note 3.

Movements on impairment provision on fair value adjustments for hedged risk are shown below:

	2014	2013
At the beginning of the year	**46.8**	37.0
Charge against profits	**1.5**	9.8
At the end of the year	**48.3**	46.8

19. Investment securities

a) Loans and receivables

	2014	2013
Loans and receivables:		
Listed	**18.1**	23.6
Unlisted	**-**	-
	18.1	23.6
Less: allowance for losses	**-**	-
	18.1	23.6

The movement in investment securities – loans and receivables excluding interest amounts, is summarised as follows:

	2014	2013

At the beginning of the year	**23.6**	294.7
Disposals and maturities	**(6.9)**	(283.4)
Exchange adjustments	**(0.5)**	0.9
Fair value movements through income or expense	**-**	(9.2)
Amortisation	**-**	20.6
At the end of the year	**16.2**	23.6

b) Available for sale

	2014	2013
Available for sale:		
Listed	**3,022.4**	2,497.2
Unlisted	**145.1**	255.2
	3,167.5	2,752.4
Less: allowance for losses	**-**	(20.0)
	3,167.5	2,732.4
Included in cash and cash equivalents	**115.0**	105.0

The movement in investment securities – available for sale excluding interest amounts, is summarised as follows:

	2014	2013
At the beginning of the year	**2,716.5**	3,775.5
Acquisitions	**1,940.1**	2,346.0
Disposals and maturities	**(1,670.0)**	(3,271.3)
Exchange adjustments	**-**	(0.9)
Fair value movements through equity	**71.1**	(32.7)
Fair value movements through income or expense	**82.7**	(105.0)
Amortisation	**(8.9)**	(13.6)
Release and utilisation of impairment provision	**20.0**	18.5
At the end of the year	**3,151.5**	2,716.5

Impairment analysis of investment securities – available for sale

	2014	2013
At the beginning of the year	**20.0**	39.0
Release for the year	**(1.1)**	-
Utilised during the year	**(18.9)**	(18.5)
Exchange adjustments	**-**	(0.5)
At the end of the year	**-**	20.0

A number of securities that had previously been fully provided for were sold during the year. Cash proceeds of £1.1m were received, resulting in a £1.1m release of the provision and utilisation of the remaining £18.9m.

c) Fair value through profit or loss

	2014	2013
Fair value through profit or loss:		
Listed	**1,236.9**	1,743.4
Unlisted	**-**	-
	1,236.9	1,743.4
Less: allowance for losses	**-**	-
	1,236.9	1,743.4

The movement in investment securities – fair value through profit or loss excluding interest amounts, is summarised as follows:

	2014	2013
At the beginning of the year	**1,730.9**	1,830.6
Reclassified to fair value through profit or loss	**-**	447.7
Acquisitions	**338.9**	2,120.9
Disposals and maturities	**(893.1)**	(2,632.9)
Exchange adjustments	**-**	(0.1)
Fair value movements through profit or loss	**53.4**	(35.3)
At the end of the year	**1,230.1**	1,730.9

d) Held for trading

As at December 2014, no held for trading investment securities were held (2013: £nil).

The movement in investment securities – held for trading excluding interest amounts, may be summarised as follows:

	2014	2013
At the beginning of the year	**-**	954.3
Reclassified to fair value through profit or loss	**-**	(447.7)
Acquisitions	**-**	30.7
Disposals and maturities	**-**	(530.9)
Exchange movements	**-**	0.7
Fair value movements through profit or loss	**-**	(7.1)
At the end of the year	**-**	-

e) Analysis of investment securities by issuer

	2014	2013
Investment securities issued by public bodies:		
Government securities	**3,210.3**	3,064.3
Other public sector securities	**339.7**	580.5
	3,550.0	3,644.8
Investment securities issued by other issuers:		
Bank and building society certificates of deposits	**145.1**	235.2
Other debt securities:		
Other floating rate notes	**709.3**	595.8
Mortgage backed securities	**18.1**	23.6
	727.4	619.4
	4,422.5	4,499.4

Other floating-rate notes (FRNs) relate to sterling denominated FRNs with maturities ranging from one month to six years from the balance sheet date.

20. Derivative financial instruments

The Bank has entered, as principal, into various derivatives either as a trading activity, which includes proprietary transactions and customer facilitation, or as a hedging activity for the management of interest rate risk, equity risk and foreign exchange rate risk. Positive and negative fair values have not been netted off as the Bank does not have a legal right of offset.

Derivatives held for trading purposes

The trading transactions are wholly interest rate related contracts including swaps, caps and floors, forward rate agreements and exchange traded futures. Trading transactions include derivatives where the Bank enters into a transaction to accommodate a customer together with the corresponding hedge transaction. The Bank no longer holds derivatives for trading purposes.

Non-trading derivatives

Non-trading transactions comprise derivatives held for hedging purposes to manage the asset and liability positions of the Bank. Derivatives used to manage interest rate related positions include swaps, caps and floors, forward rate agreements and exchange traded futures. The foreign exchange rate positions are managed using forward currency transactions and swaps. Equity risk is managed using equity swaps.

During the year the Bank has entered into fair value hedges to mitigate price movements due to interest rate sensitivities.

	2014		Restated 2013	
	Fair value		Fair value	
	Assets	**Liabilities**	Assets	Liabilities
Derivatives held for non-trading purposes				
Derivatives designated as cash flow hedges:				
Interest rate swaps	**46.1**	**(16.7)**	37.9	(56.0)
Derivatives designated as fair value hedges:				
Interest rate swaps	**0.6**	**(341.2)**	52.5	(289.4)
Cross currency interest rate swaps	**173.4**	**(17.8)**	213.4	(24.6)
Derivatives held for non-trading purposes for which hedge accounting has not been applied:				
Interest rate swaps	**198.2**	**(174.2)**	144.5	(165.0)
Forward currency transactions	**0.6**	**(0.6)**	3.2	(1.4)
OTC interest rate options	**0.9**	**(0.1)**	0.6	(2.2)
OTC equity options	**-**	**-**	0.3	-
Equity swaps	**50.9**	**(1.1)**	103.4	-
Total derivative assets/(liabilities) held for non-trading purposes	**470.7**	**(551.7)**	555.8	(538.6)
Total recognised derivative assets/(liabilities)	**470.7**	**(551.7)**	555.8	(538.6)

2013 numbers have been restated. Refer to note 3 for further information.

The derivatives designated as cash flow hedges are interest rate swaps and futures used to hedge interest rate risk in the Bank's retail operations. Cash flows are hedged by quarterly time periods for durations up to 10 years. During the year there were no forecast transactions for which hedge accounting had previously been used but are no longer expected to occur.

In line with industry standards, credit valuation adjustments (CVAs) and debit valuation adjustments (DVAs) are applied to non-collateralised swaps representing the fair value measurement of counterparty risk. The net credit adjustment across the portfolio at the end of 2014 was £3.9m (2013: £4.4m). CVAs and DVAs are not applied to derivatives that are fully cash collateralised.

27. Deposits by banks

	2014	2013
Items in course of collection	**37.9**	40.9
Deposits from other banks	**577.5**	2,716.6
	615.4	2,757.5

Included within deposits from other banks are liabilities of £nil (2013: £1,028.3m) secured on investment securities with a carrying value of £nil (2013: £1,004.4m) which have been sold under sale and repurchase agreements (note 40).

28. Customer accounts – capital bonds

	2014	2013
Retail	**263.8**	538.1

The capital bonds are fixed term customer accounts with returns based on the movement in an index (eg FTSE 100) over the term of the bond. They have been designated on initial recognition at fair value through profit or loss and are carried at fair value.

The fair values for the capital bonds are obtained on a monthly basis from the swap counterparties. These external valuations are reviewed independently using valuation software to ensure the fair values are priced on a consistent basis.

The maximum amount the Bank would contractually be required to pay at maturity for all the capital bonds is £264.3m (2013: £539.2m).

The Bank uses swaps to create economic hedges against all of its capital bonds. The gain on capital bonds in the income statement for the year is £37.8m (2013: £21.3m). However, taking into account changes in fair value of the associated swaps, the net impact to the income statement for the year is a loss of £1.5m (2013: gain of £0.9m).

29. Debt securities in issue

	2014	Restated 2013
Certificates of deposit	**-**	5.1
Fixed and floating rate notes	**3,443.6**	4,202.5
	3,443.6	4,207.6

The Bank has entered into cross currency interest rate swaps that protect it from changes in exchange rates and interest rates on its debt securities in issue. Changes in the fair values of these swaps are largely offset by changes in the sterling equivalent carrying value of the debt securities in issue.

Debt securities in issue include fixed and floating rate notes, the majority of which are secured on portfolios of variable and fixed rate mortgages. Certain of these notes (securitisations) are redeemable in part from time to time, such redemptions being limited to the net capital received from mortgagors in respect of the underlying assets. There is no obligation for the Bank to make good any shortfall out of general funds. Other notes (covered bonds secured, certificates of deposit and euro medium term notes - unsecured) require the Bank to repay contractual amounts due on specified maturity dates.

Debt securities in issue has been restated as described in note 3.

33. Provisions for liabilities and charges

2014	**Note**	**Property**	**FSCS levies**	**PPI**	**Conduct/ legal**	**Separation**	**Other**	**Total**
At the beginning of the year (as restated)		**23.1**	**13.3**	**133.8**	**304.6**	**39.4**	**35.5**	**549.7**
Provided/(released) in the year:								
Interest income		**-**	**-**	**-**	**48.0**	**-**	**-**	**48.0**
Operating expense	11	**2.1**	**24.4**	**-**	**4.4**	**94.5**	**(1.3)**	**124.1**
Provision for customer redress		**-**	**-**	**5.0**	**43.8**	**-**	**3.5**	**52.3**
Utilised during the year		**(0.5)**	**(25.0)**	**(65.2)**	**(38.3)**	**(21.6)**	**(21.5)**	**(172.1)**
Transfer to liabilities associated with non-current assets held for sale		**(0.3)**	**-**	**-**	**-**	**-**	**-**	**(0.3)**
Increase in discount on loans identified for disposal		**-**	**-**	**-**	**-**	**-**	**15.8**	**15.8**
At the end of the year		**24.4**	**12.7**	**73.6**	**362.5**	**112.3**	**32.0**	**617.5**
Provisions were analysed as follows:								
Amounts falling due within one year		**12.6**	**12.7**	**60.0**	**349.9**	**89.5**	**31.6**	**556.3**
Amounts falling due after one year		**11.8**	**-**	**13.6**	**12.6**	**22.8**	**0.4**	**61.2**

		24.4	**12.7**	**73.6**	**362.5**	**112.3**	**32.0**	**617.5**

2013	Note	Property	FSCS levies	PPI	Conduct/ legal	Separation	Other	Total
At the beginning of the year (as restated)		7.3	13.8	116.0	0.2	-	0.6	137.9
Provided/(released) in the year:								
Interest income		-	-	-	104.5	-	-	104.5
Operating expense (as restated)	11	16.3	24.1	-	-	39.4	35.0	114.8
Provision for customer redress		-	-	103.0	204.0	-	-	307.0
Utilised during the year		(0.5)	(24.6)	(85.2)	(4.1)	-	(0.1)	(114.5)
At the end of the year (as restated)		23.1	13.3	133.8	304.6	39.4	35.5	549.7
Provisions were analysed as follows:								
Amounts falling due within one year		10.2	13.3	113.8	304.6	39.4	35.5	516.8
Amounts falling due after one year		12.9	-	20.0	-	-	-	32.9
		23.1	13.3	133.8	304.6	39.4	35.5	549.7

The Directors consider conduct and legal provisions a critical accounting judgement. Further details are provided in note 2.

The 2013 comparatives for FSCS levies have been restated as described in note 3.

Property

The Bank has a number of leasehold properties available for rent. Provisions are made when either the sub-lease income does not cover the rental expense or the property is vacant. The provision is based on the expected outflows during the remaining periods of the leases. In addition, dilapidation provisions are recorded to the extent that the Bank has incurred dilapidations and/or the dilapidation clause within the contract has been invoked. During the year £2.7m (2013: £11.5m) has been provided for this.

Financial Services Compensation Scheme (FSCS) levies

In common with other regulated UK deposit takers, the Bank pays levies to the FSCS to enable the FSCS to meet claims against it. During 2008 and 2009 claims were triggered against the FSCS in relation to a number of financial institutions. The compensation paid out to consumers is currently funded through loans from HM Treasury. The Bank will be liable to pay a proportion of the outstanding borrowings that the FSCS has borrowed from HM Treasury. Additionally, the Bank is obliged to pay its share of management expenses and compensation based upon the Bank’s proportion of the total market protected deposits at 31 December of each year.

The term of these loans was interest only for the first three years, with the FSCS recovering the interest cost, together with its own ongoing management expenses, through annual management levies on its members. The initial three year term expired in September 2011, and under the renegotiated terms the interest rate was reset from 12 month LIBOR +30bps to 12 month LIBOR +100bps.

By virtue of it holding deposits protected under the FSCS scheme, the Bank has an obligation to pay levies in respect of the interest cost for 2014/15. From 2013, the FSCS had also started to repay the principal of the Treasury loans and a further levy has been raised in 2013/14 and 2014/15 for the expected capital shortfall for these loans, so that they are fully repaid by March 2016. The total levy to be raised is £1,019.0m over three years, with the first instalment of £363.0m collected in 2013 and the second instalment of £399.0m collected in 2014. The Bank has provided £12.7m as at 31 December 2014 (2013 restated: £13.3m) for its share of the levies raised by the FSCS. The Bank's interest levy provision calculation includes estimates of the total FSCS levy in each levy year and estimates of the Bank's market participation in each levy year. The Bank has also paid £14.2m and £10.8m in respect of its 2013/14 interest levy and share of the capital levy respectively in 2014.

Payment Protection Insurance (PPI)

Provisions have been made in respect of potential customer compensation claims relating to past sales of PPI. Claims are investigated on an individual basis and, where appropriate, compensation payments are made. For a number of years, the Bank, along with many other financial services providers, sold PPI alongside mortgage and non-mortgage credit products. The Bank stopped selling non-mortgage PPI in January 2009 and stopped selling mortgage PPI in March 2012.

The FSA issued a policy statement in August 2010, which amended the 'Disputes Resolution: Complaints' section of the FSA Handbook, setting out new rules for handling complaints, including complaints of PPI mis-selling. The Bank must comply with the policy statement which requires complainants to receive adequate redress and the Bank to deliver fair outcomes and treat customers fairly including non-complainants. An additional provision of £5.0m (2013: £103.0m) has been recognised in the year, in respect of the total expected cost to the Bank of carrying out this work and paying compensation, making total provisions raised of £352.0m (2013: £347.0m). This is discussed in more detail in note 2.

Refer to the Income Statement on Page 148 for details relating to the change in presentation of provision amounts in relation to net interest income, net fee and commission income and operating expenses.

Conduct/legal provisions

During the year the Bank provided an additional £48.0m (2013: £104.5m) in respect of customer redress due to breaches of the technical requirements of the Consumer Credit Act.

The £43.8m (2013: £204.0m) charged through potential customer redress consists of £37.0m in relation to arrears fees and charges and mortgage delivery costs, a £7.3m release in relation to mortgage fees, a £6.0m release in relation to mortgage documentation and a £20.1m increase of other conduct related provisions.

£4.4m has been provided through operating expenses in relation to other conduct and legal related provisions.

Refer to the Income Statement on Page 148 for details relating to the change in presentation of provision amounts in relation to net interest income, net fee and commission income and operating expenses.

Other

The net £93.2m (2013: £74.4m) charged through operating expenses consists of £94.5m in relation to costs associated with the separation of the Bank from The Co-operative Group and a £1.3m release relating to other provisions.

During December 2014 the Bank entered into a Sale and Purchase Agreement to dispose of a portfolio of performing loans and associated hedging derivatives not considered to be core assets to a third party. These assets will be derecognised in 2015 after the completion of the contract. A constructive obligation in respect of the discount on the loans identified for disposal of £15.8m has been recognised in 2014 (2013: £nil).

34. Deferred tax

Deferred taxes are calculated on all temporary differences under the liability method using a tax rate of 20% (2013: 20%).

The movements on the deferred tax accounts are as follows:

		2014			2013	(restated)	
	Note	**Deferred tax asset**	**Deferred tax liability**	**Total**	Deferred tax asset	Deferred tax liability	Total
Deferred tax at the beginning of the year		**25.1**	**(103.0)**	**(77.9)**	162.5	(121.4)	41.1
Credited/(charged) to the income statement:							
Current year		**5.5**	**19.0**	**24.5**	(15.6)	28.9	13.3
Write off of prior year deferred tax asset	13	**-**	**-**	**-**	(137.7)	(10.5)	(148.2)
Prior year		**-**	**-**	**-**	3.3	-	3.3
		5.5	**19.0**	**24.5**	(150.0)	18.4	(131.6)
Credited/(charged) to other comprehensive income:							
Cashflow hedges		**(8.7)**	**-**	**(8.7)**	12.5	-	12.5
Available for sale		**-**	**-**	**-**	0.1	-	0.1
		(8.7)	**-**	**(8.7)**	12.6	-	12.6
Reclassified to assets held for sale		**(0.9)**	**-**	**(0.9)**	-	-	-
Deferred tax at the end of the year		**21.0**	**(84.0)**	**(63.0)**	25.1	(103.0)	(77.9)

The deferred tax asset above includes an offset for those deferred tax liabilities that are permissible to be offset.

	2014		2013 (restated)	
	Deferred tax asset	**Deferred tax liability**	Deferred tax asset	Deferred tax liability
Deferred tax comprises:				

Capital allowances on fixed assets and assets leased to customers	**12.1**	**-**	7.4	-
Fair value adjustments - The Co-operative Bank subsidiaries	**-**	**(76.4)**	-	(92.9)
Other temporary differences	**21.0**	**(7.6)**	25.1	(10.1)
Cashflow hedges	**(11.5)**	**-**	(1.6)	-
Unrealised appreciation on investments	**(0.6)**	**-**	(0.6)	-
FSCS levy provision	**-**	**-**	(5.2)	-
	21.0	**(84.0)**	25.1	(103.0)

Deferred tax has been restated as described in note 3.

Net deferred tax assets expected to be recoverable after one year are £21.0m (2013: £25.1m restated).

Other temporary differences for the Bank totalling £13.4m (2013: £15.0m restated) relate to temporary differences arising on consolidation adjustments where the recoverability is not dependent on the future performance of the Bank, and temporary differences in subsidiaries that are forecast to make future taxable profits.

The deferred tax liability of £76.4m (2013: £92.9m restated) relating to fair value adjustments is net of a deferred tax asset of £3.3m (2013: £9.2m restated).

The Directors consider the recoverability of deferred tax to be a critical accounting judgement as detailed in note 2. Detail on the restatement of comparatives is provided in note 3.

The deferred tax charge/(credit) in the income statement comprises

	2014	2013 (restated)
Capital allowances on fixed assets and assets leased to customers	**(5.1)**	23.9
Fair value adjustments	**(16.5)**	37.1
Other temporary differences	**1.1**	11.1
Cashflow hedges	**1.2**	(1.4)
FSCS levy provision	**(5.2)**	5.2
Tax losses carried forward	**-**	54.8
Pensions and other post-retirement benefits	**-**	0.9
	(24.5)	131.6

Deferred tax assets totalling £297.5m (2013: £256.9m restated) have not been recognised where doubt exists over the availability of sufficient future taxable profits. Deferred tax has not been recognised in respect of trading losses of £1,229.2m (with deferred tax of £245.8m), capital losses of £16.4m (with deferred tax of £3.3m), and other temporary differences of £242.0m (with deferred tax of £48.4m). Deferred tax assets from the prior year of £nil (2013: £148.1m restated) have been written off in the period. Deferred tax assets of £22.7m (2013: £115.9m restated) in respect of the current year have not been recognised.

Reductions in the UK corporation tax rate from 23% to 21% (effective from 1 April 2014) and 20% (effective from 1 April 2015) were substantively enacted on 2 July 2013. This will reduce the Bank's future current tax charge accordingly. Deferred tax as at 31 December 2014 has been calculated based on the rate of 20% substantively enacted at the balance sheet date.

On 3 December 2014 the Chancellor of the Exchequer announced that the UK Government will introduce legislation in the Finance Bill 2015, which will restrict the proportion of banks' annual taxable profit that can be offset by certain carried forward tax losses. The restriction will take effect from 1 April 2015 and will apply to relevant tax losses arising prior to this date.

The Chancellor's announcements had not been enacted or substantively enacted at the balance sheet date and as the Bank has not recognised a deferred tax asset on carried forward tax losses there would be no impact on the tax balances in the financial statements for the year ended 31 December 2014. We will consider the impact of the final legislation once enacted.

35. Pensions

Pension charge

The pension charge in the income statement at 31 December 2014 was £31.0m (2013: £29.3m) which includes £2.1m (2013: £8.0m) as the Bank's contribution to the Pace deficit recovery charge. Of this, £nil (2013: £0.6m) is included in operating costs incurred outside the normal course of business.

The Co-operative Pension Scheme (Pace)

The Bank participates in Pace, a hybrid scheme, consisting of a defined benefit section and a defined contribution section.

At 31 December 2012 the scheme was recognised as a Group plan, since risks were shared between entities under the common control of The Co-operative Group. It was accounted for on a defined contribution basis since there was no contractual agreement or stated Co-operative Group policy for charging the net defined benefit cost for the scheme as a whole to individual participating entities. Therefore, the Bank did not recognise its share of the net defined benefit cost. The net defined benefit cost of the pension scheme was recognised fully by the sponsoring employer, which was The Co-operative Group Limited.

On 4 November 2013, The Co-operative Group and the Bank entered into an undertaking pursuant to which The Co-operative Group agreed with the Bank, subject to certain exceptions, not to require the Bank to cease to participate in Pace in connection with the LME or any subsequent reduction in The Co-operative Group's shareholding in the Bank (including to nil). During 2015, The Co-operative Group and the Bank are expected to conclude discussions to agree on the separation of Pace, so that the scheme liability properly attributable to the Bank and an equivalent proportion of the scheme's assets would be transferred to a separate tax registered pension scheme, or a segregated section of Pace. Separation of Pace will require the agreement of the Pace Trustees.

Following separation of the Bank from the wider Co-operative Group as a result of the LME, the Bank remains a participating employer in the Pace scheme and the Pace scheme is considered to be a multi-employer scheme under IAS 19 Employee benefits (revised 2011).

As a multi-employer pension scheme, Pace exposes the participating businesses to actuarial risks associated with the current and former employees of the other participating employers. The proportion of Pace liabilities accrued by members whilst employees of the Bank is believed to represent a minority of total Pace liabilities. The Bank could, however, be liable for funding a greater proportion of Pace liabilities.

There are for example liabilities in Pace relating to benefits accrued by members whilst employed by CFSMS and working in the Bank's business. On 23 January 2014, following the legal separation of the Bank from the wider Co-operative Group, employment contracts for the majority of those employees who spend most of their time working on behalf of the Bank were transferred from CFSMS to the Bank. This has increased the number of Bank employees participating in the Pace scheme in 2014.

There may also be 'orphan liabilities' in Pace that do not relate to any current employer participating in Pace. The extent to which the Bank could be liable for funding a greater proportion of Pace liabilities will depend, inter alia, on what position is reached as to the Pace liabilities properly attributable to the Bank following discussions with The Co-operative Group and the Pace Trustee. Such discussions are not yet substantively underway.

There is therefore currently insufficient information available to consistently and reliably identify the Bank's share of Pace liabilities and employer costs. For the above reasons the pension costs in respect of Pace are accounted for on a defined contribution basis in accordance with IAS 19 (revised 2011). Pension costs are recognised as an expense in the Bank income statement on a defined contribution basis as explained below, based on a fixed percentage as agreed with the Trustee.

The Pace scheme is not sectionalised and operates on a 'last man standing' basis. In the event that other participating employers become insolvent and the full statutory debt is not recovered on insolvency, the Bank would become liable for the remaining liabilities.

There is no agreed allocation of a deficit or surplus on (i) wind up of the Plan; or (ii) the entity's withdrawal from the Plan.

The key aspects of Pace are illustrated below.

Scheme information

Risks arising in Pace are identified at The Co-operative Group level, with the impact of any changes to contribution assessed under the Bank's risk management framework. The Bank is therefore exposed to potential future increases in required contributions and capital held for pension risk. The Pace Trustee, in consultation with The Co-operative Group, is responsible for the risk management arrangements for Pace agreeing suitable contribution rates, investment strategy and for taking appropriate professional advice as required.

Contribution payments

On an accounting basis the Pace scheme is in a surplus of £1,128.5m at 31 December 2014 (2013: surplus of £355.9m). Under the current arrangements the Bank does not have an unconditional right of refund of scheme assets on winding up or any right to reduction of contributions as a result of this surplus.

Based on advice from a qualified actuary, the contributions in respect of future service in the defined benefit section are currently 18%.

The Pace triennial valuation as at 5 April 2013 was completed on 21 July 2014. The funding shortfall for the entire scheme had increased from £248.0m per the previous triennial valuation as at 5 April 2010 to £600.0m as at 5 April 2013. The latest funding shortfall position calculated by the scheme actuary on an approximate basis as at 31 May 2014 was £104.0m. The level of funding for the Pace scheme is agreed between The Co-operative Group and the Pace Trustee. The Co-operative Group agreed a recovery plan with the Trustee of the scheme to contribute £25m per annum over 5 years from 1 July 2014 to 30 June 2019 (inclusive) to repay the £104.0m deficit calculated on an approximate basis as at 31 May 2014. On 19 August 2014, the Bank agreed to meet 20% of the total Pace deficit contributions at that date for a period of one year only. The Bank recognised £5m on 19 August 2014 as a result of this agreement which represented 12 months of deficit contribution being the time frame which is expected to elapse to the point that the Pace separation process is completed. The liability in respect of the deficit contribution agreement dated 19 August 2014 as at 31 December 2014 was £2.9m (2013: £nil). The current recovery plan ending in 2019 between The Co-operative Group and the Pace scheme Trustees may however be insufficient to repay the latest valuation of the deficit. The Bank's agreement on 19 August 2014 to meet 20% of the total Pace deficit contributions was predicated upon this percentage contribution not setting a precedent for future discussions on the separation of accrued Pace assets and liabilities between The Co-operative Group and the Bank. The Co-operative Group has undertaken to agree with the Bank its final proportion of employer contributions in Pace and, if not agreed, the matter will be referred to an independent third party. Accordingly, there is a wide range of outcomes regarding the duration and contribution requirements of a new schedule of contributions and recovery plan which make the overall contributions uncertain.

The next formal triennial valuation of Pace as at 5 April 2016 will not be completed until 2017, however a funding shortfall position calculated by the scheme actuary on an approximate basis is expected in 2015. There is therefore a risk that in future periods the Bank will recognise significant liabilities in respect of the scheme in its accounts.

The Bank also pays contributions in respect of the employed members of the defined contribution sections of the scheme of either 2% or 8% of pensionable salaries. The key financial aspects of Pace are illustrated below for information. These amounts are not recognised within these financial statements.

Key assumptions of the Pace pension scheme

The key aspects of the Pace scheme are as follows:

	2014	2013
The principal assumptions used to determine the liabilities of the Pace scheme are:		
Discount rate	**3.70%**	4.45%
Rate of increase in salaries	**3.30%**	3.60%
Future pension increases where capped at 5.0% per annum	**3.30%**	3.60%
Future pension increases where capped at 2.5% per annum	**2.50%**	2.50%
Assumptions used to determine net pension cost for the Pace scheme are:		
Discount rate	**4.45%**	4.60%
Rate of increase in salaries	**3.60%**	4.80%

The average life expectancy (in years) for mortality tables used to determine scheme liabilities for the Pace scheme at 31 December 2014 is:

	Male	Female
Life expectancy:		
Member currently aged 65 (current life expectancy)	**22.8**	**24.9**
Member currently aged 45 (life expectancy at age 65)	**25.0**	**27.2**

The balance sheet amounts attributable to the entire scheme are as follows:

	2014	2013
Fair value of plan assets	**9,153.7**	7,486.5
Present value of funded obligations	**(8,024.8)**	(7,125.8)
	1,128.9	360.7
Present value of unfunded obligations	**(0.4)**	(4.8)
	1,128.5	355.9

The asset allocations at the year end were as follows:

	2014	2013
Equities	**1,808.1**	2,398.8
Liability driven investments	**5,228.7**	3,382.6
Alternative growth	**964.8**	994.2
Property	**318.6**	308.6
Other	**833.5**	402.3

The table below shows the fair value of the assets in each category which have a quoted market price:

	2014	2013
Equities	**1,808.1**	2,395.8
Liability driven investments	**4,912.7**	2,654.9
Other	**378.9**	338.2

Britannia Pension Scheme (Britannia Scheme)

The Britannia Scheme is a hybrid scheme, consisting of a defined benefit section and a defined contribution section.

In 2009, following the transfer of engagements of Britannia Building Society, CFSMS, a Co-operative Group subsidiary, became principal employer of the scheme. Three other participating employers of the Britannia Scheme are Bank wholly owned subsidiary entities. The Bank itself is not a participating employer in the scheme, but provides a guarantee to the Britannia Trustee in relation to funding the pension obligations.

The scheme closed on 6 October 2010 with active members at the date of closure being invited to join the Co-operative Pension Scheme (Pace) for future pension accrual. No future service contributions are payable to the scheme due to the closure of the scheme to future accrual. The Trustee agreed to wind up the defined contribution section from February 2013, with any remaining members given the option of transferring their funds to an alternative approved pension arrangement, or secured benefits with an insurance contract. The weighted average duration of the defined benefit obligation of the Britannia Scheme is 23 years.

At 31 December 2012 the scheme was recognised as a Group plan since all participating entities were within common control of The Co-operative Group. The Bank and its subsidiary entities participating in the scheme (Platform, WMS and Britannia International) accounted for the scheme on a defined contribution basis, recognising the contribution paid as an expense in the income statement. Following separation of the Bank from the wider Co-operative Group as a result of the LME in 2013, the scheme was considered to be a multi-employer scheme under IAS 19 (revised 2011). At 31 December 2013 the Bank did not have sufficient information to reliably and consistently measure its share of the obligation and therefore the Bank accounted for the scheme on a defined contribution basis. During 2014, employment contracts for those employees who spent the majority of their time working on behalf of the Bank were transferred from CFSMS to the Bank. As a result of this transfer, whilst CFSMS remains the sponsoring employer of the scheme, the Bank will recognise the total assets and liabilities of the scheme on the balance sheet as at 31 December 2014.

Whilst the Britannia Scheme is in an accounting surplus, this has not been recognised on the balance sheet in accordance with IFRIC 14. The Bank has however recognised a £3.3m liability (2013: unrecognised £3.1m) representing unfunded pension liabilities of the Britannia Supplementary Pension and Life Assurance Plan. There is no charge supplementary arrangement for certain

Executive Directors. Benefits under this unfunded arrangement are valued on the same assumptions as the Britannia Scheme and are disclosed as unfunded obligations.

Nature of benefits

The Britannia Scheme pays out pensions at retirement based on service to 6 October 2012 and final pay for employees who commenced employment prior to 1 September 2001, when it closed to new members.

Funding the liabilities

Britannia Pension Trustees Limited is the corporate body that acts as 'Trustee' of the Britannia Scheme. UK legislation requires the Trustee to carry out valuations at least every three years and to target full funding against a basis that prudently reflects the scheme's risk exposure. The Scheme Actuary completed an actuarial valuation of the Scheme as at 5 April 2011, in accordance with the scheme specific funding requirements of the Pensions Act 2004. The results of the valuation showed that the Britannia Scheme had a shortfall of £3.7m. CFSMS (the sponsoring employer) agreed to pay a lump sum of £3.7m to eliminate this shortfall. The latest funding shortfall position calculated by the scheme actuary as at 5 April 2013 was £61.3m. The statutory deadline for the 5 April 2014 Britannia Scheme triennial valuation is 5 July 2015.

As at 31 December 2014 the Bank has no requirement to pay deficit contributions in respect of the Britannia Scheme.

Governance

The Chair of the Trustee Board is appointed by and from the Trustee Directors and the Board comprises an Independent Trustee, nominees of The Co-operative Group and elected scheme Members. The Trustee, in consultation with CFSMS and the Bank, is responsible for the risk management arrangements for the Britannia Scheme, agreeing suitable contribution rates, investment strategy and for taking professional advice as appropriate.

Risks associated with the scheme

Risks arising in the Britannia Scheme are identified and assessed under the Bank's Risk Management framework. The Bank is exposed to potential future increases in required contributions and capital held for pension risk.

Actions taken by the Pensions Regulator, changes to European legislation, or changes in the financial strength of CFSMS or the Bank could result in stronger funding standards, which could materially affect the Bank's cash flow and balance sheet. There is also a risk that changes in the assumptions for life expectancy, interest rates or in price inflation could result in a deficit in the scheme. Other assumptions used to value the defined benefit obligation are also uncertain, although their effect is less material.

The Bank has also granted a guarantee in respect of participating employers' liabilities in relation to the Britannia Scheme up to 105% funding on the section 179 Pensions Act 2004 valuation basis.

Investment strategy

Some risk arises from the Britannia Scheme defined benefit section because the value of the asset portfolio and returns from it may be less than expected. There is also a risk of a mismatch between the Scheme's assets and liabilities and differences in sensitivity to changes in financial and demographic factors. The Trustee's objective is to invest the Scheme's assets in the best interest of the Members and beneficiaries. Within this framework the Trustee has agreed a number of objectives to help guide them in their strategic management of the assets and control of the various risks to which the Britannia Scheme is exposed.

Indirect participation

In 2014 the Bank paid approximately £1m (2013: £1m) to CFSMS in relation to Britannia Scheme pension costs. The pension cost shown in these accounts is the actual contribution paid by the Bank and three of its subsidiaries.

As explained above, on 23 January 2014, following the legal separation of the Bank from the wider Co-operative Group, employment contracts for the majority of those employees who spend most of their time working on behalf of the Bank were transferred from CFSMS to the Bank.

Critical accounting estimates and judgements – sensitivity of defined benefit obligations

The measurement of the Bank's defined benefit liability is particularly sensitive to changes in certain key assumptions, which are described below. The methods used to carry out the sensitivity analyses presented below for the material assumptions are the same as those the Bank has used previously. The calculations alter the relevant assumption by the amount specified, whilst assuming that all other variables remained the same. This approach is not necessarily realistic, since some assumptions are related; for example, if the scenario is to show the effect if inflation is higher than expected, it might be reasonable to expect that nominal yields on corporate bonds will increase also. However, it enables the reader to isolate one effect from another.

Discount rate	This has been selected following actuarial advice received by the Bank, taking into account the duration of the liabilities. An increase or decrease in the discount rate of 0.1% would result in a £15.7m decrease or a £15.7m increase, respectively, in the present value of the defined benefit obligation.
Inflation	Inflation is a significant assumption as it is used to determine salary-related benefits and pension increases before and after retirement. The assumption adopted is consistent with the discount rate adopted. An increase or decrease in the inflation rate of 0.1% would result in a £15.8m increase or a £15.8m decrease, respectively, in the present value of the defined benefit obligation.
Mortality rates	The mortality assumptions adopted are based on those recommended by the actuaries that advise the scheme management and reflect the most recent information as appropriate. An increase in the assumed long term rate of improvement in mortality from 1.5% per annum to 1.75% per annum would increase the present value of the defined benefit obligation by £12.2m.

The key aspects of the defined benefit section of the Britannia Scheme are disclosed in the following tables. The Britannia Scheme was not recognised as at 31 December 2013 (as explained above), however comparative information has been provided for illustrative purposes.

	2014	2013
The principal assumptions used to determine the liabilities of the Britannia defined benefit scheme are:		
Discount rate	**3.70%**	4.45%
Rate of increase in salaries	**3.20%**	3.60%
Future pension increases where capped at 5.0% per annum	**3.15%**	3.60%
Future pension increases where capped at 2.5% per annum	**2.20%**	2.50%
Assumptions used to determine net pension cost for the Britannia defined benefit scheme are:		
Discount rate	**4.45%**	4.60%

Rate of increase in salaries	**3.60%**	4.80%

The average life expectancy (in years) for mortality tables used to determine defined benefit scheme liabilities for the former Britannia Building Society Scheme as at 31 December 2014 is:

	Male	Female
Life expectancy:		
Member currently aged 65 (current life expectancy)	**22.9**	**25.1**
Member currently aged 45 (life expectancy at age 65)	**25.2**	**27.5**

The amounts recognised in the balance sheet of the Bank are as follows:

	2014	2013
Fair value of plan assets	**728.5**	630.7
Present value of funded obligations	**(683.7)**	(604.2)
	44.8	26.5
Pension surplus not recognised under IAS 19 (revised 2011)	**(44.8)**	(26.5)
Present value of unfunded obligations	**(3.3)**	(3.1)
	(3.3)	(3.1)

The amounts recognised in the income statement of the Bank are as follows:

	2014	2013
Interest expense on defined benefit obligation	**(26.5)**	(26.6)
Interest income on plan assets	**27.7**	27.4
Interest expense on effect of onerous liability	**(1.2)**	(0.7)
Total net interest cost	**-**	0.1
Administrative expenses	**(1.5)**	(1.1)
Defined benefit cost included in income statement	**(1.5)**	(1.0)

Changes in the present value of the defined benefit obligation are as follows:

	2014	2013
Defined benefit obligation at the start of the year	**604.2**	586.8
Interest expense	**26.5**	26.6
Benefit payments from plan assets	**(15.8)**	(16.2)
Remeasurements:		

Effect of changes in demographic assumptions	**12.0**	-
Effect of changes in financial assumptions	**56.8**	7.0
Defined benefit obligation at the end of the year	**683.7**	604.2

Changes in the fair value of the plan assets are as follows:

	2014	2013
Fair value of plan assets at the start of the year	**630.7**	602.7
Interest income	**27.7**	27.4
Benefit payments from plan assets	**(15.8)**	(16.2)
Administrative expenses paid from plan assets	**(1.5)**	(1.1)
Return on plan assets (excluding interest income)	**87.4**	17.9
Fair value of plan assets at the end of the year	**728.5**	630.7

Changes in the effect of the asset ceiling are as follows:

		2014			2013	
	Asset	**Defined benefit obligation**	**Asset ceiling**	Asset	Defined benefit obligation	Asset ceiling
At the start of the year	**630.7**	**(604.2)**	**(26.5)**	602.7	(586.8)	(15.9)
Interest income/(expense)	**27.7**	**(26.5)**	**(1.2)**	27.4	(26.6)	(0.8)
Administrative expenses paid from plan assets	**(1.5)**	**-**	**1.5**	(1.1)	-	1.1
Benefits paid	**(15.8)**	**15.8**	**-**	(16.2)	16.2	-
Actuarial gains/(losses)	**87.4**	**(68.8)**	**(18.6)**	17.9	(7.0)	(10.9)
Fair value of plan assets at the end of the year	**728.5**	**(683.7)**	**(44.8)**	630.7	(604.2)	(26.5)

The asset allocations at the year end were as follows:

	2014	2013
Equities	**118.5**	153.4
Liability driven investments	**463.0**	286.4
Alternative growth	**49.1**	100.6
Property	**87.3**	89.6

Other	**10.6**	0.7

The table below shows the fair value of the assets in each category which have a quoted market price:

	2014	2013
Equities	**118.5**	153.4
Liability driven investments	**425.7**	286.4
Other	**9.3**	0.1

Bank (unfunded) pension scheme

The Bank also operates a small unfunded pension scheme.

	2014	2013	2012	2011	2010
Rate of increase of pensions in payment	**3.3%**	3.6%	3.3%	3.3%	3.7%
Rate of increase in salaries	**3.3%**	5.1%	4.8%	4.8%	5.2%
Discount rate	**3.7%**	4.7%	4.6%	4.6%	5.2%

The assumptions used by the actuary were the best estimates chosen from a range of possible actuarial assumptions which, due to the timescales covered, may not necessarily be borne out in practice.

The values of the assets and liabilities of the unfunded pension scheme were:

	2014	2013
Present value of unfunded obligations	**(4.7)**	(4.0)
Deficit in scheme	**(4.7)**	(4.0)
Related deferred tax asset	**0.9**	0.9
Net pension liability	**(3.8)**	(3.1)
Analysis of amount charged to income statement:		
Current service cost	**-**	-
Interest on pension scheme liabilities	**0.2**	0.2
	0.2	0.2

Changes in the present value of the scheme liabilities are as follows:

	2014	2013
Opening defined benefit liabilities	**4.0**	4.0

Current service cost	**-**	-
Interest on liabilities	**0.2**	0.2
Actuarial losses	**0.7**	-
Benefits paid	**(0.2)**	(0.2)
Closing defined benefit liabilities	**4.7**	4.0

Amounts recognised in the statement of comprehensive income:

	2014	2013
Actuarial losses on scheme liabilities during the period	**0.7**	-
Total scheme losses during the period	**0.7**	-

The amounts for the current year are as follows:

	2014	2013
Defined benefit obligation	**(4.7)**	(4.0)
Deficit in scheme	**(4.7)**	(4.0)
Experience adjustment on scheme liabilities	**-**	-
Experience adjustment on scheme assets	**-**	-

36. Contingent liabilities

The tables below provide the contract amounts and risk weighted amounts of contingent liabilities and commitments. The contract amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. The risk weighted amounts have been calculated in accordance with the PRA rules.

The contingent liabilities, as detailed below, arise in the normal course of banking business and it is not practical to quantify their future financial effect.

		Unaudited		Unaudited
	Contract amount 2014	Risk weighted amount 2014	Contract amount 2013	Risk weighted amount 2013
Contingent liabilities:				
Guarantees and irrevocable letters of credit	43.2	18.0	86.4	45.4

Other commitments:				
Documentary credits and short term trade related transactions	-	-	0.8	0.2
Forward asset purchases and forward deposits placed (1)	154.9	77.8	570.1	152.1
Undrawn formal standby facilities, credit lines and other commitments to lend (includes revocable and irrevocable commitments) (2)	2,862.9	448.5	3,432.8	684.3
	3,061.0	544.3	4,090.1	882.0

(1) Forward asset purchases have significantly reduced during the year due to repos maturing and there being lower funding requirements.

(2) Undrawn loan commitments include revocable commitments which are unused credit card limits of £1,787.3m (2013: £1,968.1m).

Assets pledged

Assets are pledged as collateral under repurchase agreements with other banks. These deposits are not available to finance the Bank's day-to-day operations. Mandatory reserve deposits are also held with the Bank of England in accordance with statutory requirement.

See note 40.d for further details of assets pledged.

Commitments under operating leases

The Bank leases various properties and equipment under non-cancellable operating lease arrangements. The leases have various terms, ranging from six months to 999 years. None of these leases are individually material and none have any material clauses. The Co-operative Bank plc remains in negotiations to enter into leases for the CIS Building in Manchester and these are expected to be finalised in 2015. The table below discloses the minimum operating lease payments the Bank will be required to make over the remaining lives of the leases.

	Land and buildings 2014	Equipment 2014	Land and buildings 2013	Equipment 2013
Falling due:				
Within one year	18.3	0.1	18.7	-
Between one and five years	46.3	0.3	50.7	0.4
In five years or more	51.5	-	70.0	-
	116.1	0.4	139.4	0.4

The Bank leases a number of branch and office premises under operating leases. The leases typically run for a period of up to 25 years, with an option to renew the lease after that period. Lease payments are generally reviewed every three to five years to reflect market rentals.

The total value of future minimum sub-lease payments expected to be received under non-cancellable sub-leases for the Bank was £5.0m (2013: £8.0m).

Indemnification agreement

The Bank has an indemnification agreement with CFSMS, accounted for as a guarantee under IFRS 4, in which the Bank has agreed to indemnify CFSMS against all and any liability, loss, damage, costs and expense arising from the agreement (under which CFSMS provides certain assets and services to the Bank). This agreement will remain in place until it is terminated after separation activities with the wider Co-operative Group are fully completed, but this will require the consent of CFSMS.

Conduct issues

Given the high level of scrutiny regarding financial institutions' treatment of customers and business conduct from regulatory bodies, the media and politicians, there is a risk that certain aspects of the Bank's current or historic business, including, amongst other things, mortgages and relationship banking, may be determined by the FCA and other regulatory bodies or the courts as, in their opinion, not being conducted in accordance with applicable laws or regulations, or fair and reasonable treatment.

In particular, there is currently a significant regulatory focus on the sale practices and reward structures that financial institutions have used when selling financial products. There is a risk that there may be other regulatory investigations and action against the Bank in relation to conduct and other issues that the Bank is not presently aware of, including investigations and actions against it resulting from alleged mis-selling of financial products or the ongoing servicing of those financial products. The nature of any future disputes and legal, regulatory or other investigations or proceedings into such matters cannot be predicted in advance. Furthermore, the outcome of any on-going disputes and legal, regulatory or other investigations or proceedings is difficult to predict.

Consumer Credit Act issues

The Consumer Credit Act regulates consumer lending and governs the way in which entities, including banks, providing consumer credit to retail customers carry out business. From 1 April 2014 the Financial Services and Markets Act 2000 also applies alongside certain retained provisions of the Consumer Credit Act. The Consumer Credit Act includes very detailed, prescriptive and highly technical requirements for lenders affecting customer documentation and which, in turn, impact how operational processes and IT systems are configured. While the Bank has undertaken a detailed analysis to identify certain instances where its documentation or processes have not been fully compliant with the technical requirements and has provided accordingly, it is not possible to rule out the possibility of other instances which have not yet been identified. Breaches may have the effect of triggering periods of non-compliance during which an affected customer is not liable to pay interest.

Debit interest refunds would therefore need to be made in certain cases where a period of non-compliance has been previously triggered, in the same way the Bank will be making such refunds as a consequence of the issues already identified (and provided for).

During the year the Bank provided £69.0m (2013: £109.5m) for identified issues. As part of the process of identification, detailed and technical legal analysis has been carried out as to whether breaches of the technical requirements have in fact occurred. Such legal analysis by its nature involves judgement and assessment of the facts of particular circumstances. In the event that such legal analysis and judgements are determined to be wrong, the Bank could be exposed to a material additional liability. The amount of £174.5m which has been provided is the best estimate of the liability based on the legal analysis.

Regulatory and other investigations

The Bank is the subject of multiple regulatory and other investigations and enquiries into events at the Bank and circumstances surrounding them. These include:

- The Treasury announced by press release on 22 November 2013 that it intends to conduct an independent investigation into events at the Bank and the circumstances surrounding them from 2008, including the Verde transaction and Britannia merger. The investigation will review the conduct of Regulators and the Government but is not anticipated to commence until it is clear that it will not prejudice the outcome of the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA) enforcement investigations.

- The PRA is undertaking an enforcement investigation in relation to the Bank and as part of that investigation will consider the role of former senior managers.
- The FCA is undertaking enforcement investigations into events and decisions at the Bank up to June 2013.
- The Financial Reporting Council has launched an investigation under its Accountancy Scheme into the preparation, approval and audit of the Bank's accounts up to and including its 2012 annual accounts.

The Bank is co-operating with the investigating authorities. It is not possible to estimate the financial impact upon the Bank should any adverse findings be made.

Legal proceedings

The Bank is engaged in various other legal proceedings in the UK involving claims by and against it which arise in the ordinary course of business, including debt collection, mortgage enforcement, consumer claims and contractual disputes. The Bank does not expect the ultimate resolution of any of these proceedings to which the Bank is party to have a material adverse effect on its results of operations, cash flows or the financial position of the Bank and has not disclosed the contingent liabilities associated with these claims. Provisions have been recognised for those cases where the Bank is able reliably to estimate the probable loss where the probable loss is not de minimis. See note 33.

Mortgage securitisation representations and warranties

In connection with the Bank's mortgage securitisations and covered bond transactions described in note 29 (Bank financial statements) and note 23 (Company financial statements), the Bank makes various representations and warranties relating to the mortgage loans, including in relation to ownership, compliance with legislation and origination procedures. If the representations and warranties are breached subject to any applicable materiality determination, the Bank may be required to repurchase the affected mortgage loans or in some circumstances pay compensation to the securitisation vehicle.

There is a risk that a number of the underlying matters giving rise to the conduct and legal provisions set out in note 33 could have given rise to breaches of such representations and warranties. Accordingly there is a risk that the Bank may be required to pay compensation or repurchase affected mortgage loans in amounts that may reduce the Bank's liquidity.

The Bank is unable to estimate the extent to which, the matters described above will impact it or how future developments may have a material adverse impact on the Bank's net assets, operating results or cash flows in any particular period.

Pensions

There is uncertainty over the amount that the Bank will have to pay while it continues to participate in Pace. The Bank's obligations to contribute to Pace would increase significantly if another large employer in Pace becomes insolvent while the Bank continues to participate. If the Bank seeks to address these risks by terminating its participation, the default position is that material liabilities in respect of the deficit in Pace will arise. The Co-operative Group and the Bank have entered good faith discussions to manage this by reaching agreement so that the liabilities properly attributable to the Bank (and an equivalent proportion of assets) would be transferred to a separate scheme, or a segregated section of Pace, on the Bank's exit but, no arrangements have yet been agreed. There is therefore uncertainty over the amount that the Bank will have to pay in the event that it exits Pace. Separation of Pace will also require the co-operation of the Pace Trustees which may not be forthcoming.

The Pace scheme is not sectionalised and operates on a 'last man standing' basis. In the event that other participating employers become insolvent and the full statutory debt is not recovered on insolvency, the Bank would become liable for the remaining liabilities.

Other pensions risks and uncertainties include the risk to the Bank's capital and funds from the Bank's exposure to scheme liabilities (to the extent liabilities are not met by scheme assets), risks inherent in the valuation of scheme liabilities and assets, risks regarding the split of liabilities between the Bank and other participating employers while the Bank continues to participate in Pace and on exit from Pace and, in respect of the Britannia Scheme, risks on separation from The Co-operative Group.

In respect of the Britannia Scheme, the Bank will need to manage the liabilities that could arise on separation from The Co-operative Group. This will require the co-operation of the Trustees of the Britannia Scheme, which may not be forthcoming. It is not practicable to provide an estimate of the financial impact of these matters or what effect if any that these matters may have upon the Bank's operative revenues, cash flows or financial position in any period.

Former Britannia Building Society pension scheme guarantee

Following the transfer of engagements of Britannia Building Society, in 2009 the Britannia pension scheme transferred to CFSMS. Under the terms of this transfer the Bank entered into a deed of guarantee to provide assurance to the trustees of the pension scheme to support CFSMS in meeting its funding obligations to the scheme should CFSMS be unable to pay its obligations as they fall due. However, The Co-operative Group has undertaken to ensure that, CFSMS will not take or omit to take any action without the Bank's prior agreement if the result would be to increase the Bank's liabilities or contributions in respect of the Britannia Scheme. The most recent actuarial report indicated that the funding deficit in the Britannia Scheme as at 5 April 2013 was £61.0m. The scheme was recognised in 2014 as explained in note 35.

Tax treatment of separation

Until separation of the Bank from The Co-operative Group is complete, the Bank will continue to be responsible for indemnifying CFSMS under the CFSMS-Bank Services Agreement.

During 2013, the Directors reviewed and reconsidered the accounting treatment of the intangible asset in development and all other assets held on the balance sheet of CFSMS which were used solely by the Bank. The Directors concluded that the Bank was substantially exposed to the risks and rewards of these assets and after considering the funding of the asset and CFSMS's lack of assets to absorb losses, the appropriate accounting treatment would be to hold these assets on the balance sheet of the Bank. The Bank applied an approach to the tax and accounting treatment of the Bank exclusive assets. However, if, and that to the extent that, there is a change to this treatment, there may be an additional tax charge. In November 2014 the Bank became the legal owner of the assets held by CFSMS for the provision of services exclusively to the Bank.

There will continue to be VAT charges incurred in respect of any assets that are supplied to the Bank under the CFSMS-Bank Services Agreement that are not owned by the Bank, until separation is fully effected.

38. Related party transactions

Parent, subsidiary and ultimate controlling party

The ownership structure of the Bank changed on 20 December 2013 as a result of the LME, after which, The Co-operative Banking Group, a subsidiary of The Co-operative Group, owned approximately 30% of the Bank. The remaining, approximately 70%, was owned by a number of investors, none of which individually owned more than 10% at the end of 2013. As a result of a further share issue of £400m to existing shareholders in May 2014, The Co-operative Banking Group's share dropped to 20.16%.

At 31 December 2014, the Bank is an associate of, and therefore a related party of, The Co-operative Group as The Co-operative Group owns 20.16% of the Bank's ordinary shares, has the right to Bank Board representation and there are material transactions between the two companies.

The Bank has a significant relationship with The Co-operative Group. As part of the Recapitalisation plan and the Bank ceasing to be a wholly owned subsidiary of The Co-operative Group, the Bank entered into the following agreements and several other arrangements.

Transactions with The Co-operative Group

Balances owed by The Co-operative Group to the Bank are shown on page 221. In total these exceed amounts owed by any other single counterparty and would exceed the Bank's risk appetite in the normal course of business. These obligations are currently performing in line with expectations and based on investigations and the information provided, the Board considers that impairment is not required.

Relationship Agreement

In anticipation of the completion of the LME and the Bank ceasing to be a wholly-owned subsidiary of The Co-operative Group, the Bank entered into an agreement with The Co-operative Group and The Co-operative Banking Group on 4 November 2013 (the Relationship Agreement) to regulate the basis of their on-going relationship. For more information about the Relationship Agreement see the Corporate Governance Report Co-existence.

Principles

The Co-existence Principles govern the use of trademarks containing 'Co-operative' or 'Co-op' and other associated trademarks owned by both parties. For more information about the Co-existence Principles see the Corporate Governance Report - Co-existence Principles and the use of the 'Co-op' brand.

2014 Commitment Agreement

On 4 November 2013, The Co-operative Banking Group entered into the 2014 commitment agreement with the Bank (the 2014 Commitment Agreement), conditional on the successful implementation of the LME, to subscribe for new ordinary shares satisfied by an irrevocable undertaking to pay £333m (the Undertaking to Pay to the Bank). These commitments were satisfied with the final tranche paid by The Co-operative Group in December 2014.

Intra-group Loan

On 4 November 2013, the Bank, The Co-operative Banking Group and the Co-operative Group Limited entered into an intra-group loan facility (the Intra-group Loan) whereby the Co-operative Group Limited made available to The Co-operative Banking Group during 2014 a term loan facility of up to £313m to be utilised by way of advances. The maturity date of the loan facility is 27 July 2019.

The purpose of the Intra-group Loan was to support The Co-operative Banking Group's Undertaking to Pay the Bank the agreed 2014 capital commitment as a result of the LME, which was paid in full by December 2014.

Pensions Undertaking

On 4 November 2013, The Co-operative Group and the Bank entered into an undertaking whereby The Co-operative Group agreed with the Bank not to require the Bank to cease to participate in Pace in connection with the LME. The parties also agreed at the request of one of the parties to enter into good faith discussions to reach agreement on the separation of Pace and agree the Bank's proportion of employer contributions in Pace (and if not agreed, the matter will be referred to an independent third party). Further information is provided in note 35.

IT and other services

The Bank and The Co-operative Group entered into an IT Costs Separation Agreement on 22 January 2015, in consequence of the Bank's IT outsourcing agreement with IBM for enterprise computing services the Bank is not progressing the proposed revised IT Service Agreement (ITSA) and Professional Services Master Service Agreement (PSMSA) which were described in the 2013 Annual Report and Accounts. A number of service contracts under the PSMSA have now been terminated and services repatriated to the Bank, with the intention that all will be terminated by the end of 2015 except pensions and membership.

IT separation costs agreement

Under the IT costs separation agreement, both CGL and CFSMS undertake to support activities for the separation of the Bank's IT infrastructure from the wider Co-operative Group's IT infrastructure, to enable the smooth transition to IBM. Further, CGL and CFSMS undertake that any notice to terminate the existing IT services agreement (in the case of CGL) and the CFSMS-Bank Framework Agreement (in the case of CFSMS) would not take effect prior to 31 December 2017 to give the Bank sufficient time to separate the Bank's IT infrastructure. The IT separation costs agreement also allocated the contributions to be made towards The Co-operative Group's own costs of keeping the wider Co-operative Group's existing IT infrastructure stable and operable during and following the Bank's separation of its IT infrastructure; to this end CBGL (as the parent of CFSMS) undertook to contribute a maximum of £95m towards such Co-operative Group costs, with the Bank to make a contribution of up to £25m, based on a formula in the event that the total cost of this Co-operative Group project falls between £76m and £120m.

Deed of surrender and release – Bank ATMs in Group Food stores

On 1 January 2008 the Bank was granted a licence by CGL to install and operate ATMs at a number of Co-operative Food stores in the UK. On 14 April 2014 CGL served notice on the Bank to terminate this licence with effect from 1 January 2016. As part of a new arrangement between CGL and another third party, on 20 November 2014 CGL and the Bank entered into a deed for the Bank to surrender immediately any rights of occupation it may have in relation to these premises. In consideration for this early surrender, CGL paid to the Bank £2.9m, with a further £5.2m to be received in 2015. The Bank entered into a simultaneous agreement with Cardtronics UK Limited for the sale of these ATMs in CGL premises.

CFSMS transactions

CFSMS is a subsidiary of The Co-operative Banking Group and continues to undertake the provision of supplies and services on behalf of the Bank. Further details of the CFSMS - Bank Framework agreement are disclosed below.

CFSMS-Bank Framework

On 16 February 2006, the Bank and CFSMS entered into the CFSMS-Bank Services Agreement pursuant to which CFSMS provides assets such as office equipment, materials and office space, other facilities and services, and consultants who act as secondees to the Bank. The Bank provides CFSMS with an indemnity for all liabilities, losses, damages, costs and expenses of any nature as a result of CFSMS entering into and performing the agreement in respect of the assets, services and personnel provided to the Bank.

The Bank and CFSMS commenced unwinding this arrangement during 2014 with the transfer of the employment of most staff to the Bank (see 'Transfer of Staff from CFSMS to Bank' below), the transfer of assets to the Bank (see 'Tangible and Intangible Assets' below) and the Bank entering in to numerous contracts with third party suppliers to replace those previously provided through CFSMS or the wider Co-operative Group. These activities continue into 2015, in particular in respect of the Bank's transition of enterprise services to IBM (see note 41).

Tax loss share

As part of the negotiations relating to the separation of the Bank from The Co-operative Group, the Bank and The Co-operative Group also agreed terms relating to the surrender of group relief between the entities in the Bank's tax group and entities in The Co-operative Group tax group. A deed sets out the basis of the agreement by The Co-operative Group to take proactive steps to allow it to maximise its claim for tax losses from the Bank for the accounting periods to 31 December 2012 and 2013. The deed also addresses the terms of the payment by The Co-operative Group to the Bank for those tax losses. The 2014 financial statements, which include a group relief debtor of £126.8m (2013: £126.6m), have been prepared on a basis consistent with the deed. The Bank receive payment from The Co-operative Group when The Co-operative Group realises the benefit of the losses surrendered and at the corporation tax rate at which the benefit is realised.

Transfer of staff from CFSMS to Bank

As explained in relation to the CFSMS-Bank Framework above, from 16 February 2006 CFSMS provided consultants acting as secondees to the Bank. The employment of substantially all Bank dedicated staff provided under that arrangement was transferred to the Bank under the Transfer of Undertakings (Protection of Employment) Regulations, on 23 January 2014.

IT security

The Bank's specialist IT security team will continue to provide an IT security service in relation to the IT infrastructure which the Bank and Co-operative Insurance Services General Insurance Limited (CISGIL) share until that infrastructure is separated. This service comprises of a small number of people. The Bank has historically provided ad hoc IT security services to The Co-operative Group. Whilst no services are currently being provided, the Bank and The Co-operative Group entered in to an agreement to provide a framework for future services on 28 November 2014.

Tangible and intangible assets

A number of assets were originally purchased by CFSMS using funds advanced by the Bank and then provided to the Bank by CFSMS under the 2006 CFSMS-Bank Services Agreement referred to above. In 2013, the Directors of the Bank concluded these assets met the accounting criteria to be shown as assets for the Bank, and therefore reported them on the balance sheet. This is referred to in more detail in the 2013 Annual Report and Accounts. Legal title of these assets transferred to the Bank in 2014.

As part of the separation activity, in November 2014 the Bank purchased the legal title of all Bank specific assets held by CFSMS (shared assets remained with CFSMS) through an SPV called CBG Asset Management Limited. The carrying value of these assets on the balance sheet at 31 December 2014 is £126.0m (2013: £127.8m).

Balances with The Co-operative Group

The tables below provide an analysis of balances with The Co-operative Group and its undertakings at 31 December 2014 and 31 December 2013 and their location within the Bank's balance sheet.

2014

	Loans & advances to customers	Other assets	Customer accounts	Other liabilities
The Co-operative Group	**51.0**	**127.1**	**(163.7)**	**-**
The Co-operative Banking Group Ltd	**-**	**-**	**(55.5)**	**-**
Subsidiaries of The Co-operative Banking Group Ltd	**-**	**35.7**	**(27.3)**	**(126.0)**
	51.0	**162.8**	**(246.5)**	**(126.0)**

2013

	Loans & advances to customers	Other assets	Customer accounts	Other liabilities
The Co-operative Group	110.1	126.6	(26.7)	-
The Co-operative Banking Group Ltd	-	303.2	(49.6)	-
Subsidiaries of The Co-operative Banking Group Ltd	-	-	(16.0)	(156.5)
	110.1	429.8	(92.3)	(156.5)

	2014		2013	
	Interest and fees received	**Interest and fees paid**	Interest and fees received	Interest and fees paid
The Co-operative Group Limited	**6.3**	**2.1**	5.0	0.6
The Co-operative Banking Group Ltd	**-**	**-**	-	-
Subsidiaries of The Co-operative Banking Group Ltd	**0.3**	**-**	0.7	-
	6.6	**2.1**	5.7	0.6

A number of transactions are entered into with related parties in the normal course of business on normal commercial terms. These include loans and deposits. Outstanding balances at the year end and related income and expense for the year is presented in the tables above.

Shareholder rights agreement

At the time of the capital raising in May 2014, the Bank entered into a Shareholder Rights Agreement with The Co-operative Group and a number of other investors. As at 31 December 2014, SP COOP INVESTMENTS LTD owns more than 10% of the Bank's ordinary shares and is therefore a related party of the Bank.

The Shareholder Rights Agreement grants certain rights to the shareholders including the right of Silverpoint and Perry Capital (who hold less than 10%) to nominate a Director for appointment to the Board for so long as it continues to own 5% or more of the Bank. In addition, the Shareholder Rights Agreement grants the right for one Director to be appointed to a sub-committee of the Board to assess the feasibility of the Bank listing its ordinary shares on the London Stock Exchange (IPO Committee).

Transactions with other related parties

Key management, as defined by IAS 24 (Related Party Disclosures), are considered to be Board and Executive members of the Bank, and Board and Executive members of the Bank's immediate and ultimate holding organisations. The volume of related party transactions with key management is provided below:

Directors, key management personnel and close family members

	2014	2013
Loans outstanding at the beginning of the year	**0.3**	2.6
Net movement	**(0.3)**	(2.3)
Loans outstanding at the end of the year	**-**	0.3

	2014	2013
Deposits and investments at the beginning of the year	**0.2**	2.4
Net movement	**-**	(2.2)
Deposits and investments at the end of the year	**0.2**	0.2

Directors' loans

	2014			2013		
	Mortgages	Personal loans	Credit cards	Mortgages	Personal loans	Credit cards
Number of Directors with loan type	-	-	-	1.0	1.0	1.0
Total value of Directors' loans	-	-	-	0.2	-	-

Key management compensation

	2014	2013
Salaries and short term benefits	**6.3**	3.4
Termination benefits	**-**	0.5
	6.3	3.9

Executive Directors' remuneration

A list of the members of the Board of Directors is shown on page 42. The total remuneration of Executive Directors was £3.6m (2013: £2.3m)

Further details of Directors' remuneration are provided in the Directors' Remuneration report.

39. Share capital

	2014		2013	
	No. of shares (millions)	**Share capital**	No. of shares (millions)	Share capital

Allotted, called up and fully paid (ordinary shares of 5p each)				
At the beginning of the year	**250.0**	**12.5**	8,200.0	410.0
Shares cancelled	**-**	**-**	(8,200.0)	(410.0)
Issue of new ordinary shares	**200.5**	**10.0**	250.0	12.5
Issue of new bonus shares	**1.0**	**0.1**	-	-
At the end of the year	**451.5**	**22.6**	250.0	12.5

Share premium account		
At the beginning of the year	**1,359.8**	8.8
Issue of new ordinary shares	**377.2**	1,351.0
Issue of new bonus shares	**(0.1)**	
At the end of the year	**1,736.9**	1,359.8

The £400.0m capital raising completed in May 2014 resulted in an issuance of new ordinary share capital of £10.0m and a gross increase in share premium of £390.0m. Bonus shares of £0.1m were also issued. As part of the capital raising the Bank incurred transaction costs of £12.8m. These were offset against the gross share premium amount, giving a net increase in capital of £387.2m, of which £377.1m was recorded as share premium.

The number of ordinary shares in issue at 31 December 2014 was 451,456,510 (2013: 250,000,000). The ordinary shareholders have one vote for every share held.

Liability Management Exercise

This exercise involved issuing new shares and new debt in exchange for cash and extinguishing existing debt and preference shares.

The Bank announced, in November 2013, a Recapitalisation plan to generate £1.5bn additional CET1, which was discussed with the relevant regulatory bodies. The key objective of the plan was to strengthen significantly the Bank's CET1 base with the support and participation of certain holders of the Bank's securities and without the need for support from the taxpayer.

The £1.5bn Recapitilisation plan consisted of three elements:

a) The Liability Management Exercise (LME) to generate c.£1.2bn of new CET1;
b) The commitment of The Co-operative Group to contribute £333m of CET1 by the end of 2014; and
c) £40m of CET1 generated in 2014 from interest savings on the securities surrendered in the LME.

The transaction has been accounted for in accordance with IFRIC 19: Extinguishing Financial Liabilities with Equity Instruments.

Details of the Liability Management Exercise

a) The LME

A core part of the Recapitalisation plan was achieved through successful completion of the LME on 20 December 2013. This involved the following elements:

i. The issuance in 2013 of £0.2bn of new subordinated debt and £0.6m of new ordinary shares in exchange for £1.3bn of existing debt and preference shares and additional contribution from bondholders of £0.1bn;

ii. The cancellation in 2013 of £0.4bn of existing ordinary share capital, which resulted in the creation of a capital redemption reserve of the same value; and

iii. The sale of investment assets that were used as economic hedges for the existing debt, generating a profit of £11.1m, in 2013. These assets had been accounted for as available for sale, and therefore there was an equivalent reduction in the available for sale reserve.

b) The contribution of £333m by The Co-operative Group. This was paid as follows:

i. £20m paid in December 2013;

ii. £50m paid in January 2014;

iii. £100m paid on 30 June 2014; and

iv. £163m paid on 31 December 2014.

c) The balance of the £1.5bn is £40m of savings in 2014 generated on securities surrendered as part of the LME

Elements a) and b) together created additional CET1 in the following ways:

i. New ordinary share – a total of £0.8bn of new ordinary shares were issued in 2013 to both existing bondholders and The Co-operative Banking Group. This was recorded as share capital and share premium as shown in the table below.

ii. Income - £0.7bn was recognised in the 2013 income statement. This arose because the amount of debt extinguished and contributions received (£1.3bn and £0.4bn) was greater than the amount of the new debt and shares issued (£0.2bn and £0.8bn). In accordance with company law, which requires that the share premium is determined by reference to the amount of debt extinguished, the element of income relating to new shares issues (£0.6bn) was transferred from retained earnings to share premium.

Effect of the Recapitalisation plan on 2013 profit and reserves

		Effect on reserves – 2013					
	Profit	Share capital	Share premium	Available for sale reserve	Capital redemption reserve	Retained earnings	Net effect on reserves
Issuance of new debt and ordinary shares in exchange for existing debt and contributions	707.7	12.5	777.5	-	-	707.7	1,497.7
Sale of assets hedging pre-LME debt positions	11.1	-	-	(11.1)	-	11.1	-
Effect of transactions with a profit impact (before costs)	718.8	12.5	777.5	(11.1)	-	718.8	1,497.7
Costs associated with LME transaction	(30.5)	-	(21.3)	-	-	(30.5)	(51.8)
Effect of transactions with a profit impact (after costs)	688.3	12.5	756.2	(11.1)	-	688.3	1,445.9

Other LME transactions (with no profit impact):							
Cancellation of share capital (capital redemption reserve created)	-	(410.0)	-	-	410.0	-	-
Transfer of retained earnings to share premium account	-	-	594.8	-	-	(594.8)	-
Total effect of recapitalisation transactions on profit and reserves	688.3	(397.5)	1,351.0	(11.1)	410.0	93.5	1,445.9

40. Fair values of financial assets and liabilities

The fair values in this note are stated at a specific date and may be significantly different from the amounts which will actually be paid on the maturity or settlement dates of the instruments. The tables below analyse the balance sheet carrying values of financial assets and liabilities by classification.

Balance sheet categories	Held for trading	Designated at fair value	Loans and receivables	Available for sale	Liabilities at amortised cost	Derivatives in a hedging relationship	Total
2014							
Assets							
Cash and balances at central banks	**-**	**-**	**4,765.3**	**-**	**-**	**-**	**4,765.3**
Loans and advances to banks	**-**	**-**	**1,608.4**	**-**	**-**	**-**	**1,608.4**
Loans and advances to customers	**3.9**	**182.7**	**25,190.8**	**-**	**-**	**-**	**25,377.4**
Fair value adjustments for hedged risk	**-**	**-**	**148.5**	**-**	**-**	**-**	**148.5**
Investment securities	**-**	**1,236.9**	**18.1**	**3,167.5**	**-**	**-**	**4,422.5**
Derivative financial instruments	**250.6**	**-**	**-**	**-**	**-**	**220.1**	**470.7**
Equity shares	**-**	**-**	**-**	**2.8**	**-**	**-**	**2.8**
Other assets	**-**	**-**	**187.6**	**-**	**-**	**-**	**187.6**
Total financial assets	**254.5**	**1,419.6**	**31,918.7**	**3,170.3**	**-**	**220.1**	**36,983.2**
Non-financial assets							**599.7**
Total assets							**37,582.9**

Liabilities

Deposits by banks	**-**	**-**	**-**	**-**	**615.4**	**-**	**615.4**
Customer accounts	**-**	**-**	**-**	**-**	**29,614.0**	**-**	**29,614.0**
Customer accounts – capital bonds	**-**	**263.8**	**-**	**-**	**-**	**-**	**263.8**
Debt securities in issue	**-**	**-**	**-**	**-**	**3,443.6**	**-**	**3,443.6**
Derivative financial instruments	**176.0**	**-**	**-**	**-**	**-**	**375.7**	**551.7**
Other borrowed funds	**-**	**-**	**-**	**-**	**196.4**	**-**	**196.4**
Other liabilities	**-**	**-**	**-**	**-**	**150.9**	**-**	**150.9**
Total financial liabilities	**176.0**	**263.8**	**-**	**-**	**34,020.3**	**375.7**	**34,835.8**
Non-financial liabilities							**732.6**
Total liabilities							**35,568.4**
Capital and reserves							**2,014.5**
Total liabilities and equity							**37,582.9**

IAS 39 requires derivative financial instruments that are not in a hedging relationship to be classified as ‘held for trading’; this definition differs from the definition of ‘derivatives held for trading purposes’ as shown in note 20.

Balance sheet categories	Held for trading	Designated at fair value	Loans and receivables	Available for sale	Liabilities at amortised cost	Derivatives in a hedging relationship	Total
2013 restated (1)							
Assets							
Cash and balances at central banks	-	-	5,418.8	-	-	-	5,418.8
Loans and advances to banks	-	-	1,594.4	-	-	-	1,594.4
Loans and advances to customers	-	134.2	30,151.9	-	-	-	30,286.1
Fair value adjustments for hedged risk	-	-	106.3	-	-	-	106.3
Investment securities	-	1,743.4	23.6	2,732.4	-	-	4,499.4
Derivative financial instruments	252.0	-	-	-	-	303.8	555.8
Equity shares	-	-	-	5.8	-	-	5.8
Other assets	-	-	480.9	-	-	-	480.9
Total financial assets	252.0	1,877.6	37,775.9	2,738.2	-	303.8	42,947.5

Non-financial assets							436.3
Total assets							43,383.8
Liabilities							
Deposits by banks	-	-	-	-	2,757.5	-	2,757.5
Customer accounts	-	-	-	-	32,463.3	-	32,463.3
Customer accounts - capital bonds	-	538.1	-	-	-	-	538.1
Debt securities in issue	-	-	-	-	4,207.6	-	4,207.6
Derivative financial instruments	168.6	-	-	-	-	370.0	538.6
Other borrowed funds	-	-	-	-	196.3	-	196.3
Other liabilities	-	-	-	-	202.9	-	202.9
Total financial liabilities	168.6	538.1	-	-	39,827.6	370.0	40,904.3
Non-financial liabilities							711.0
Total liabilities							41,615.3
Capital and reserves							1,768.5
Total liabilities and equity							43,383.8

(1) The 2013 comparatives have been restated as described in note 3.

a) Use of financial instruments

The use of financial instruments is essential to the Bank's business activities, and financial instruments constitute a significant proportion of the Bank's assets and liabilities. The main financial instruments used by the Bank, and the purposes for which they are held, are outlined below:

Loans and advances to customers and customer accounts

The provision of banking facilities to customers is the primary activity of the Bank, and loans and advances to customers and customer accounts are major constituents of the balance sheet. Loans and advances to customers include retail mortgages, corporate loans, credit cards, unsecured retail lending and overdrafts. Customer accounts include retail and corporate current and savings accounts.

Loans and advances to banks and investment securities

Loans and advances to banks and investment securities underpin the Bank's liquidity requirements and generate incremental net interest income. Held for trading investments are held for economic hedging purposes only as the Bank does not have an active trading book.

Deposits by banks and debt securities in issue

The Bank issues medium term notes within an established euro medium term note programme and also issues certificates of deposit and commercial paper as part of its normal treasury activities.

Other borrowed funds

The Bank utilises a broad spread of long term wholesale funding in the form of fixed rate subordinated debt in addition to funding from ordinary share capital and retained earnings. Refer to note 30 for details of changes to other borrowed funds as a result of the LME.

Derivatives

A derivative is a financial instrument that derives its value from an underlying rate or price such as interest rates, exchange rates and other market prices. Derivatives are an efficient means of managing market risk and limiting counterparty exposure. The Bank uses them mainly for hedging purposes and to meet the needs of customers.

The most frequently used derivative contracts are interest rate swaps, exchange traded futures and options, caps and floors, currency swaps and forward currency transactions. Terms and conditions are determined by using standard industry documentation. Derivatives are subject to the same market and credit risk control procedures as are applied to other wholesale market instruments and are aggregated with other exposures to monitor total counterparty exposure which is managed within approved limits for each counterparty.

Foreign exchange

The Bank undertakes foreign exchange dealing to facilitate customer requirements and to generate incremental income from short term trading in the major currencies. Structured risk and trading related risk are managed formally within position limits which are set by the ALCO, to which authority is delegated by the Board.

b) Valuation of financial assets and liabilities at fair value

The following tables analyse financial assets and liabilities carried at fair value by the three level fair value hierarchy defined as follows:

- Level 1 – Quoted market prices in active markets
- Level 2 – Valuation techniques using observable inputs
- Level 3 – Valuation techniques using unobservable inputs

	Fair value at end of the reporting period using:			
	Level 1	**Level 2**	**Level 3**	**Total**
2014				
Non-derivative financial assets				
Held for trading:				
Loans and advances to customers	**-**	**3.9**	**-**	**3.9**
Designated at fair value:				
Loans and advances to customers	**-**	**176.0**	**6.7**	**182.7**
Investment securities	**1,236.9**	**-**	**-**	**1,236.9**
Available for sale financial assets:				
Investment securities	**3,022.5**	**145.0**	**-**	**3,167.5**
Equity shares	**0.1**	**2.7**	**-**	**2.8**

Derivative financial instruments	**-**	**470.7**	**-**	**470.7**
Non-financial instruments				
Investment properties	**-**	**-**	**2.1**	**2.1**
Total assets carried at fair value	**4,259.5**	**798.3**	**8.8**	**5,066.6**
Non-derivative financial liabilities				
Designated at fair value:				
Customer accounts – capital bonds	**-**	**263.8**	**-**	**263.8**
Derivative financial instruments	**-**	**551.7**	**-**	**551.7**
Total liabilities carried at fair value	**-**	**815.5**	**-**	**815.5**

	Fair value at end of the reporting period using:			
	Level 1	Level 2	Level 3	Total
2013				
Non-derivative financial assets				
Designated at fair value:				
Loans and advances to customers	-	125.5	8.7	134.2
Investment securities	1,743.4	-	-	1,743.4
Available for sale financial assets:				
Investment securities	2,497.2	235.2	-	2,732.4
Equity shares	0.1	5.7	-	5.8
Derivative financial instruments	-	525.3	30.5	555.8
Non-financial instruments				
Investment properties	-	157.9	6.2	164.1
Total assets carried at fair value	4,240.7	1,049.6	45.4	5,335.7
Non-derivative financial liabilities				
Designated at fair value:				
Customer accounts – capital bonds	-	538.1	-	538.1
Derivative financial instruments	-	477.4	61.2	538.6
Total liabilities carried at fair value	-	1,015.5	61.2	1,076.7

The carrying values of financial instruments measured at fair value are determined in compliance with the accounting policies on pages 154 to 168 and according to the following hierarchy:

Level 1 – Quoted market prices in active markets

Financial instruments with quoted prices for identical instruments in active markets. The best evidence of fair value is a quoted market price in an actively traded market.

Level 2 – Valuation techniques using observable inputs

Financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.

The valuation techniques used to value these instruments employ only observable market data and relate to the following assets and liabilities.

Loans and advances to customers

Loans and advances to customers include corporate loans of £164.7m (2013: £125.5m) which are fair valued through income or expense using observable inputs. Loans held at fair value are valued at the sum of all future expected cash flows, discounted using a yield curve based on observable market inputs.

Investment securities – available for sale

Fair value is based on available market prices. Where this information is not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

Derivative financial instruments

Over-the-counter (ie non-exchange traded) derivatives are valued using valuation models which are based on observable market data. Valuation models calculate the present value of expected future cash flows, based upon 'no arbitrage' principles. The Bank enters into vanilla foreign exchange and interest rate swap derivatives, for which modelling techniques are standard across the industry. Examples of inputs that are generally observable include foreign exchange spot and forward rates, and benchmark interest rate curves.

Investment properties

Investment properties are carried at fair value. For those within Level 2 fair value is calculated by using recent valuations of individual assets within the portfolio, indexed linked to the balance sheet date using the relevant regional house price index where appropriate.

Customer accounts – capital bonds

The estimated fair value of customer accounts – capital bonds is based on independent third party valuations using forecast future movements in the appropriate indices.

Equity shares

Equity shares primarily relate to investments held in VocaLink Holdings Limited which are unquoted shares. The valuation of these shares is based on the Bank's percentage shareholding and the net asset value of the consolidated group according to its most recently published financial statements.

Level 3 – Valuation techniques using unobservable inputs

This is used for financial instruments valued using models where one or more significant inputs are not observable.

The small proportion of financial assets valued based on significant unobservable inputs are analysed as follows:

Loans and advances to customers

Loans and advances to customers include 25 year fixed rate mortgages of £6.7m (2013: £8.7m) which are fair valued through income or expense using unobservable inputs. 25 year fixed rate mortgages are valued using future interest cash flows at the fixed customer rate and estimated schedule of customer repayments. Cash flows are discounted at a credit adjusted discount rate; the credit adjustment is based on the average margin of new long dated (five years or greater) fixed rate business written in the last six months, and subject to quarterly review. The eventual timing of future cash flows may be different from that forecast due to unpredictable customer behaviour, particularly on a 25 year product. The valuation methodology takes account of credit risk and has decreased the valuation by £0.5m in 2014 (2013: £0.8m decrease). A reasonable change in the assumptions would not result in any material change in the valuation.

Derivative financial instruments

Derivative financial instruments in the form of interest rate swaps have been entered into between the Bank and its subsidiaries, and external counterparties.

The purpose of the swaps is to convert the fixed and base rate linked revenue receipts of the pool of mortgage assets to the same LIBOR linked basis as the intercompany loan. Under this swap arrangement the Bank's subsidiaries pay to the swap counterparty, the monthly mortgage revenue receipts of the pool of assets and receives from the swap counterparty LIBOR plus a contractual spread on the same notional balance, the spread being sufficient to cover the intercompany loan and any expenses. The Bank has a 'back to back' swap that is the mirror image of the subsidiaries' swaps.

The swaps are valued based on an assumed amortisation profile of the pool of assets to the bond maturity date (assuming some annual prepayment), an assumed profile of customer receipts over this period, and LIBOR prediction using forward rates. Swap cash flows are discounted to present value using mid-yield curve zero coupon rates, ie no adjustment is made for credit losses, nor for transaction or any other costs.

Movements in fair values of instruments with significant unobservable inputs (level 3) were:

	Fair value at the beginning of the year	Purchases and transfers in	Sales and transfers out (1)	Income or expense including impairment	Fair value at the end of the year
2014					
Loans and advances to customers	**8.7**	**-**	**(1.5)**	**(0.5)**	**6.7**
Derivative assets	**30.5**	**-**	**(30.5)**	**-**	**-**
Derivative liabilities	**(61.2)**	**-**	**61.2**	**-**	**-**
Investment properties	**6.2**	**-**	**(4.3)**	**0.2**	**2.1**
	(15.8)	**-**	**24.9**	**(0.3)**	**8.8**
2013					
Loans and advances to customers	11.2	-	(1.7)	(0.8)	8.7
Derivative assets	35.4	12.6	(22.6)	5.1	30.5

Derivative liabilities	(12.4)	(52.0)	0.6	2.6	(61.2)
Investment properties	173.0	-	(166.6)	(0.2)	6.2
	207.2	(39.4)	(190.3)	6.7	(15.8)

(1) See note on page 231

c) Fair values of financial assets and liabilities not carried at fair value

The carrying values of financial instruments measured at amortised cost are determined in compliance with the accounting policies on pages 154 to 168.

The table below sets out a summary of the carrying and fair values of:

- financial assets classified as loans and receivables; and
- financial liabilities classified as held at amortised cost,

unless there is no significant difference between carrying and fair values.

	Carrying value	Fair value
2014		
Financial assets		
Loans and advances to banks	**1,608.4**	**1,608.4**
Loans and advances to customers	**25,190.8**	**23,657.6**
Fair value adjustments to hedged risk	**148.5**	**148.5**
Investments securities	**18.1**	**14.3**
Other assets	**187.6**	**187.6**
Financial liabilities		
Deposits by banks	**615.4**	**615.4**
Customer accounts	**29,614.0**	**29,625.6**
Debt securities in issue	**3,443.6**	**3,478.9**
Other borrowed funds	**196.4**	**223.2**
Other liabilities	**150.9**	**150.9**

	Carrying value (restated) (1)	Fair value (restated) (1)	Fair value (apply 2014 Methodology) (2)
2013			
Financial assets			
Loans and advances to banks	**1,594.4**	**1,594.4**	**1,594.4**

Loans and advances to customers	**30,151.9**	**27,776.9**	**27,939.5**
Fair value adjustments to hedged risk	**106.3**	**106.3**	**106.3**
Investments securities	**23.6**	**21.4**	**21.4**
Other assets	**480.9**	**480.9**	**480.9**
Financial liabilities			
Deposits by banks	2,757.4	2,757.4	2,757.4
Customer accounts	32,463.3	32,488.3	32,488.3
Debt securities in issue	4,207.6	4,716.1	4,716.1
Other borrowed funds	196.3	234.2	234.2
Other liabilities	202.9	202.9	202.9

(1) The 2013 comparatives have been restated as described in note 3.

(2) In 2014, the Bank reviewed and improved the methods used to calculate the fair values. The 2013 comparatives for loans and advances to customers have been recalculated accordingly to reflect these changes in methods.

Key considerations in the calculation of fair values for loans and receivables and financial liabilities at amortised cost are as follows:

Loans and advances to banks/deposits by banks

Loans and advances to banks include interbank placements and items in the course of collection.

The amortised cost value of all loans and advances to banks are deemed to be a close approximation of their fair value due to their short maturity. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money market interest rates for debts with similar credit risk and remaining maturity.

Loans and advances to customers

The fair value of loans and advances to customers is calculated by segmenting the overall balance into Retail, Optimum and Corporate.

- ***Retail***

Fixed rate loans and advances to customers are revalued to fair value based on future interest cash flows and principal cash flows discounted using an appropriate market rate. The market rate applied in the calculation is the average market rate for new originations of mortgages with similar characteristics to the book of mortgages being valued. This rate is assumed to encompass the time value of money, plus a risk premium to account for the inherent uncertainty and the timing and amount of future cashflows arising from a book of mortgage assets.

Forecast principal repayments are based on redemption at the earlier of maturity or re-pricing date with some overlay for historical behavioural experience where relevant. The eventual timing of future cash flows may be different from the forecast due to unpredictable customer behaviour. It is assumed that there would be no other factors which market participants would take into account when assessing the fair value of the Retail mortgage assets. It is assumed there is no fair value adjustment required in respect of interest rate movement on standard variable rate mortgage assets, as the interest rate being charged is assumed to be equal to the market rate for those mortgage assets.

- ***Optimum***

Fair values have been calculated using the future lifetime spread income approach. Under this approach, value is measured by determining discounted expected cashflows, derived using redemption profiles, from the portfolio and applying the future lifetime spread which reflects the difference between current market rates for products with similar characteristics and risk profiles and the actual rates the portfolio is generating. The current market rate used is assumed to encompass the time value of money, plus a risk premium to account for the inherent uncertainty in the timing and amount of future cash flows arising from a book of mortgage assets.

- ***Corporate***

As part of the implementation of the Bank's strategy for Non-core assets, certain assets have either already been sold after the year end or plans to sell are well advanced. For these assets, the fair value can therefore be determined from the actual sale price achieved or expected to be received.

For other corporate assets an expected cashflow income approach has been used. Under this approach, value is measured by determining expected cashflows, derived using redemption profiles, from the portfolio and then considering credit costs, funding costs and tax to derive equity cashflows which are discounted at an appropriate blended cost of capital. The blended cost of capital is taken as an average of quoted cost of capital for the six largest listed banks in the UK, as this is assumed to represent the rate at which market participants would discount the future cash flows of a portfolio of corporate loans when assessing the fair value of such a portfolio.

The fair value of loans and advances to customers in total is 96% of the carrying value as at 31 December 2014 (2013 when applying 2014 methodology: 93%). The overall fair values are less than par primarily due to two main factors for Non-core loans in particular:

- Customer interest rates are below the market rate at the balance sheet date until expected maturity or the re-pricing date, if earlier; and
- Credit risk adjustments due to incurred and expected future credit losses.

Investment securities

Fair value is based on available market prices. Where this information is not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

Customer accounts

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest bearing deposits and other borrowings without quoted market prices is based on future interest cash flows (at funding rates) and principal cash flows, discounted using an appropriate market rate.

Debt securities in issue and other borrowed funds

The aggregate fair values are calculated based on quoted market prices where available. For those notes where quoted market prices are not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics. Quoted prices may be from inactive markets.

The fair value of debt securities in issue is significantly above the carrying value as a result of the carrying value being net of merger fair value adjustments. The carrying values of debt securities in issue are expected to increase as the merger fair value adjustments continue to unwind, as shown in the following section.

Unwind of merger fair value adjustments

On the merger of the Bank and Britannia Building Society in August 2009 an exercise was undertaken to fair value the respective assets and liabilities of Britannia Building Society. These fair value adjustments are unwound on an EIR basis over the effective lives of the assets and liabilities. As at 31 December 2014, the remaining merger fair value unwinds and the forecast unwind profiles can be summarised as follows:

				Forecast unwind			
	Carrying amount at year end	Remaining merger fair value to be unwound at year end	Actual unwind for the year to 31 December 2014	2015	2016	2017	2018+
2014							
Assets							
Loans and advances to customers	**25,377.4**	**(44.8)**	**(10.1)**	**(4.3)**	**(4.0)**	**(3.7)**	**(32.8)**
Fair value adjustment for hedged risk	**148.5**	**(21.0)**	**(16.7)**	**(2.7)**	**(2.5)**	**(2.4)**	**(13.4)**
Other	**12,057.0**	**27.0**	**9.0**	**4.5**	**4.5**	**4.5**	**13.5**
Total assets	**37,582.9**	**(38.8)**	**(17.8)**	**(2.5)**	**(2.0)**	**(1.6)**	**(32.7)**
Liabilities							
Debt securities in issue	**3,443.6**	**(378.6)**	**(109.2)**	**(144.6)**	**(176.0)**	**(58.0)**	**-**
Deferred tax liabilities	**84.0**	**76.4**	**16.5**	**29.8**	**36.4**	**11.9**	**(1.7)**
Other	**32,040.8**	**-**	**0.5**	**-**	**-**	**-**	**-**
Total liabilities	**35,568.4**	**(302.2)**	**(92.2)**	**(114.8)**	**(139.6)**	**(46.1)**	**(1.7)**

A breakdown of the unwind on debt securities in issue held at merger is as follows:

							Forecast unwind		
Issue Name	**Issue date**	**Contractual maturity date**	**Carrying amount at year end**	**Fair value at year end**	**Remaining merger fair value to be unwound at year end**	**Actual unwind for the year to 31 December 2014**	**2015**	**2016**	**2017**
2014									
Leek Finance Number Seventeen plc	April 2006	June 2016	**581.5**	**585.9**	**77.0**	**36.6**	**47.5**	**29.5**	**-**
Leek Finance Number Eighteen plc	October 2006	December 2016	**724.2**	**722.9**	**123.4**	**39.7**	**51.4**	**72.0**	**-**
Leek Finance Number Nineteen plc	April 2007	June 2017	**712.8**	**710.9**	**186.7**	**35.8**	**49.7**	**78.1**	**58.9**
Total Leek Notes			**2,018.5**	**2,019.7**	**387.1**	**112.1**	**148.6**	**179.6**	**58.9**

Of which liabilities held internally within the Bank are as follows:

Issue Name	Carrying amount at year end	Fair value at year end	Remaining merger fair value to be unwound at year end	Actual unwind for the year to 31 December 2014	Forecast Unwind		
					2015	2016	2017
2014							
Internally Held Leek Notes	**549.6**	**544.7**	**8.6**	**4.2**	**4.1**	**3.6**	**0.9**

Fair values of financial assets and liabilities which are not carried at fair value and bases of valuation

Fair values are determined according to the hierarchy set out on page 230.

	Carrying value	Level 1	Level 2	Level 3
2014				
Financial assets				
Loans and receivables:				
Loans and advances to banks	**1,608.4**	**-**	**1,608.4**	**-**
Loans and advances to customers	**25,190.8**	**-**	**-**	**23,657.6**
Fair value adjustment for hedged risk	**148.5**	**-**	**-**	**148.5**
Investment securities	**18.1**	**14.3**	**-**	**-**
Financial liabilities				
Financial liabilities at amortised cost				
Deposits by banks	**615.4**	**-**	**615.4**	**-**
Customer accounts	**29,614.0**	**-**	**29,625.6**	**-**
Debt securities in issue	**3,443.6**	**789.1**	**2,689.8**	**-**
Other borrowed funds	**196.4**	**-**	**223.2**	**-**

The carrying value is a reasonable approximation of fair value for the following assets and liabilities: loans and advances to banks, other assets, deposits by banks and other liabilities.

	Carrying value	Level 1	Level 2	Level 3
2013				
Financial assets				
Loans and receivables:				
Loans and advances to banks	1,594.4	-	1,594.4	-
Loans and advances to customers (1)	30,151.9	-	-	27,939.9

Fair value adjustment for hedged risk	106.3	-	-	106.3
Investment securities	23.6	21.4	-	-
Financial liabilities				
Financial Liabilities at amortised cost				
Deposits by banks	2,757.5	-	2,757.5	-
Customer accounts	32,463.3	-	32,488.3	-
Debt securities in issue	4,207.6	892.5	3,822.4	-
Other borrowed funds	196.3	-	234.2	-

(1) The 2013 fair value of loans and advances to customers has been recalculated using the 2014 methodology. Using 2013 methodology, the comparative, restated in note 3, is £27,776.9m.

d) Fair value of transferred assets and associated liabilities

Securitisation vehicles

The beneficial ownership of the loans and advances to customers sold to securitisation vehicles by the subsidiaries of the Bank fail the derecognition criteria, and consequently, these loans remain on the balance sheets of the sellers. Each seller therefore recognises a deemed loan financial liability on its balance sheet and an equivalent deemed loan asset is held on each securitisation company's balance sheet. The deemed loans are repaid as and when principal repayments are made by customers against these transferred loans and advances.

The securitisation vehicles have issued fixed and floating rate notes which are secured on the loans and advances to customers. The notes are redeemable in part from time to time, such redemptions being limited to the net capital received from mortgagors in respect of the underlying assets.

The Bank retains substantially all of the risks and rewards of ownership. The Bank benefits to the extent to which surplus income generated by the transferred mortgage portfolios exceeds the administration costs of those mortgages. The Bank continues to bear the credit risk of these mortgage assets.

The results of the securitisation vehicles listed in note 24 of the Company's Financial Statements are consolidated into the results of the Bank. The table below shows the carrying values and fair values of the assets transferred to securitisation vehicles and their associated liabilities. The carrying values presented below are the carrying amounts as recorded in the books of the subsidiaries companies, some of these issued notes are held internally by the Bank and as such are not shown in the consolidated balance sheet of the Group.

In 2014, the Bank reviewed and improved the methods used to calculate the fair values. The 2013 comparatives (with the exception of fair value adjustment for hedged risk and customer accounts) have been re-calculated accordingly to reflect these changes in methods.

	Carrying amount of transferred assets not derecognised	Carrying amount of associated liabilities	Fair value of transferred assets not derecognised	Fair value of associated liabilities	Net position
2014					
Leek Finance Number Seventeen plc	**554.0**	**581.5**	**403.1**	**585.9**	**(182.8)**

Leek Finance Number Eighteen plc	**662.9**	**724.2**	**485.0**	**722.9**	**(237.9)**
Leek Finance Number Nineteen plc	**642.9**	**712.8**	**473.6**	**710.9**	**(237.3)**
Leek Finance Number Twenty plc	**1,340.1**	**1,319.7**	**1,338.9**	**1,269.6**	**69.3**
Leek Finance Number Twenty One plc	**763.6**	**775.4**	**788.6**	**719.3**	**69.3**
Leek Finance Number Twenty Two plc	**351.1**	**366.4**	**365.3**	**341.7**	**23.6**
Silk Road Finance Number One plc	**1,126.0**	**1,135.6**	**1,126.0**	**1,130.4**	**(4.4)**
Silk Road Finance Number Three plc	**451.3**	**459.8**	**457.7**	**463.1**	**(5.4)**
Cambric Finance Number One plc	**883.4**	**902.0**	**986.2**	**878.3**	**107.9**
Meerbrook Finance Number Eight plc	**564.5**	**564.5**	**570.3**	**458.2**	**112.1**
	7,339.8	**7,541.9**	**6,994.7**	**7,280.3**	**(285.6)**

The above carrying amount of associated liabilities can be reconciled to debt securities in issue, as set out on page 202, as follows:

	Carrying value
Carrying amount of associated liabilities as given above	**7,541.9**
Internally held fixed and floating rate notes	**(4,756.0)**
Loan facilities and subdebt not included in debt securities in issue	**(506.1)**
Non securitised debt securities	**1,536.7**
Merger fair value adjustment	**(387.1)**
Other adjustments	**14.3**
Debt securities in issue per financial liabilities	**3,443.6**

Of the notes listed above, those held by the Bank are as follows:

	Carrying amount of transferred assets not derecognised	Carrying amount of associated liabilities	Fair value of assets not derecognised	Fair value of associated liabilities	Net position
2014					
Leek Finance Number Seventeen plc	**150.4**	**155.8**	**136.4**	**154.8**	**(18.4)**

Leek Finance Number Eighteen plc	**180.9**	**195.6**	**164.7**	**189.7**	**(25.0)**
Leek Finance Number Nineteen plc	**182.5**	**198.2**	**165.7**	**200.2**	**(34.5)**
Leek Finance Number Twenty plc	**1,340.1**	**1,319.7**	**1,338.9**	**1,269.6**	**69.3**
Leek Finance Number Twenty One plc	**763.6**	**775.4**	**788.6**	**719.3**	**69.3**
Leek Finance Number Twenty Three plc	**351.1**	**366.4**	**365.3**	**341.7**	**23.6**
Silk Road Finance Number One plc	**844.4**	**734.9**	**793.8**	**728.7**	**65.1**
Silk Road Finance Number Three plc	**120.9**	**108.0**	**117.2**	**107.2**	**10.0**
Cambric Finance Number One plc	**883.4**	**902.0**	**986.2**	**878.3**	**107.9**
	4,817.3	**4,756.0**	**4,856.8**	**4,589.5**	**267.3**

The above carrying value and fair value of assets held for each entity has been determined by applying the proportion of internally held liabilities.

Transferred assets include securitised gilts and loans and advances to customers that have not been derecognised by the seller. The associated liabilities include the fixed and floating rate notes, bank loans and intercompany loans that specifically relate to the funding for the assets securitised.

The difference between the fair value and carrying value of the mortgages that have been securitised within Leek 17, 18 and 19 is significantly higher than the fair value to carrying value difference for the associated liabilities. This is because it is expected that the notes will be repaid at par at the call date of the Leek liabilities whereas most of the mortgages will continue to be held on the Bank's balance sheet for a significant period after the notes have repaid and these mortgages have an interest rate which is below the equivalent market rate at the balance sheet date for loans of a similar nature.

The securitisation vehicles receive cash daily in relation to the transferred loans and advances and semi-annually for the transferred gilts. These amounts are held within loans and advances to banks until the associated liabilities' payments are due. Payments are made quarterly for all associated liabilities except for the variable funding notes associated with the transferred gilts, which are paid semi-annually. The amounts held within loans and advances to banks are not included in the table above but will be used in part to cover the repayments made on the associated liabilities.

The following table provides the fair value of the transferred assets and associated liabilities for 2013 recalculated on the basis of the new methodology applied in 2014.

	Carrying amount of transferred assets not derecognised	Carrying amount of associated liabilities	Fair value of assets not derecognised	Fair value of associated liabilities	Net position
2013 – applying 2014 fair value methodology					
Leek Finance Number Seventeen plc	588.8	624.6	605.3	619.4	(14.1)
Leek Finance Number Eighteen plc	703.1	762.5	690.1	748.1	(58.0)
Leek Finance Number Nineteen plc	680.5	749.6	670.9	737.1	(66.2)
Leek Finance Number Twenty plc	1,438.2	1,413.3	1,419.5	1,364.0	55.5
Leek Finance Number Twenty One	850.1	864.1	872.1	784.6	87.5

plc					
Leek Finance Number Twenty Two plc	372.6	389.0	383.6	356.0	27.6
Silk Road Finance Number One plc	1,466.4	1,481.2	1,461.5	1,486.3	(24.8)
Silk Road Finance Number Two plc	562.0	561.1	573.7	563.4	10.3
Silk Road Finance Number Three plc	583.1	597.9	588.2	604.6	(16.4)
Cambric Finance Number One plc	1,339.8	1,384.5	1,425.2	1,310.9	114.3
Meerbrook Finance Number Eight plc	625.9	635.8	760.1	601.4	158.7
	9,210.5	9,463.6	9,450.2	9,175.8	274.4

	Carrying amount of transferred assets not derecognised	**Carrying amount of associated liabilities**	**Fair value of assets not derecognised**	**Fair value of associated liabilities**	**Net position**
2013 – as per published report and accounts					
Leek Finance Number Seventeen plc	588.8	624.6	490.9	619.4	(128.5)
Leek Finance Number Eighteen plc	703.1	762.5	592.3	748.1	(155.8)
Leek Finance Number Nineteen plc	680.5	749.6	573.0	737.1	(164.1)
Leek Finance Number Twenty plc	1,438.2	1,413.3	1,135.1	1,364.0	(228.9)
Leek Finance Number Twenty One plc	850.1	864.1	770.1	784.6	(14.5)
Leek Finance Number Twenty Two plc	372.6	389.0	309.1	356.0	(46.9)
Silk Road Finance Number One plc	1,466.4	1,481.2	1,466.4	1,486.3	(19.9)
Silk Road Finance Number Two plc	562.0	561.1	562.5	563.4	(0.9)
Silk Road Finance Number Three plc	583.1	597.9	584.2	604.6	(20.4)
Cambric Finance Number One plc	1,339.8	1,384.5	1,238.8	1,310.9	(72.1)
Meerbrook Finance Number Eight plc	625.9	635.8	616.1	601.4	14.7
	9,210.5	9,463.6	8,338.5	9,175.8	(837.3)

Covered Bond Limited Liability Partnerships

Moorland Covered Bonds LLP was established as a result of a £1.4bn covered bond retained issuance. Loans and advances to customers of £1.9bn were transferred to Moorland Covered Bonds LLP. The transfer was funded by a loan of £1.4bn and capital contribution of £0.5bn. During October 2011 the £1.4bn loan was repaid. Following additional capital contribution repayment and on achieving Regulated Covered Bond status there was a public issuance of notes in November 2011 totaling £0.6bn. As a result of these changes, at the period end the Bank held a loan of £0.6bn (31 December 2013: £0.6bn) and a capital contribution of £0.7bn (31 December 2013: £0.9bn) with Moorland Covered Bonds LLP.

Moorland Covered Bonds LLP does not have ordinary share capital. The Bank's interest in Moorland Covered Bonds LLP is in substance no different from a wholly owned subsidiary and consequently it is fully consolidated in the Consolidated Bank accounts. The table below shows the carrying values and fair values of the assets transferred to the covered bond and their associated liabilities:

	Carrying amount of transferred loans and advances to customers	Carrying amount of fixed and floating rate notes	Fair value of transferred loans and advances to customers	Fair value of fixed and floating rate notes	Net position
2014					
Moorland Covered Bonds LLP	**1,092.1**	**596.5**	**1,084.9**	**671.5**	**413.4**
2013					
Moorland Covered Bonds LLP	1,448.8	596.1	1,417.9	628.4	789.6

Assets pledged

Assets are pledged as collateral under repurchase agreements with other banks. These deposits are not available to finance the Consolidated Bank's day to day operations.

	Carrying amount of assets not derecognised	Carrying amount of associated liabilities	Fair value of assets not derecognised	Fair value of associated liabilities	Net position
2014					
Investments securities sold under repurchase agreements	**-**	**-**	**-**	**-**	**-**
2013					
Investments securities sold under repurchase agreements	1,004.4	1,028.3	1,022.5	1,028.3	(5.8)

The Bank has repo transactions of £500m that are secured by its own issued retained securitisation notes which are not recognised on the Balance sheet as it relates to structures for which its assets didn't meet the de-recognition criteria. At the end of 2013 the Bank had a number of gilt repos in place which no longer existed at the end of 2014.

41. Post balance sheet events

It is a requirement of IAS 10 (Events after the balance sheet date) that these financial statements reflect events arising after 31 December 2014. The following events have occurred between 31

December 2014 and 26 March 2015 (the date of approval of these financial statements) and represent ‘non-adjusting’ post balance sheet events:

Migration of IT Infrastructure

On 23 January 2015 the Bank entered into a contract with IBM to migrate its IT infrastructure from The Co-operative Group into IBM managed data centres. The Bank will pay IBM £93m to lead and implement the transition of these services to IBM data centres. The Bank has also entered into a 10 year managed service contract at a total ongoing cost of £275m and has options to terminate throughout the life of the contract.