

Registered Number: R0000733

ULSTER BANK LIMITED

REPORT OF THE DIRECTORS AND FINANCIAL STATEMENTS

31 December 2012

ULSTER BANK LIMITED

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ULSTER BANK LIMITED

BOARD OF DIRECTORS AND SECRETARIES

Directors

S Bell
T Bowen
J Brown
C Campbell
S Dorgan (Chairman)
E Gleeson
N Hamilton
C M Mills
A McLaughlin
P Nolan
D O'Shea
B Rosewell
I Webb

Registered Office

11-16 Donegall Square East
Belfast
BT1 5UB

Secretaries

R Bergin
E Dignam (Deputy secretary)
R Curran (Assistant secretary)

Auditors

Deloitte & Touche
Chartered Accountants & Statutory Audit Firm
Deloitte and Touche House
Earlsfort Terrace
Dublin 2

ULSTER BANK LIMITED

REPORT OF THE DIRECTORS

The directors of Ulster Bank Limited ("the Bank") present their report, together with audited financial statements of the Bank and its subsidiaries (together "the Group") for the year ended 31 December 2012. The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union (EU).

ACTIVITIES AND BUSINESS REVIEW

Principal activities

The Group's principal operating entities are leading retail and commercial banks in Northern Ireland and the Republic of Ireland, operating under the Ulster Bank brand. The Group provides a comprehensive range of financial services through both its Retail Banking division, which provides loan and deposit products through a network of branches and direct channels, and its Corporate Banking division, which provides services to business and corporate customers.

Business review

The Group's performance continues to be impacted by difficult economic conditions in the markets in which it operates (particularly in the Republic of Ireland) and a challenging macroeconomic environment, including continued uncertainty arising from concerns regarding the future economic outlook for the Eurozone. The Group's financial performance reflects this with charges for bad and non performing loans continuing to have a significant negative impact, although to a lesser extent than in previous years. The market for deposits remains competitive and margins continue to be constrained, however the Group has, nonetheless, significantly increased customer deposits in the year to 31 December 2012.

The directors continue to implement a strategy to strengthen its underlying business, support its customers and return the Group to sustainable profitability. In its ambition to become the compelling choice for banking on the island of Ireland, the Group has continued to implement a number of actions to simplify its operating model, to better serve its customers, reduce operating costs across the Group and continue to build on commitments made to its customers through its 'Helpful Banking' campaign.

In June 2012 a significant number of the Group's customers were impacted by The Royal Bank of Scotland Group plc ("RBS Group") technology incident affecting the Bank's transaction batch processing. Throughout the incident the Bank took action to help customers experiencing difficulty by opening branches for longer and increasing the number of staff in locally based call centres. Thereafter the Bank focused on honouring its commitment to put impacted customers back to the position they would have been in had the incident not occurred. Staff, customer redress and other costs associated with the incident amounted to £84m.

Financial performance

The Group's financial performance is presented in the Consolidated Income Statement on page 8.

Net interest income decreased by 17% due to the impact of higher funding costs coupled with a reduction in the loan book and an increase in non-performing loans.

Non-interest income decreased from £446m to £260m, primarily due to the 2011 gain on the buy-back of certain externally issued mortgage securitisation bonds at a discount to par.

Operating expenses increased by 10% on prior year as underlying cost savings were negated by costs of £84m associated with the RBS Group technology incident.

Impairment losses have decreased from £3,718m to £2,340m but remain at a heightened level due to ongoing challenging economic conditions.

At the year end the total assets of the Group were £44,695m (2011: £48,945m).

Risk management

The Group's future performance and results could be materially different from expected results depending on the outcome of certain potential risks and uncertainties.

The major risks associated with the Group's businesses are credit, liquidity, market, regulatory, reputational, operational, conduct and sovereign risk. The Group has established a comprehensive framework for managing these risks, which is continually evolving as the Group's business activities change in response to market, credit, product, regulatory and other developments. The Group is also exposed to risks from its defined benefit pension schemes. The Group's policies for managing each of these risks and its exposure thereto are detailed in Note 23 to the financial statements.

ULSTER BANK LIMITED

REPORT OF THE DIRECTORS (continued)

Accounting policies

The reported results of the Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. Details of the Group's critical accounting policies and key sources of accounting judgements are included in the Accounting policies on pages 21 to 23.

Outlook

The directors acknowledge the challenges of the external market and customer environment. They consider the Group and the Bank to be in a stable financial position and confirm that it has adequate resources, with ongoing support from RBS Group, to continue in business for the foreseeable future. Accordingly they continue to adopt the going concern basis in preparing the financial statements.

Share capital

Details of share capital can be found in Note 20 to the financial statements.

Directors and secretaries

The names of the current members of the Board of Directors are shown on page 1 and brief biographical details are shown on pages 88 to 89. From 1 January 2012 to date the following changes have taken place:

	<u>Appointed</u>	<u>Resigned</u>
<u>Directors</u>		
S Bell	23 March 2012	
D O'Shea	12 November 2012	
R Ryan		26 January 2012
C McManus		17 August 2012
<u>Deputy Secretary</u>		
E Dignam	1 January 2012	

In accordance with the Articles of Association, the directors are not required to retire by rotation.

Directors' indemnities

In terms of Section 236 of the Companies Act 2006, nine directors have been granted Qualifying Third Party Indemnity Provisions by the RBS Group.

Staff involvement

The Group values the input of its employees and actively seeks opportunities to engage with staff at all levels. The annual survey of employee opinions known as Your Feedback provides valuable data to decision makers across the Group in support of improving employee engagement and satisfaction.

Employees across the Group continued to give generously, both financially and through volunteering, to many community and other worthy causes. Such giving is encouraged by the Group through its use of matched funding and staff charity funds which support worthy causes at local, national and international level.

The Group is represented on the European Employee Communication Council which facilitates dialogue amongst employee representatives in the European Economic Area.

Employment of disabled persons

The Group's policy is that disabled persons are considered for employment and subsequent training, career development and promotion based on merit. If members of staff become disabled, it is the Group's policy, wherever possible, to retain them in their existing jobs or to re-deploy them in suitable alternative duties.

Diversity

The attainment of an effective equal opportunities policy is a natural and integral part of good management practice. Key elements of policy are an intention to develop and treat people fairly and create an environment within which staff can develop to their full potential. It is the Group's policy to comply with the relevant provisions of legislation and have regard to Codes of Practice affecting employment practices. Through the Managing Diversity Programme, the Group aims to value and engage individual difference and maximise inclusion to create a positive experience for its people and customers.

ULSTER BANK LIMITED

REPORT OF THE DIRECTORS (continued)

Diversity (continued)

The Group's commitment to diversity underpins its desire to be the financial services provider of choice for customers and to be the employer of choice. The Group will recruit, retain, develop and promote people based solely on merit regardless of their gender, disability, political opinion, race, religious belief or any other characteristics.

Safety, health and wellbeing

The Group recognises that people are key to the success of its business. The Group's vision is for its employees, peers and communities to recognise that the Group's pride and performance in safety, health and wellbeing adds value to them and to the Group's business. Industry leading expertise, innovative tools, products and services and a practical approach to implementation are combined to ensure improved performance continues to be delivered.

During 2012, the Group continued to focus on compliance, governance and managing risk across both jurisdictions in which it operates. Opportunities to improve the efficiency and effectiveness of safety, health and wellbeing management policies and services were monitored and, where relevant, implemented.

Policy and practice on payment of creditors

The Group is committed to maintaining a normal commercial relationship with its suppliers. Consequently, it is the Group's policy to negotiate and agree terms and conditions with its suppliers, which includes the giving of an undertaking to pay suppliers within 30 days of receipt of a correctly prepared invoice submitted in accordance with the terms of the contract or such other payment period as may be agreed.

RBS Group Payables manages the creditors payments process on behalf of various RBS Group entities, including Ulster Bank Group. At 31 December the amount owed to trade creditors by the RBS Group, expressed as a proportion of the amounts invoiced by suppliers during the year then ended, was 25 days (2011: 27 days).

Charitable contributions

During the year the Group made charitable and community investment donations in the United Kingdom and the Republic of Ireland totalling £662,982 (2011: £1,264,983).

Political donations

During the year the Group made no political donations in the UK or the EU (2011: £nil).

Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position, including potential risks and uncertainties, are set out in the Business review on pages 2 and 3.

The financial position of the Group, its cash flows, liquidity position, capital and funding sources are set out in the financial statements. Notes 23 and 24 to the financial statements include the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to market, credit and liquidity risks.

The Group is part of the RBS Group and receives ongoing capital, funding and liquidity resources which, coupled with other sources of funding and liquidity, enable the Group to meet its obligations as they fall due. Other sources of funding and liquidity include retail, wholesale and central bank liquidity facilities.

The directors are satisfied that the Group will continue to receive support from the RBS Group by way of capital, funding and liquidity facilities. After considering the Group's financial outlook and related funding and capital needs, the directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

Investments in Group undertakings

The investments in Group undertakings are shown in Note 12. All of these companies are included in the Group's consolidated financial statements and all have an accounting reference date of 31 December.

Dividends

The directors do not recommend the payment of a dividend on ordinary shares (2011: £nil).

ULSTER BANK LIMITED

REPORT OF THE DIRECTORS (continued)

Post balance sheet events

There have been no significant events between the year end and the date of approval of the financial statements which would require a change or additional disclosure or amendment in the financial statements.

Directors' disclosure to auditors

Each of the directors at the date of approval of this report confirms that:

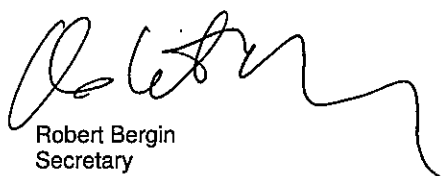
- (a) in so far as the director is aware, there is no relevant audit information of which the Bank's auditors are unaware; and
- (b) the director has taken all steps he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the Bank's auditors are aware of that information.

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

Auditors

The auditors Deloitte & Touche have indicated their willingness to continue in office as auditors.

By order of the Board:



Robert Bergin
Secretary
11-16 Donegall Square East
Belfast
BT1 5UB

22 February 2013

Ulster Bank Limited is registered in Northern Ireland No. R0000733

ULSTER BANK LIMITED

STATEMENT OF DIRECTORS' RESPONSIBILITIES

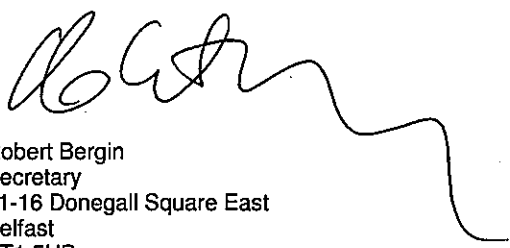
The directors are responsible for preparing the financial statements in accordance with applicable laws and regulation. Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare Group and Bank financial statements in accordance with IFRS as adopted by the EU. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Bank and of the profit or loss for that period. In preparing these financial statements, the directors are required to:

- properly select and apply accounting policies;
- 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 IFRS are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the Group and Bank's ability to continue as a going concern.

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

The directors confirm that these financial statements comply with the aforementioned requirements.

By order of the Board:



Robert Bergin
Secretary
11-16 Donegall Square East
Belfast
BT1 5UB

22 February 2013

Ulster Bank Limited is registered in Northern Ireland No. R0000733

ULSTER BANK LIMITED

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF ULSTER BANK LIMITED

We have audited the financial statements of Ulster Bank Limited for the year ended 31 December 2012 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Group and Bank Balance Sheets, the Group and Bank Statements of Changes in Equity, the Group and Bank Cash Flow Statements, the accounting policies and the related notes 1 to 33. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

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

Respective responsibilities of directors and auditors

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

Scope of the audit of the financial statements

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

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the Bank's affairs as at 31 December 2012 and of the Group's loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the Bank's financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

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

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



Martin Reilly (Senior Statutory Auditor)
for and on behalf of Deloitte & Touche
Chartered Accountants and Statutory Audit Firm
Dublin

22 February 2013

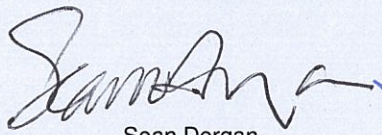
ULSTER BANK LIMITED

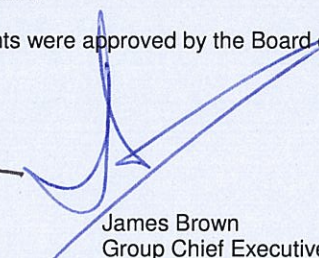
CONSOLIDATED INCOME STATEMENT for the year ended 31 December 2012

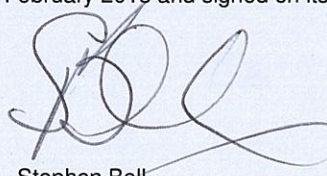
		Group	
	Note	2012	2011
		£m	£m
Interest receivable		1,194	1,478
Interest payable		(499)	(638)
Net interest income	1	695	840
Fees and commission receivable		156	145
Fees and commission payable		(9)	(6)
Income from trading activities		94	42
Other operating income		19	265
Non-interest income	2	260	446
Total income		955	1,286
Operating expenses	3	(706)	(640)
Operating profit before impairment losses		249	646
Impairment loss on loans and advances	9	(2,340)	(3,718)
Operating loss before tax		(2,091)	(3,072)
Tax (charge)/credit	6	(114)	260
Loss for the year		(2,205)	(2,812)
Profit/(loss) attributable to:			
Non-controlling interests		-	8
Ordinary shareholders		(2,205)	(2,820)
		(2,205)	(2,812)

The accompanying accounting policies on pages 13 to 25 and the notes on pages 26 to 87 form an integral part of these financial statements.

The financial statements were approved by the Board of Directors on 22 February 2013 and signed on its behalf by:


Sean Dorgan
Chairman


James Brown
Group Chief Executive


Stephen Bell
Chief Risk Officer

Ulster Bank Limited is registered in Northern Ireland No. R0000733

ULSTER BANK LIMITED

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME for the year ended 31 December 2012

	Group	
	2012	2011
	£m	£m
Loss for the year	(2,205)	(2,812)
Other comprehensive (losses)/income:		
Fair value gains on available-for-sale financial assets	-	2
Exchange differences on translation of foreign operations	(146)	(241)
Actuarial losses on defined benefit plans and other movements	-	(10)
Other comprehensive loss before tax	(146)	(249)
Tax relating to components of other comprehensive losses	-	(1)
Other comprehensive loss after tax	(146)	(250)
Total comprehensive loss for the year	(2,351)	(3,062)
Attributable to:		
Non-controlling interests	(13)	(7)
Ordinary shareholders	(2,338)	(3,055)
	(2,351)	(3,062)

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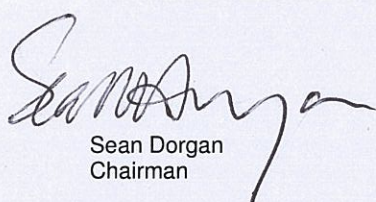
ULSTER BANK LIMITED

BALANCE SHEETS as at 31 December 2012

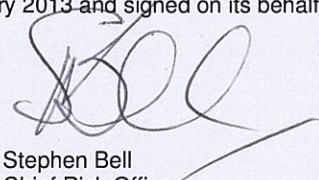
		Group		Bank	
	Note	2012 £m	2011 £m	2012 £m	2011 £m
Assets					
Cash and balances at central banks	8	725	749	545	522
Loans and advances to banks	8	8,190	7,331	7,054	6,757
Loans and advances to customers	8	34,406	38,945	6,020	6,453
Debt securities	8,10	26	98	26	71
Equity shares	8,11	7	5	-	-
Investments in Group undertakings	8,12	-	-	2,544	3,488
Derivatives	8,15	724	997	37	87
Property, plant and equipment	8,14	341	349	64	81
Prepayments, accrued income and other assets	8,16	123	155	87	149
Retirement benefit assets	4,8	82	31	55	23
Deferred taxation	8,18	71	285	2	1
Total assets		44,695	48,945	16,434	17,632
Liabilities					
Deposits by banks	8	7,895	12,830	4,540	4,365
Customer accounts	8	23,070	22,348	7,154	7,487
Debt securities in issue	8	3,254	3,530	2	38
Derivatives	8,15	992	1,352	78	84
Accruals, deferred income and other liabilities	8,17	910	871	668	639
Deferred taxation	8,18	23	18	20	15
Subordinated liabilities	8,19	1,157	1,183	939	961
Total liabilities		37,301	42,132	13,401	13,589
Equity					
Non-controlling interests		500	512	-	-
Shareholders' equity:					
Called up share capital	20	1,505	1,505	1,505	1,505
Reserves		5,389	4,796	1,528	2,538
Total equity	8	7,394	6,813	3,033	4,043
Total liabilities and equity		44,695	48,945	16,434	17,632

The accompanying accounting policies on pages 13 to 25 and the notes on pages 26 to 87 form an integral part of these financial statements.

The financial statements were approved by the Board of Directors on 22 February 2013 and signed on its behalf by:


Sean Dorgan
Chairman


James Brown
Group Chief Executive


Stephen Bell
Chief Risk Officer

Ulster Bank Limited is registered in Northern Ireland No. R0000733

ULSTER BANK LIMITED

STATEMENTS OF CHANGES IN EQUITY for the year ended 31 December 2012

	Group		Bank	
	2012	2011	2012	2011
	£m	£m	£m	£m
Called up share capital				
At 1 January and 31 December	1,505	1,505	1,505	1,505
Share premium account				
At 1 January and 31 December	907	907	907	907
Available-for-sale reserve				
At 1 January	-	(1)	-	(5)
Unrealised gains/(losses) in the year	1	(2)	1	1
Realised losses in the year	(1)	-	-	-
Exchange gains in the year	-	4	-	5
Taxation	-	(1)	(1)	(1)
At 31 December	-	-	-	-
Foreign exchange reserve				
At 1 January	(36)	190	(260)	(260)
Retranslation of net assets	(133)	(226)	-	-
At 31 December	(169)	(36)	(260)	(260)
Retained earnings				
At 1 January	(6,651)	(3,821)	(8,685)	(4,684)
Actuarial losses on defined benefit plans and other movements	-	(10)	-	(2)
Loss attributable to ordinary shareholders	(2,205)	(2,820)	(3,941)	(3,999)
At 31 December	(8,856)	(6,651)	(12,626)	(8,685)
Capital contribution				
At 1 January	10,576	5,918	10,576	5,918
Capital contribution	2,931	4,658	2,931	4,658
At 31 December	13,507	10,576	13,507	10,576
Shareholders' equity at 31 December	6,894	6,301	3,033	4,043
Non-controlling interests				
At 1 January	512	558	-	-
Increase/(decrease) in loan classed as equity	1	(39)	-	-
Currency translation and other adjustments	(13)	(15)	-	-
Gain attributable to non-controlling interests	-	8	-	-
At 31 December	500	512	-	-
Total equity at 31 December	7,394	6,813	3,033	4,043
Total comprehensive loss recognised in the Statement of Changes in Equity is attributable as follows:				
Non-controlling interests	(13)	(7)	-	-
Ordinary shareholders	(2,338)	(3,055)	(3,941)	(3,997)
	(2,351)	(3,062)	(3,941)	(3,997)

The accompanying accounting policies on pages 13 to 25 and the notes on pages 26 to 87 form an integral part of these financial statements.

ULSTER BANK LIMITED

CASH FLOW STATEMENTS for the year ended 31 December 2012

		Group		Bank	
	Note	2012 £m	2011 £m	2012 £m	2011 £m
Operating activities					
Operating loss before tax		(2,091)	(3,072)	(4,032)	(4,165)
Adjustments for:					
Depreciation, amortisation and impairment		43	30	17	10
Interest on subordinated liabilities		27	34	13	19
Charge for defined benefit pension schemes		26	27	7	6
Cash contribution to defined benefit pension schemes		(77)	(75)	(40)	(39)
Loan impairment provisions net of recoveries		2,128	3,544	256	737
Impairment of investments in Group undertakings		-	-	3,663	3,518
Elimination of foreign exchange differences		(194)	(411)	(9)	(7)
Other non-cash items		(244)	(295)	(33)	(51)
Net cash flows from trading activities	26	(382)	(218)	(158)	28
Changes in operating assets and liabilities		(1,764)	(3,228)	211	(2,076)
Net cash flows from operating activities before tax		(2,146)	(3,446)	53	(2,048)
Income taxes received		124	182	155	137
Net cash flows from operating activities	26	(2,022)	(3,264)	208	(1,911)
Investing activities					
Sale and maturity of securities		73	281	47	128
Purchase of equity shares		(2)	(3)	-	-
Sale of equity shares		-	1	-	-
Purchase of property, plant and equipment		(11)	(60)	(2)	(1)
Sale of property, plant and equipment		3	8	2	-
Investment in subsidiary undertakings		-	-	(2,730)	(4,068)
Net cash flows from investing activities		63	227	(2,683)	(3,941)
Financing activities					
Capital contribution		2,931	4,658	2,931	4,658
Interest on subordinated liabilities		(27)	(34)	(13)	(19)
Net cash flows from financing activities		2,904	4,624	2,918	4,639
Effect of exchange rate changes on cash and cash equivalents		(117)	(70)	(2)	-
Net increase/(decrease) in cash and cash equivalents		828	1,517	441	(1,213)
Cash and cash equivalents 1 January	29	5,697	4,180	2,963	4,176
Cash and cash equivalents 31 December	29	6,525	5,697	3,404	2,963

The accompanying accounting policies on pages 13 to 25 and the notes on pages 26 to 87 form an integral part of these financial statements.

ULSTER BANK LIMITED

ACCOUNTING POLICIES

1. Presentation of financial statements

The consolidated financial statements are prepared on a going concern basis and in accordance with IFRS issued by the International Accounting Standards Board (IASB), and interpretations issued by the International Financial Reporting Interpretations Committee of the IASB as adopted by the EU. The Group and Bank's financial statements are presented in accordance with the Companies Act 2006.

The Bank is incorporated and registered in Northern Ireland. The Group and Bank's financial statements are prepared on the historical cost basis except that the following assets and liabilities are stated at their fair value: derivative financial instruments, held-for-trading financial assets and financial liabilities, financial assets and financial liabilities that are designated at fair value through profit or loss, available-for-sale financial assets and investment property. Recognised financial assets and financial liabilities in fair value hedges are adjusted for changes in fair value in respect of the risk that is hedged.

2. Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank (Ulster Bank Limited) and entities (including certain special purpose entities) that are controlled by the Bank (its subsidiaries). Control exists where the Group has the power to govern the financial and operating policies of the entity so as to obtain benefit from its activities; generally conferred by holding a majority of voting rights.

On acquisition of a subsidiary, its identifiable assets, liabilities and contingent liabilities are included in the consolidated financial statements at their fair value. Any excess of the cost (the fair value of assets given, liabilities incurred or assumed and equity instruments issued by the Group plus any directly attributable costs) of an acquisition over the fair value of the net assets acquired is recognised as goodwill. The interest of non-controlling shareholders is stated at their share of the fair value of the subsidiary's net assets.

The results of subsidiaries acquired are included in the consolidated income statement from the date control passes until the Group ceases to control them through a sale or significant change in circumstances. Changes in interest that do not result in a loss of control are recognised in equity. Total comprehensive income of subsidiaries is attributed to the owners of the Group and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

All intra-group balances, transactions, income and expenses are eliminated on consolidation. The consolidated financial statements are prepared using uniform accounting policies.

3. Revenue recognition

Interest income on financial assets that are classified as loans and receivables, available-for-sale or held-to-maturity and interest expense on financial liabilities other than those at fair value through profit or loss is determined using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial asset or financial liability (or group of financial assets or liabilities) and of allocating the interest income or interest expense over the expected life of the asset or liability. The effective interest rate is the rate that exactly discounts estimated future cash flows to the instrument's initial carrying amount. Calculation of the effective interest rate takes into account fees payable or receivable, that are an integral part of the instrument's yield, premiums or discounts on acquisition or issue, early redemption fees and transaction costs. All contractual terms of a financial instrument are considered when estimating future cash flows.

Financial assets and financial liabilities held-for-trading or designated as at fair value through profit or loss are recorded at fair value. Changes in fair value are recognised through profit or loss together with dividends and interest receivable and payable.

Commitment and utilisation fees are determined as a percentage of the outstanding facility. If it is unlikely that a specific lending arrangement will be entered into, such fees are taken through profit or loss over the life of the facility otherwise they are deferred and included in the effective interest rate on the advance.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

3. Revenue recognition (continued)

Fees in respect of services are recognised as the right to consideration accrues through the provision of the service to the customer. The arrangements are generally contractual and the cost of providing the service is incurred as the service is rendered. The price is usually fixed and always determinable. The application of this policy to significant fee types is outlined below.

Payment services: this income comprises income received for payment services including cheques cashed and direct debits. These are generally charged on a per transaction basis. The income is earned when the payment or transaction occurs. Charges for payment services are usually debited to the customer's account, monthly or quarterly in arrears. Income is accrued at period end for services provided but not charged.

Card related services: fees from credit card business include:

- Commission received from retailers for processing credit and debit card transactions: income is accrued to the income statement as the service is performed;
- Interchange received: as issuer, the Group receives a fee (interchange) each time a cardholder purchases goods and services. The Group also receives interchange fees from other card issuers for providing cash advances through its branch and automated teller machine networks. These fees are accrued once the transaction has taken place; and
- Annual fees payable by credit card holders: these are deferred and taken to profit or loss over the period of the service i.e. 12 months.

Insurance brokerage: this is made up of fees and commissions received from the agency sale of insurance. Commission on the sale of an insurance contract is earned at the inception of the policy as the insurance has been arranged and placed. However, provision is made where commission is refundable in the event of policy cancellation in line with estimated cancellations.

Investment management fees: fees charged for managing investments are recognised as revenue as the services are provided. Incremental costs that are directly attributable to securing an investment management contract are deferred and charged as an expense as the related revenue is recognised.

Fees and commissions payable: Fees and commissions are payable in respect of services provided by third party intermediaries. These are charged through profit or loss over the life of the underlying product.

4. Pensions and other post-retirement benefits

The Group provides post-retirement benefits in the form of pensions to eligible employees.

For defined benefit schemes, scheme liabilities are measured on an actuarial basis using the projected unit credit method and discounted at a rate that reflects the current rate of return on a high quality corporate bond of equivalent term and currency to the scheme liabilities. Scheme assets are measured at their fair value. Cumulative actuarial gains or losses that exceed 10 percent of the greater of the assets or the obligations of the scheme are amortised to the statement of comprehensive income over the expected average remaining lives of participating employees. Past service costs are recognised immediately to the extent that benefits have vested; otherwise they are amortised over the period until the benefits become vested.

Any surplus or deficit of scheme assets over liabilities adjusted for unrecognised actuarial gains and losses and past service costs is recognised in the balance sheet as an asset (surplus) or liability (deficit).

Contributions to defined contribution pension schemes are recognised in the income statement when payable.

5. Intangible assets and goodwill

Intangible assets that are acquired by the Group are stated at cost less accumulated amortisation and accumulated impairment losses. The intangible assets of the Group and Bank are fully impaired.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

6. Property, plant and equipment

Items of property, plant and equipment (except investment properties – see accounting policy 8) are stated at cost less accumulated depreciation (see below) and accumulated impairment losses. Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for separately.

Depreciation is charged to profit or loss on a straight-line basis so as to write off the depreciable amount of property, plant and equipment (including assets owned and let on operating leases) over their estimated useful lives. The depreciable amount is the cost of an asset less its residual value. Land is not depreciated. Estimated useful lives are as follows:

Freehold and long leasehold buildings	50 years
Short leaseholds	unexpired period of the lease
Property adaptation costs	10 to 15 years
Computer equipment	up to 5 years
Other equipment	4 to 15 years

The residual value and useful life of property, plant and equipment are reviewed at each balance sheet date and updated for any changes.

7. Impairment of property, plant and equipment

At each reporting date, the Group assesses whether there is any indication that the value of its property, plant and equipment is impaired. If any such indication exists, the Group estimates the recoverable amount of the asset and the impairment loss, if any. If an asset does not generate cash flows that are independent from those of other assets or groups of assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. The recoverable amount of an asset is the higher of its fair value less cost to sell and its value in use. Value in use is the present value of future cash flows from the asset or cash-generating unit discounted at a rate that reflects market interest rates adjusted for risks specific to the asset or cash-generating unit that have not been reflected in the estimation of future cash flows. If the recoverable amount of a tangible asset is less than its carrying value, an impairment loss is recognised immediately in profit or loss and the carrying value of the asset reduced by the amount of the loss. A reversal of an impairment loss on property, plant and equipment is recognised as it arises provided the increased carrying value does not exceed that which it would have been had no impairment loss been recognised.

8. Investment properties

Investment property, which is property held to earn rentals and/or for capital appreciation (including property under construction for such purposes), is measured initially at its cost, including transaction costs. Subsequent to initial recognition, investment property is measured at fair value. Fair value is based on current prices for similar properties in the same location and condition using internal valuation models based on yield comparables and any available recent market transactions taking cognisance of the principles of the Royal Institute of Chartered Surveyors (RICS) valuation methodology.

Fair value of the investment properties is determined on at least an annual basis by officers of the Group. A selection of properties may be valued by external appointed surveyors from time to time as the commercial need arises. Gains and losses arising from changes in the fair value of investment property are included in profit or loss in the period in which they arise.

Rental income from investment property is recognised on a straight line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income.

9. Foreign currencies

The Group's consolidated financial statements are presented in Sterling, which is the functional currency of the Bank.

Transactions in foreign currencies are translated into Sterling at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into Sterling at the rates of exchange ruling at the balance sheet date. Foreign exchange differences arising on translation are reported in income from trading activities except for differences arising on cash flow hedges and hedges of net investments in foreign operations. Non-monetary items denominated in foreign currencies that are stated at fair value are translated into Sterling at foreign exchange rates ruling at the dates the values were determined. Translation differences arising on non-monetary items measured at fair value are recognised in profit or loss except for differences arising on available-for-sale non-monetary financial assets, for example equity shares, which are included in the available-for-sale reserve in equity unless the asset is the hedged item in a fair value hedge.

Assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated into Sterling at foreign exchange rates ruling at the balance sheet date. Income and expenses of foreign operations are translated into Sterling at average exchange rates unless these do not approximate to the foreign exchange rates ruling at the dates of the transactions. Foreign exchange differences arising on translation of foreign operations are recognised directly in equity and included in profit or loss on its disposal.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

10. Leases

As lessor

Contracts with customers to lease assets are classified as finance leases if they transfer substantially all the risks and rewards of ownership of the asset to the customer. All other contracts with customers to lease assets are classified as operating leases.

Finance lease are included in the balance sheet, within Loans and advances to banks and Loans and advances to customers, at the amount of the net investment in the lease being the minimum lease payments and any unguaranteed residual value discounted at the interest rate implicit in the lease. Finance lease income is allocated to accounting periods so as to give a constant periodic rate of return before tax on the net investment and included in interest receivable. Unguaranteed residual values are subject to regular review; If there is a reduction in their value, income allocation is revised and any reduction in respect of amounts accrued is recognised immediately.

Rental income from operating leases is credited to the income statement on a receivable basis over the term of the lease. Operating lease assets are included within property, plant and equipment and depreciated over their useful lives (see accounting policy 6). Operating lease rentals receivable are included in other operating income.

As lessee

Rentals payable under operating leases are charged to the income statement on a straight-line basis over the term of the relevant lease.

11. Provisions and contingent liabilities

The Group recognises a provision for a present obligation resulting from a past event when it is more likely than not that it will be required to transfer economic benefits to settle the obligation and the amount of the obligation can be estimated reliably.

Provision is made for restructuring costs, including the costs of redundancy, when the Group has a constructive obligation to restructure. An obligation exists when the Group has a detailed formal plan for the restructuring and has raised a valid expectation in those affected by starting to implement the plan or announcing its main features.

If the Group has a contract that is onerous, it recognises the present obligation under the contract as a provision. An onerous contract is one where the unavoidable costs of meeting the obligations under it exceed the expected economic benefits. When the Group vacates a leasehold property, a provision is recognised for the costs under the lease less any expected economic benefits (such as rental income).

Contingent liabilities are possible obligations arising from past events whose existence will be confirmed only by uncertain future events or present obligations arising from past events that are not recognised because either an outflow of economic benefits is not probable or the amount of the obligation cannot be reliably measured. Contingent liabilities are not recognised but information about them is disclosed unless the possibility of any outflow of economic benefits in settlement is remote.

12. Taxation

Income tax expense or income, comprising current tax and deferred tax, is recorded in the income statement except income tax on items recognised outside profit or loss which is credited or charged to other comprehensive income or to equity as appropriate.

Current tax is income tax payable or recoverable in respect of the taxable profit or loss for the year arising in income or in equity. Provision is made for current tax at rates enacted or substantively enacted at the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable in respect of temporary differences between the carrying amount of an asset or liability for accounting purposes and its carrying amount for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that they will be recovered. Deferred tax is calculated using tax rates expected to apply in the periods when the assets will be realised or the liabilities settled, based on tax rates and laws enacted, or substantively enacted, at the balance sheet date.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

13. Financial assets

On initial recognition financial assets are classified into held-to-maturity investments; available-for-sale financial assets; held-for-trading; designated as at fair value through profit or loss; or loans and receivables.

Held-to-maturity investments - a financial asset may be classified as a held-to-maturity investment only if it has fixed or determinable payments, a fixed maturity and the Group has the positive intention and ability to hold to maturity. Held-to-maturity investments are initially recognised at fair value plus directly related transaction costs. They are subsequently measured at amortised cost using the effective interest method (see accounting policy 3) less any impairment losses.

Held-for-trading - a financial asset is classified as held-for-trading if it is acquired principally for sale in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative (not in a qualifying hedge relationship). Held-for-trading financial assets are recognised at fair value with transaction costs being recognised in profit or loss. Subsequently they are measured at fair value. Gains and losses on held-for-trading financial assets are recognised in profit or loss as they arise.

Designated as at fair value through profit or loss - financial assets may be designated as at fair value through profit or loss only if such designation: (a) eliminates or significantly reduces a measurement or recognition inconsistency; or (b) applies to a group of financial assets, financial liabilities or both, that the Group manages and evaluates on a fair value basis; or (c) relates to an instrument that contains an embedded derivative which is not evidently closely related to the host contract.

Financial assets that the Group designates on initial recognition as being at fair value through profit or loss are recognised at fair value, with transaction costs being recognised in profit or loss and are subsequently measured at fair value. Gains and losses on financial assets that are designated as at fair value through profit or loss are recognised in profit or loss as they arise.

The Group has designated financial assets as at fair value through profit or loss principally where the assets are economically hedged by derivatives and fair value designation eliminates the measurement inconsistency that would arise if the assets were carried at amortised cost or classified as available-for-sale.

Loans and receivables - non-derivative financial assets with fixed or determinable repayments that are not quoted in an active market are classified as loans and receivables, except those that are classified as available-for-sale or as held-for-trading, or designated as at fair value through profit or loss. Loans and receivables are initially recognised at fair value plus directly related transaction costs. They are subsequently measured at amortised cost using the effective interest method (see accounting policy 3) less any impairment losses.

Available-for-sale - financial assets that are not classified as held-to-maturity; held-for-trading; designated as at fair value through profit or loss; or loans and receivables are classified as available-for-sale. Financial assets can be designated as available-for-sale on initial recognition. Available-for-sale financial assets are initially recognised at fair value plus directly related transaction costs. They are subsequently measured at fair value. Unquoted equity investments whose fair value cannot be measured reliably are carried at cost and classified as available-for-sale financial assets. Impairment losses and exchange differences resulting from retranslating the amortised cost of monetary available-for-sale financial assets denominated in a foreign currency are recognised in profit or loss together with interest calculated using the effective interest method (see accounting policy 3). Other changes in the fair value of available-for-sale financial assets and any related tax are reported in a separate component of shareholders' equity until disposal, when the cumulative gain or loss is recognised in profit or loss.

Regular way purchases of financial assets classified as loans and receivables are recognised on settlement date; all other regular way purchases are recognised on trade date.

Fair value for a net open position in a financial asset that is quoted in an active market is the current bid price times the number of units of the instrument held. Fair values for financial assets not quoted in an active market are determined using appropriate valuation techniques including discounting future cash flows, option pricing models and other methods that are consistent with accepted economic methodologies for pricing financial assets.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

14. Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or group of financial assets classified as held-to-maturity, available-for-sale or loans and receivables is impaired. A financial asset or portfolio of financial assets is impaired and an impairment loss incurred if there is objective evidence that an event or events since initial recognition of the asset have adversely affected the amount or timing of future cash flows from the asset.

Financial assets carried at amortised cost - if there is objective evidence that an impairment loss on a financial asset or group of financial assets classified as loans and receivables or as held-to-maturity investments has been incurred, the Group measures the amount of the loss as the difference between the carrying amount of the asset or group of assets and the present value of estimated future cash flows from the asset or group of assets discounted at the original effective interest rate of the instrument at initial recognition. For collateralised loans and receivables, estimated future cash flows include cash flows that may result from foreclosure less the costs of obtaining and selling the collateral, whether or not foreclosure is probable.

Where, in the course of the orderly realisation of a loan it is exchanged for equity shares or properties, the exchange is accounted for as the sale of the loan and the acquisition of equity securities or investment properties. Where the Group's interest in equity shares following the exchange is such that the Group controls an entity, that entity is consolidated.

Impairment losses are assessed individually for financial assets that are individually significant and individually or collectively for assets that are not individually significant. In making collective assessment of impairment, financial assets are grouped into portfolios on the basis of similar risk characteristics. Future cash flows from these portfolios are estimated on the basis of the contractual cash flows and historical loss experience for assets with similar credit risk characteristics. Historical loss experience is adjusted, on the basis of current observable data, to reflect current conditions not affecting the period of historical experience.

Impairment losses are recognised in profit or loss and the carrying amount of the financial asset or group of financial assets reduced by establishing an allowance for impairment losses. If, in a subsequent period, the amount of the impairment loss reduces and the reduction can be ascribed to an event after the impairment was recognised, the previously recognised loss is reversed by adjusting the allowance. Once an impairment loss has been recognised on a financial asset or group of financial assets, interest income is recognised on the carrying amount using the original effective rate of interest at which estimated future cash flows were discounted in measuring impairment.

Impaired loans and receivables are written off, i.e. the impairment provision is applied in writing down the loan's carrying value partially or in full, when the Group concludes that there is no longer any realistic prospect of recovery of part or all of the loan. For portfolios that are collectively assessed for impairment, the timing of write off principally reflects historic recovery experience for each portfolio. For loans that are individually assessed for impairment, the timing of write off is determined on a case-by-case basis. Such loans are reviewed regularly and write offs will be prompted by bankruptcy, insolvency, restructuring and similar events. Amounts recovered after a loan has been written off are credited to the loan impairment charge for the period in which they are received.

Financial assets carried at fair value - when a decline in the fair value of a financial asset classified as available-for-sale has been recognised directly in equity and there is objective evidence that the asset is impaired, the cumulative loss is removed from equity and recognised in profit or loss. The loss is measured as the difference between the acquisition cost of the financial asset and its current fair value. Impairment losses on available-for-sale equity instruments are not reversed through profit or loss, but those on available-for-sale debt instruments are reversed, if there is an increase in fair value that is objectively related to a subsequent event.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

15. Financial liabilities

On initial recognition financial liabilities are classified into held-for-trading; designated as at fair value through profit or loss; or amortised cost.

Held-for-trading - a financial liability is classified as held-for-trading if it is incurred principally for the repurchase in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative (not in a qualifying hedge relationship). Held-for-trading financial liabilities are recognised at fair value with transaction costs being recognised in profit or loss. Subsequently they are measured at fair value. Gains and losses are recognised in profit or loss as they arise.

Designated as at fair value through profit or loss - financial liabilities may be designated as at fair value through profit or loss only if such designation (a) eliminates or significantly reduces a measurement or recognition inconsistency; or (b) applies to a group of financial assets, financial liabilities or both that the Group manages and evaluates on a fair value basis; or (c) relates to an instrument that contains an embedded derivative which is not evidently closely related to the host contract.

Financial liabilities that the Group designates on initial recognition as being at fair value through profit or loss are recognised at fair value, with transaction costs being recognised in profit or loss, and are subsequently measured at fair value. Gains and losses on financial liabilities that are designated as at fair value through profit or loss are recognised in profit or loss as they arise.

The principal category of financial liabilities designated as at fair value through profit or loss is structured liabilities issued by the Group: designation significantly reduces the measurement inconsistency between these liabilities and the related derivatives carried at fair value.

Amortised cost - all other financial liabilities are measured at amortised cost using the effective interest method (see accounting policy 3).

Fair value for a net open position in a financial liability that is quoted in an active market is the current offer price times the number of units of the instrument held or issued. Fair values for financial liabilities not quoted in an active market are determined using appropriate valuation techniques including discounting future cash flows, option pricing models and other methods that are consistent with accepted economic methodologies for pricing financial liabilities. Credit valuation adjustments are made when valuing financial liabilities to reflect the Group's own credit standing.

16. Derecognition

A financial asset is derecognised when it has been transferred and the transfer qualifies for derecognition. A transfer requires that the Group either: (a) transfers the contractual rights to receive the asset's cash flows; or (b) retains the rights to the asset's cash flows but assumes a contractual obligation to pay those cash flows to a third party. After a transfer, the Group assesses the extent to which it has retained the risks and rewards of ownership of the transferred asset. If substantially all the risks and rewards have been retained, the asset remains on the balance sheet. If substantially all of the risks and rewards have been transferred, the asset is derecognised. If substantially all the risks and rewards have been neither retained nor transferred, the Group assess whether or not it has retained control of the asset. If it has not retained control, the asset is derecognised. Where the Group has retained control of the asset, it continues to recognise the asset to the extent of its continuing involvement.

A financial liability is removed from the balance sheet when the obligation is discharged, or cancelled, or expires. On the redemption or settlement of debt securities (including subordinated liabilities) issued by the Group, the Group derecognises the debt instrument and records a gain or loss being the difference between the debt's carrying amount and the cost of redemption or settlement. The same treatment applies where the debt is exchanged for a new debt issue that has terms substantially different from those of the existing debt. The assessment of whether the terms of the new debt instrument are substantially different takes into account qualitative and quantitative characteristics including a comparison of the discounted present value of the cash flows under the new terms with the discounted present value of the remaining cash flows of the original debt issue.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

17. Sale and repurchase transactions

Securities subject to a sale and repurchase agreement under which substantially all the risks and rewards of ownership are retained by the Group continue to be shown on the balance sheet and the sale proceeds recorded as a deposit. Securities acquired in reverse sale and repurchase transactions under which the Group is not exposed to substantially all the risks and rewards of ownership are not recognised on the balance sheet and the consideration is recorded in Loans and advances to banks or Loans and advances to customers as appropriate.

Securities borrowing and lending transactions are usually secured by cash or securities advanced by the borrower. Borrowed securities are not recognised on the balance sheet or lent securities derecognised. Cash collateral received or given is treated as a loan or deposit; collateral in the form of securities is not recognised. However, where securities borrowed are transferred to third parties, a liability for the obligation to return the securities to the stock lending counterparty is recorded.

18. Netting

Financial assets and financial liabilities are offset and the net amount presented in the balance sheet when, and only when, the Group has a legally enforceable right to set off the recognised amounts; and it intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously. The Group is party to a number of arrangements, including master netting agreements that give it the right to offset financial assets and financial liabilities. Where it does not intend to settle the amounts net or simultaneously the assets and liabilities concerned are presented gross.

19. Capital instruments

The Group classifies a financial instrument that it issues as a financial asset, financial liability or an equity instrument in accordance with the substance of the contractual arrangement. An instrument is classified as a liability if it is a contractual obligation to deliver cash or another financial asset, or to exchange financial assets or financial liabilities on potentially unfavourable terms. An instrument is classified as equity if it evidences a residual interest in the assets of the Group after the deduction of liabilities. The components of a compound financial instrument issued by the Group are classified and accounted for separately as financial assets, financial liabilities or equity as appropriate.

20. Derivatives and hedging

Derivative financial instruments are initially recognised, and subsequently measured, at fair value. Derivative fair values are determined from quoted prices in active markets where available. Where there is no active market for an instrument, fair value is derived from prices for the derivative's components using appropriate pricing or valuation models. Credit valuation adjustments are made when valuing derivative financial assets to incorporate counterparty credit risk. Adjustments are also made when valuing financial liabilities to reflect the Group's own credit standing.

A derivative embedded in a contract is accounted for as a stand-alone derivative if its economic characteristics are not closely related to the economic characteristics of the host contract; unless the entire contract is carried at fair value through profit or loss.

Gains and losses arising from changes in fair value of a derivative are recognised as they arise in non-interest income within profit or loss.

21. Share-based payments

The RBS Group awards options over shares to its employees under various share option schemes. IFRS 2 'Share-based Payment' is applied by the RBS Group to grants made under these schemes after 7 November 2002 that had not vested on 1 January 2010. The RBS Group recognises an expense for these transactions with its employees based on the fair value on the date the options are granted. It includes the cost of these awards in determining any recharges of employee costs it makes to subsidiaries in the Group.

22. Cash and cash equivalents

In the cash flow statement, cash and cash equivalents comprise cash and demand deposits with banks together with short-term highly liquid investments that are readily convertible to known amounts of cash and subject to insignificant risk of change in value.

23. Shares in Group entities

The Bank's investments in its subsidiaries are stated at cost less any accumulated impairment losses.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

Critical accounting policies and key sources of accounting judgements

The reported results of the Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. UK company law and IFRS require the directors, in preparing the Group's financial statements, to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent. In the absence of an applicable standard or interpretation, International Accounting Standard ("IAS") 8 'Accounting Policies, Changes in Accounting Estimates and Errors', requires management to develop and apply an accounting policy that results in relevant and reliable information in light of the requirements and guidance in IFRS dealing with similar and related issues and the IASB's Framework for the Preparation and Presentation of financial statements.

The judgements and assumptions involved in the Group's accounting policies that are considered by the Board to be the most important to the portrayal of its financial condition are discussed below. The use of estimates, assumptions or models that differ from those adopted by the Group would affect its reported results.

Loan impairment provisions

The Group's loan impairment provisions are established to recognise incurred impairment losses in its portfolio of loans classified as loans and receivables and carried at amortised cost. A loan is impaired when there is objective evidence that events since the loan was granted have affected expected cash flows from the loan. The impairment loss is the difference between the carrying value of the loan and the present value of estimated future cash flows at the loan's original effective interest rate.

At 31 December 2012, gross loans and advances to customers totalled £45,180m (2011: £47,996m) and customer loan impairment provisions amounted to £10,774m (2011: £9,051m).

There are three components to the Group's loan impairment provisions: individual, collective and latent.

Individual component - all impaired loans that exceed specific thresholds are individually assessed for impairment. Individually assessed loans principally comprise the Group's portfolio of commercial loans to medium and large businesses. Impairment losses are recognised as the difference between the carrying value of the loan and the discounted value of management's best estimate of future cash repayments and proceeds from any security held. These estimates take into account the customer's debt capacity and financial flexibility; the level and quality of its earnings; the amount and sources of cash flows; the industry in which the counterparty operates; and the realisable value of any security held. Estimating the quantum and timing of future recoveries involves significant judgement. The size of receipts will depend on the future performance of the borrower and the value of security, both of which will be affected by future economic conditions; additionally, collateral may not be readily marketable. The actual amount of future cash flows and the date they are received may differ from these estimates and consequently actual losses incurred may differ from those recognised in these financial statements.

Collective component - impaired loans that are below individual assessment thresholds are collectively assessed. Collectively assessed provisions are established on a portfolio basis using a present value methodology taking into account the level of arrears, security, past loss experience, credit scores and defaults based on portfolio trends. The most significant factors in establishing these provisions are the expected loss rates and the related average life. These portfolios include smaller commercial loans, credit card receivables and other personal advances including mortgages. The future credit quality of these portfolios is subject to uncertainties that could cause actual credit losses to differ materially from reported loan impairment provisions. These uncertainties include the economic environment, notably interest rates and their effect on customer spending, the unemployment level, payment behaviour and bankruptcy trends.

Latent component - this consists of loan losses that have been incurred but have not been separately identified at the balance sheet date. Latent loss provisions are held against estimated impairment losses in the performing portfolio that have yet to be identified as at the balance sheet date. To assess that latent loss within its portfolios, the Group has developed methodologies to estimate the time that an asset can remain impaired within a performing portfolio before it is identified and reported as such.

Forbearance

The forbearance policies are the main response to managing mortgage customers in financial difficulty and are deployed through the Group's forbearance initiative. Forbearance is applied to secured retail products where temporary relief is offered through the renegotiation of the original contract, although on terms not generally available on a commercial basis. This may include offering contract revision by various means including reduced repayment, interest only arrangements, negative amortisation, payment moratorium, term extension, lifetime reduced repayment and/or interest rate reduction; these forbearance arrangements are subject to heightened monitoring.

Forbearance offered by the Group on loans where an impairment loss provision has been previously recognised will result in such loans retaining their classification as non-performing. Where the customer met the loan terms prior to modification and there is a realistic expectation that the customer will adhere to forbearance terms, these loans are classified as performing loans. In recognising their credit risk profile, they carry a provision incorporating an expectation that some customers will fail to comply with the terms of the forbearance together with the associated loss rate.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

Critical accounting policies and key sources of accounting judgements (continued)

Impairment of investment in Group undertakings

The fair value of investments in Group undertakings is calculated using a model based on expected future profits plus future equity requirements. The net equity flows are discounted relative to the number of years from the current year. A discounted terminal value is added to the discounted expected future profits to provide the fair value of the subsidiary. If the fair value of the subsidiary is less than its carrying value, an impairment loss is recognised immediately in profit or loss and the carrying value of the asset reduced by the amount of the loss.

Valuation of investment property

Investment property, which is property held to earn rentals and/or for capital appreciation (including property under construction for such purposes), is measured initially at its cost, including transaction costs. Subsequent to initial recognition, investment property is measured at fair value. Fair value is based on current prices for similar properties in the same location and condition using internal valuation models based on yield comparables and any available recent market transactions taking cognisance of the principles of the Royal Institute of Chartered Surveyors (RICS) valuation methodology.

Fair value of the investment properties is determined on at least an annual basis by officers of the Group. A selection of properties may be valued by external appointed surveyors from time to time as the commercial need arises. Gains and losses arising from changes in the fair value of investment property are included in profit or loss in the period in which they arise.

Deferred tax

The Group makes provision for deferred tax on short-term and other temporary differences where tax recognition occurs at a different time from accounting recognition. Deferred tax assets of £71m were recognised as at 31 December 2012 (2011: £285m). Deferred tax assets of £886m (2011: £494m) have not been recognised in respect of tax losses carried forward where doubt exists over the availability of future taxable profits.

The Group has recognised deferred tax assets in respect of losses and short-term timing differences. Deferred tax assets are recognised in respect of unused tax losses to the extent that it is probable that there will be future taxable profits against which the losses can be utilised. Business projections prepared for impairment reviews indicate that sufficient future taxable income will be available against which to offset these recognised deferred tax assets within 7 years (2011: 7 years). The Group's cumulative losses are principally attributable to the recent unparalleled market conditions.

Pensions

There are three defined benefit pension schemes in operation within the Group: Ulster Bank Pension Scheme, Ulster Bank Pension Scheme (Republic of Ireland) and First Active Pension Scheme. The assets of defined benefit schemes are measured at their fair value at the balance sheet date. Scheme liabilities are measured using the projected unit method, which takes account of projected earnings increases, using actuarial assumptions that give the best estimate of the future cash flows that will arise under the scheme liabilities. These cash flows are discounted at an interest rate based on the yields of high-quality corporate bonds of appropriate duration, with high-quality almost universally understood to mean AA-rated. The choice of discount rate is a source of estimation uncertainty, due to a lack of appropriate Euro-denominated AA-rated bonds of equivalent duration to the pension schemes' liabilities.

The approach used is to fit a yield curve to an appropriate dataset of AA bonds, and derive the discount rate from that curve. To increase the number of reference bonds available at the end of the reporting period, equivalent AA yields were extrapolated for longer dated A and AAA rated bonds by applying a credit spread adjustment to their actual yields. These were then included in the dataset used to create the yield curve.

Any recognisable surplus or deficit in excess of 10% of the greater of scheme assets and scheme liabilities is recognised in the balance sheet as an asset (surplus) or liability (deficit).

In determining the value of scheme liabilities, financial and demographic assumptions are made as to price inflation, pension increases, earnings growth and employee life expectancy. A range of assumptions could be adopted in valuing the schemes' liabilities. Different assumptions could significantly alter the amount of the surplus or deficit recognised in the balance sheet and the pension cost charged to the income statement. The assumptions adopted for the Group's pension schemes are set out in Note 4 to the financial statements together with sensitivities of the balance sheet and income statement to changes in those assumptions. The Group pension surplus recognised on the balance sheet at 31 December 2012 was £82m (2011: £31m).

The Group has also reduced the allowance made for future discretionary increases to pensions in payment, in light of recent experience.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

Critical accounting policies and key sources of accounting judgements (continued)

Pensions (continued)

IAS19 revised

The Group will apply IAS 19 'Employee Benefits (revised)' (IAS 19 revised) from 1 January 2013. The revised standard requires: the immediate recognition of all actuarial gains and losses eliminating the "corridor approach"; interest cost to be calculated on the net pension liability or asset at the long-term bond rate, an expected rate of return will no longer be applied to assets; and all past service costs to be recognised immediately when a scheme is curtailed or amended. If the Group had adopted IAS 19 revised as at 31 December 2012, the net pension asset would become a net pension liability of £180m (2011: liability of £33m). The pension cost would remain unchanged and there would have been no movement in the profit after tax for the period ended 31 December 2012 (2011: loss after tax would be higher by £4m).

Fair value – financial instruments

Financial instruments classified as held-for-trading or designated as at fair value through profit or loss and financial assets classified as available-for-sale are recognised in the financial statements at fair value. All derivatives are measured at fair value. On the balance sheet, financial assets carried at fair value are included within debt securities, equity shares and derivatives as appropriate. Financial liabilities carried at fair value are included within deposits by banks, customer accounts and derivatives. Derivative assets and derivative liabilities are shown separately on the face of the balance sheets. Gains or losses arising from changes in fair value of financial instruments classified as held-for-trading or designated as at fair value through profit or loss are included in the income statement. Unrealised gains and losses on available-for-sale financial assets are recognised directly in equity unless an impairment loss is recognised. The carrying value of a financial asset or a financial liability carried at cost or amortised cost that is the hedged item in a qualifying hedge relationship is adjusted by the gain or loss attributable to the hedged risk.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Fair values are determined by reference to observable market prices where available and reliable. Where representative market prices for an instrument are not available or are unreliable because of poor liquidity, the fair value is derived from prices for its components using appropriate pricing or valuation models that are based on independently sourced market parameters, including interest rate yield curves, option volatilities and currency rates. Financial assets carried at fair value include government and corporate debt securities, reverse repos, loans, corporate equity shares and derivatives. Financial liabilities carried at fair value include deposits, repos, debt securities issued and derivatives. Fair value for a substantial proportion of these instruments is based on observable market prices or derived from observable market parameters. Where observable prices are not available, fair value is based on appropriate valuation techniques or management estimates.

The Group's derivative products include swaps, forwards, futures and options. Exchange traded instruments are valued using quoted prices. The fair value of over-the-counter instruments is derived from pricing models which take account of contract terms, including maturity, as well as quoted market parameters such as interest rates and volatilities. Most of the Group's pricing models do not entail material subjectivity because the methodologies utilised do not incorporate significant judgement and the parameters included in the models can be calibrated to actively quoted market prices. Values established from pricing models are adjusted for credit risk, liquidity risk and future operational costs.

A negligible proportion of the Group's trading derivatives are valued directly from quoted prices, the remaining majority being valued using appropriate valuation techniques. The fair value of substantially all securities positions carried at fair value is determined directly from quoted prices. Fair value for a net open position in a financial instrument in an active market is the number of units of the instrument held times the current bid price (for financial assets) or offer price (for financial liabilities). In determining the fair value of derivative financial instruments gross long and short positions measured at current mid market prices are adjusted by bid-offer reserves calculated on a portfolio basis. Credit valuation adjustments are made when valuing derivative financial assets to incorporate counterparty credit risk. Adjustments are also made when valuing financial liabilities to reflect the Group's own credit standing. Where the market for a financial instrument is not active, fair value is established using a valuation technique. These valuation techniques involve a degree of estimation, the extent of which depends on the instrument's complexity and the availability of market-based data.

More details about the Group's valuation methodologies of the fair value of financial instruments valued using techniques where at least one significant input is unobservable are given in Note 8.

Accounting developments

The following IFRSs and amendments to IFRS have an effective date of 1 January 2013 except for the Amendments to IAS 1 which have an effective date of 1 July 2012:

IFRS 10 'Consolidated Financial Statements' replaces SIC-12 'Consolidation - Special Purpose Entities' and the consolidation elements of the existing IAS 27 'Consolidated and Separate Financial Statements'. IFRS 10 adopts a single definition of control: a reporting entity controls another entity when the reporting entity has the power to direct the activities of that other entity to generate returns for the reporting entity. IFRS 10 requires retrospective application.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

Accounting developments (continued)

Implementation of IFRS 10 will not have a material effect on the Group's financial statements.

IFRS 11 'Joint Arrangements', which supersedes IAS 31 'Interests in Joint Ventures', distinguishes between joint operations and joint ventures. Joint operations are accounted for by the investor recognising its assets and liabilities including its share of any assets held and liabilities incurred jointly and its share of revenues and costs. Joint ventures are accounted for in the investor's consolidated accounts using the equity method. IFRS 11 requires retrospective application. Implementation of IFRS 11 will not have a material effect on the Group's financial statements.

IFRS 12 'Disclosure of Interests in Other Entities' covers disclosures for entities reporting under IFRS 10 and IFRS 11 replacing those in IAS 28 and IAS 27. Entities are required to disclose information that helps financial statement readers evaluate the nature, risks and financial effects associated with an entity's interests in subsidiaries, in associates and joint arrangements and in unconsolidated structured entities.

IAS 27 'Separate Financial Statements' comprises those parts of the existing IAS 27 that deal with separate financial statements and IAS 28 'Investments in Associates and Joint Ventures' covers joint ventures as well as associates; both must be accounted for using the equity method. The mechanics of the equity method are unchanged. These two revised standards have no effect on the Group's financial statements.

Although IFRS 10-12 (as amended) and revised IAS 27 and IAS 28 have an effective date of 1 January 2013, they have been endorsed by the EU for application from 1 January 2014. However, early adoption is permitted and the Group implemented these standards from 1 January 2013.

IFRS 13 'Fair Value Measurement' sets out a single IFRS framework for defining and measuring fair value and requiring disclosures about fair value measurements. Implementation of IFRS 13 will not have a material effect on the Group's financial statements.

'Disclosures - Offsetting Financial Assets and Financial Liabilities (Amendments to IFRS 7)' amended IFRS 7 to require disclosures about the effects and potential effects on an entity's financial position of offsetting financial assets and financial liabilities and related arrangements.

IAS 19 'Employee Benefits' (revised) requires: the immediate recognition of all actuarial gains and losses eliminating the "corridor approach"; interest cost to be calculated on the net pension liability or asset at the long-term bond rate, an expected rate of return will no longer be applied to assets; and all past service costs to be recognised immediately when a scheme is curtailed or amended. The Group will apply IAS 19 (revised) from 1 January 2013. Details of the impact on the Group's financial statements are shown on page 23.

Amendments to IAS 1 'Presentation of Items of Other Comprehensive Income' require items that will never be recognised in profit or loss to be presented separately in other comprehensive income from those items that are subject to subsequent reclassification.

'Annual Improvements 2009-2011 Cycle' makes a number of minor changes to IFRSs. These will not have a material effect on the Group's financial statements.

In October 2012, the IASB issued 'Investment Entities (amendments to IFRS 10, IFRS 12 and IAS 27)'. The amendments apply to 'investment entities': entities whose business is to invest funds solely for returns from capital appreciation, investment income or both and which evaluate the performance of their investments on a fair value basis. The amendments provide an exception to IFRS 10 by requiring investment entities to measure their subsidiaries (other than those that provide services related to the entity's investment activities) at fair value through profit or loss, rather than consolidate them. The amendments are effective from 1 January 2014.

In December 2011, the IASB issued 'Offsetting Financial Assets and Financial Liabilities (Amendments to IAS 32)'. The amendments add application guidance to IAS 32 to address inconsistencies identified in applying some of the standard's criteria for offsetting financial assets and financial liabilities. The amendments are effective for annual periods beginning on or after 1 January 2014 and must be applied retrospectively.

In November 2009, the IASB issued IFRS 9 'Financial Instruments' simplifying the classification and measurement requirements in IAS 39 in respect of financial assets. The standard reduces the measurement categories for financial assets to two: fair value and amortised cost. A financial asset is classified on the basis of the entity's business model for managing the financial asset and the contractual cash flow characteristics of the financial asset. Only assets with contractual terms that give rise to cash flows on specified dates that are solely payments of principal and interest on principal and which are held within a business model whose objective is to hold assets in order to collect contractual cash flows are classified as amortised cost. All other financial assets are measured at fair value. Changes in the value of financial assets measured at fair value are generally taken to profit or loss.

ULSTER BANK LIMITED

ACCOUNTING POLICIES (continued)

Accounting developments (continued)

In October 2010, IFRS 9 was updated to include requirements in respect of the classification and measurement of liabilities. These do not differ markedly from those in IAS 39 except for the treatment of changes in the fair value of financial liabilities that are designated as at fair value through profit or loss attributable to own credit; these must be presented in other comprehensive income.

In December 2011, the IASB issued amendments to IFRS 9 and to IFRS 7 'Financial Instruments: Disclosures' delaying the effective date of IFRS 9 to annual periods beginning on or after 1 January 2015 and introducing revised transitional arrangements including additional transition disclosures. If an entity implements IFRS 9 in 2012 the amendments permit it either to restate comparative periods or to provide the additional disclosures. Additional transition disclosures must be given if implementation takes place after 2012.

IFRS 9 makes major changes to the framework for the classification and measurement of financial instruments and will have a significant effect on the Group's financial statements. The Group is assessing the effect of IFRS 9 which will depend on the results of IASB's reconsideration of IFRS 9's classification and measurement requirements and the outcome of the other phases in the development of IFRS 9.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

1. Net interest income

	Group	
	2012	2011
	£m	£m
Loans and advances to customers	1,088	1,355
Loans and advances to banks	104	116
Debt securities	2	7
Interest receivable	1,194	1,478
Customer accounts	(327)	(347)
Deposits by banks	(113)	(193)
Debt securities in issue	(32)	(64)
Subordinated liabilities	(27)	(34)
Interest payable	(499)	(638)
Net interest income	695	840

Included within net interest income is £249m (2011: £252m) of interest on impaired loans.

2. Non-interest income

	Group	
	2012	2011
	£m	£m
Fees and commission receivable	156	145
Fees and commission payable	(9)	(6)
Income from trading activities ⁽¹⁾ :		
Foreign exchange ⁽²⁾	31	42
Interest rates ⁽³⁾	63	-
Other operating income:		
Profit on buyback of securitisation bonds	-	255
Other income ⁽¹⁾	19	10
Non-interest income	260	446

The analysis of trading income is based on how the business is organised and the underlying risks managed.

During the year ended 31 December 2011 the Group bought back certain externally issued mortgage securitisation bonds at a discount to par and realised a gain of £255m.

Trading income comprises gains and losses on financial instruments held-for-trading, both realised and unrealised, interest income and dividends and the related funding costs. The types of instruments include:

(1) For the year ended 31 December 2011 certain amounts have been reclassified within and between Income from trading activities and Other Income to better reflect the underlying nature of the income stream.

(2) Foreign exchange: spot foreign exchange contracts, currency swaps and options, emerging markets and related hedges and funding.

(3) Interest rates: interest rate swaps, forward foreign exchange contracts, forward rate agreements, interest rate options, interest rate futures and related hedges and funding.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

3. Operating expenses

	Group	
	2012	2011
	£m	£m
Wages, salaries and other staff costs	251	270
Social security costs	27	26
Pension costs:		
- defined benefit schemes (see Note 4)	26	27
- defined contribution schemes (see Note 4)	3	2
Restructure costs	26	5
Staff costs	333	330
Premises and equipment	103	140
Administration	227	140
Other expenses	330	280
Property, plant and equipment depreciation (see Note 14)	26	30
Impairment of property, plant and equipment (see Note 14)	17	-
Depreciation, amortisation and impairment	43	30
	706	640

Included within operating expenses above are the following amounts in respect of costs associated with the technology incident which impacted the Group during 2012:

	2012	2011
	£m	£m
Staff costs	7	-
Other expenses	77	-

The average number of persons employed by the Group during the year, excluding temporary staff was 5,671 (2011: 5,725). The average number of temporary employees during 2012 was 295 (2011: 217). The number of persons employed by the Group at 31 December, excluding temporary staff, was as follows:

	Group	
	2012	2011
	Number	Number
Retail Banking	2,203	2,366
Corporate Banking/Other	3,387	3,386
	5,590	5,752

	Group	
	2012	2011
	£'000	£'000
Auditors' remuneration		
Statutory audit work	1,161	1,118
Non audit work:		
- Other services pursuant to legislation	9	9
	1,170	1,127

Other than the amounts disclosed above, no additional remuneration was payable to the auditors for any other services.

Bank Levy

The Finance Act 2011 introduced an annual bank levy in the UK. The levy is collected through the existing quarterly Corporation Tax collection mechanism.

The levy is based on the total chargeable equity and liabilities as reported in the balance sheet at the end of a chargeable period. The levy is not charged on the first £20 billion of chargeable liabilities.

The levy was charged at a rate of 0.088 per cent for 2012 (2011: 0.075 per cent). Levy costs in respect of the Bank will be borne by the RBS Group for 2012 as in 2011. As the RBS Group continues to target a reduction in wholesale funding, the cost should decline over time in the absence of further rate increases. The levy for 2013 is currently set at 0.105 per cent.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

4. Pension costs

The Group operates the following defined benefit pension schemes, the assets of which are independent of the Group's finances:

Name of schemes

Ulster Bank Pension Scheme
Ulster Bank Pension Scheme (Republic of Ireland)
First Active Pension Scheme

The schemes were closed to new entrants in 2009, when a new defined contribution scheme was launched.

Employees make contributions at varying levels depending on which scheme they are a member of and when they joined the scheme. In addition, employees may make voluntary contributions to secure additional benefits on a money-purchase basis.

The Group also make contributions to a small number of RBS Group Pension Schemes, the costs of which are accounted for as defined contributions. The Group made contributions of £3,252k to its own defined contribution schemes in 2012 (2011: £2,345k). The Bank made contributions of £541k to its own defined contribution schemes in 2012 (2011: £453k).

The corridor method of accounting permits the Group to defer recognition of actuarial gains and losses that are within 10% of the larger of the fair value of plan assets and present value of defined benefit obligations of the schemes, on an individual scheme basis at the beginning of the year. Any excess variations are amortised prospectively over the average remaining service lives of current members of the schemes.

The Group will apply IAS 19 'Employee Benefits revised' (IAS 19 revised) from 1 January 2013. The revised standard requires: the immediate recognition of all actuarial gains and losses eliminating the "corridor approach"; interest cost to be calculated on the net pension liability or asset at the long-term bond rate, an expected rate of return will no longer be applied to assets; and all past service costs to be recognised immediately when a scheme is curtailed or amended.

Interim valuations of the Group's schemes were prepared to 31 December 2012 by independent actuaries, using the following assumptions:

Principal actuarial assumptions at 31 December (weighted average)	Group	
	2012	2011
Discount rate	4.10% - 4.50%	5.00% - 5.75%
Expected return on plan assets	4.10% - 4.50%	5.44% - 5.72%
Rate of increase in salaries	1.75% - 3.90%	1.75%
Rate of increase in pensions in payment	1.00% - 2.00%	1.50% - 2.10%
Inflation assumption	2.00% - 2.90%	2.00% - 3.00%

Major classes of plan assets as a percentage of total plan assets	Group	
	2012	2011
Equities	41%	42%
Index-linked bonds	11%	16%
Government fixed interest bonds	1%	2%
Corporate and other bonds	18%	15%
Hedge Funds	12%	8%
Property	4%	5%
Derivatives	1%	-
Cash and other assets	12%	12%

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

4. Pension costs (continued)

The pension costs disclosures for the year ending 31 December 2013 will be prepared under IAS19 revised which uses the discount rate rather than best-estimate asset returns to calculate the asset return component of the income statement charge. Therefore a table of expected returns for the current year is not presented.

The returns on the major classes of plan assets are based on market expectations at the end of the period.

Principal actuarial assumptions at 31 December	Bank	
	2012	2011
Discount rate	4.50%	5.00%
Expected return on plan assets (weighted average)	4.50%	5.72%
Rate of increase in salaries	3.90%	1.75%
Rate of increase in pensions in payment	1.00%	1.50% - 2.10%
Inflation assumption	2.90%	3.00%

Major classes of plan assets as a percentage of total plan assets	Bank	
	2012	2011
Equities	38%	38%
Index-linked bonds	16%	19%
Government fixed interest bonds	-	-
Corporate and other bonds	17%	15%
Hedge Funds	13%	9%
Property	4%	5%
Derivatives	-	-
Cash and other assets	12%	14%

The pension costs disclosures for the year ending 31 December 2013 will be prepared under IAS19 revised which uses the discount rate rather than best-estimate asset returns to calculate the asset return component of the income statement charge. Therefore a table of expected returns for the current year is not presented.

The returns on the major classes of plan assets are based on market expectations at the end of the period.

Post-retirement mortality assumptions (Main scheme)	Bank	
	2012	2011
Longevity at age 70 for current pensioners (years)		
Males	17.3	17.1
Females	18.7	18.6
Longevity at age 63 for future pensioners (years)		
Males	23.9	23.7
Females	25.5	25.4

These post-retirement mortality assumptions are derived from standard mortality tables used by the scheme actuary to value the liabilities for the main scheme.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

4. Pension costs (continued)

Group (all schemes)	Fair value of plan assets £m	Present value of defined benefit obligations £m	Net pension asset/(liability) £m
Changes in value of net pension asset			
At 1 January 2012	1,162	(1,195)	(33)
Currency translation and other adjustments	(15)	15	-
<i>Income statement:</i>			
Expected return	64	-	64
Interest cost	-	(62)	(62)
Current service cost	-	(30)	(30)
Past service cost	-	2	2
	64	(90)	(26)
<i>Statement of comprehensive income:</i>			
Actuarial gain/(loss)	54	(251)	(197)
Contributions by employer	77	-	77
Contributions by plan participants	4	(4)	-
Benefits paid	(17)	17	-
At 31 December 2012	1,329	(1,508)	(179)
Unrecognised actuarial losses			261
Retirement benefit assets at 31 December 2012			82

Of the expense for the year, £26m (2011: £27m) has been included in the income statement within staff costs (see Note 3). Actuarial gains and losses have been reported in other comprehensive income.

The Group expects to contribute £70m to its defined benefit pension schemes in 2013.

Group (all schemes)	Fair value of plan assets £m	Present value of defined benefit obligations £m	Net pension asset/(liability) £m
Changes in value of net pension asset			
At 1 January 2011	1,146	(1,180)	(34)
Currency translation and other adjustments	(19)	20	1
<i>Income statement:</i>			
Expected return	73	-	73
Interest cost	-	(65)	(65)
Current service cost	-	(33)	(33)
Past service cost	-	(2)	(2)
	73	(100)	(27)
<i>Statement of comprehensive income:</i>			
Actuarial (loss)/gain	(79)	31	(48)
Contributions by employer	75	-	75
Contributions by plan participants	4	(4)	-
Benefits paid	(38)	38	-
At 31 December 2011	1,162	(1,195)	(33)
Unrecognised actuarial losses			64
Retirement benefit assets at 31 December 2011			31

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

4. Pension costs (continued)

Bank	Fair value of plan assets £m	Present value of defined benefit obligations £m	Net pension asset/(liability) £m
Changes in value of net pension asset			
At 1 January 2012	556	(553)	3
<i>Income statement:</i>			
Expected return	32	-	32
Interest cost	-	(27)	(27)
Current service cost	-	(12)	(12)
	32	(39)	(7)
<i>Statement of comprehensive income:</i>			
Actuarial gain/(loss)	18	(20)	(2)
Contributions by employer	40	-	40
Contributions by plan participants	1	(1)	-
Benefits paid	2	(2)	-
At 31 December 2012	649	(615)	34
Unrecognised actuarial losses			21
Retirement benefit assets at 31 December 2012			55

Of the expense for the year, £7m (2011: £6m) has been included in the income statement within staff costs.

The Bank expects to contribute £37m to its defined benefit pension scheme in 2013.

Bank	Fair value of plan assets £m	Present value of defined benefit obligations £m	Net pension asset/(liability) £m
Changes in value of net pension asset			
At 1 January 2011	525	(527)	(2)
<i>Income statement:</i>			
Expected return	34	-	34
Interest cost	-	(29)	(29)
Current service cost	-	(11)	(11)
	34	(40)	(6)
<i>Statement of comprehensive income:</i>			
Actuarial losses	(25)	(3)	(28)
Contributions by employer	39	-	39
Contributions by plan participants	1	(1)	-
Benefits paid	(18)	18	-
At 31 December 2011	556	(553)	3
Unrecognised actuarial losses			20
Retirement benefit assets at 31 December 2011			23

History of defined benefit schemes (Group)	2012 £m	2011 £m	2010 £m	2009 £m	2008 £m
Present value of defined benefit obligations	(1,508)	(1,195)	(1,180)	(1,272)	(1,233)
Fair value of plan assets	1,329	1,162	1,146	1,012	867
Net deficit	(179)	(33)	(34)	(260)	(366)
Experience gains/(losses) on plan liabilities ⁽¹⁾	31	12	137	(184)	(18)
Experience gains/(losses) on plan assets	54	(79)	44	83	(299)
Actual return on pension scheme assets	118	(6)	109	139	(232)

(1) 2011 experience gains on plan liabilities have been adjusted to exclude the impact of changes in actuarial assumptions.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

4. Pension costs (continued)

History of defined benefit schemes (Bank)	2012 £m	2011 £m	2010 £m	2009 £m	2008 £m
Present value of defined benefit obligations	(615)	(553)	(527)	(557)	(462)
Fair value of plan assets	649	556	525	458	388
Net surplus/(deficit)	34	3	(2)	(99)	(74)
Experience gains/(losses) on plan liabilities ⁽¹⁾	28	5	54	(137)	1
Experience gains/(losses) on plan assets	18	(25)	25	29	(108)
Actual return on pension scheme assets	51	9	56	56	(76)

(1) 2011 experience gains on plan liabilities have been adjusted to exclude the impact of changes in actuarial assumptions.

The table below sets out the sensitivities of the pension cost for the year and the present value of defined benefit obligations at the balance sheet dates to a change in the principal actuarial assumptions:

	Group			
	(Decrease)/increase in pension cost for the year		(Decrease)/increase in obligation at 31 December	
	2012	2011	2012	2011
	£m	£m	£m	£m
0.25% increase in the discount rate	(6)	(3)	(77)	(60)
0.25% increase in inflation	7	6	82	63
0.25% additional rate of increase in pensions in payment	3	3	47	38
0.25% additional rate of increase in deferred pensions	-	-	9	8
0.25% additional rate of increase in salaries	3	3	24	17
Longevity increase of 1 year	2	2	30	24

	Bank			
	(Decrease)/increase in pension cost for the year		(Decrease)/increase in pension cost for the year	
	2012	2011	2012	2011
	£m	£m	£m	£m
0.25% increase in the discount rate	(2)	(1)	(29)	(28)
0.25% increase in inflation	2	2	30	29
0.25% additional rate of increase in pensions in payment	1	1	19	19
0.25% additional rate of increase in deferred pensions	-	-	3	3
0.25% additional rate of increase in salaries	1	1	8	7
Longevity increase of 1 year	1	1	12	11

In the Republic of Ireland, the Finance (No.2) Act 2011 introduced a levy at the rate of 0.6% per annum for each of the four years, 2011 to 2014. The Act states that payment is due by 25 September each year. The levy is payable on all of a scheme's assets (other than "excluded assets") and is recognised in the income statement as a reduction in the expected return of assets. An amount of £3.6m (excluding Additional Voluntary Contributions) was deducted from the asset value of the Group's two Republic of Ireland pension schemes within the statutory deadlines (2011: £3.6m).

5. Emoluments of directors

	2012 £	2011 £
Emoluments for the provision of directors' services:		
Non-executive directors - emoluments	346,319	252,000
Chairman and executive directors		
- Emoluments	1,724,916	2,865,300
- Pension contributions	57,638	-
Total emoluments received	2,128,873	3,117,300

Two of the non-executive directors of the Bank, Andrew McLaughlin and Christopher Campbell, are employed by The Royal Bank of Scotland plc and are remunerated for their services to the RBS Group as a whole.

No retirement benefits are accruing to directors under either defined contribution or defined benefit schemes at year end (2011: none).

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

5. Emoluments of directors (continued)

Performance related bonuses are awarded on the basis of measuring annual performance against certain specified financial targets, which include both corporate performance objectives and key strategic objectives.

During the year there were no emoluments in respect of compensation payments for loss of office (2011: £584,265).

During the year the highest paid director received emoluments of £744,792 (2011: £561,948). The highest paid director did not exercise any share options during the year.

The executive directors may also participate in the RBS Group's executive share option and sharesave schemes.

On the 5 July 2012, the Group CEO Jim Brown informed the Board of Directors that he did not wish to be considered for an annual bonus award for 2012.

6. Taxation

	Group	
	2012 £m	2011 £m
Current taxation:		
<i>United Kingdom Corporation Tax at 24.5% (2011: 26.5%)</i>		
Credit for the year	98	180
(Under)/over provision in respect of prior periods	(11)	12
	87	192
<i>Overseas Tax at 12.5% (2011: 12.5%)</i>		
Credit for the year	3	-
Over provision in respect of prior periods	5	4
Total current taxation	95	196
Deferred taxation:		
(Charge)/credit for the year	(13)	57
(Under)/over provision in respect of prior periods	(196)	7
Total deferred taxation	(209)	64
Tax (charge)/credit for the year	(114)	260

The actual tax charge differs from the expected tax credit computed by applying the standard rate of UK Corporation Tax of 24.5% (2011: 26.5%) as follows:

	2012 £m	2011 £m
Operating loss before tax	(2,091)	(3,072)
Expected tax credit	512	814
<i>Factors affecting the credit for the year:</i>		
Tax arising at rates other than the standard rate of tax	(201)	(349)
Non-deductible items	(4)	(9)
Other timing differences	(10)	34
De-recognition of a deferred tax asset	(203)	-
Unrecognised losses (1)	(208)	(253)
Adjustments to tax credit in respect of prior periods	-	23
Actual tax (charge)/credit for the year	(114)	260

The effective tax rate for the year was (5.5%) (2011: 8.5%).

(1) In 2011 'unrecognised losses' included the rate differential between the UK and Irish standard tax rates in respect of such losses. The 2011 comparative figure above recategorises the rate differential of £(284m) under 'tax arising at rates other than the standard rate of tax' in line with the 2012 categorisation.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

7. Loss dealt with in the financial statements of the Bank

In accordance with the exemption contained within Section 408(3) of the Companies Act 2006 the primary financial statements of the Bank do not include an Income Statement or Statement of Comprehensive Income. The Bank's loss after tax for the year ended 31 December 2012 is £3,941m (2011: £3,999m), which includes write downs of investments in Group undertakings which eliminate on consolidation in the results of the Group.

8. Financial instruments

The following tables analyse the financial assets and financial liabilities in accordance with the categories of financial instruments in accordance with IAS 39. Assets and liabilities outside the scope of IAS 39 are shown separately.

	Group						
	Held-for-trading £m	Designated as at fair value through profit or loss £m	Available- for-sale £m	Loans and receivables £m	Other (amortised cost) £m	Non financial assets/ liabilities £m	Total £m
2012							
Assets							
Cash and balances at central banks ⁽¹⁾	-	-	-	725	-	-	725
Loans and advances to banks ⁽²⁾	13	-	-	8,177	-	-	8,190
Loans and advances to customers ⁽³⁾	-	25	-	34,381	-	-	34,406
Debt securities	-	-	26	-	-	-	26
Equity shares	-	-	7	-	-	-	7
Derivatives	724	-	-	-	-	-	724
Property, plant and equipment	-	-	-	-	-	341	341
Prepayments, accrued income and other assets	-	-	-	-	-	123	123
Retirement benefit assets	-	-	-	-	-	82	82
Deferred taxation	-	-	-	-	-	71	71
	737	25	33	43,283	-	617	44,695
Liabilities							
Deposits by banks ⁽⁴⁾	58	-	-	-	7,837	-	7,895
Customer accounts ⁽⁵⁾	4	2,069	-	-	20,997	-	23,070
Debt securities in issue ⁽⁶⁾	-	-	-	-	3,254	-	3,254
Derivatives	992	-	-	-	-	-	992
Accruals, deferred income and other liabilities	-	-	-	-	-	910	910
Deferred taxation	-	-	-	-	-	23	23
Subordinated liabilities	-	-	-	-	1,157	-	1,157
	1,054	2,069	-	-	33,245	933	37,301
Equity							7,394
							44,695

For notes relating to this table refer to page 35.

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NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

8. Financial instruments (continued)

	Group						
2011	Held-for-trading £m	Designated as at fair value through profit or loss £m	Available-for-sale £m	Loans and receivables £m	Other (amortised cost) £m	Non financial assets/liabilities £m	Total £m
Assets							
Cash and balances at central banks (1)	-	-	-	749	-	-	749
Loans and advances to banks (2) (11)	21	-	-	7,310	-	-	7,331
Loans and advances to customers (3) (7) (11)	-	32	-	38,913	-	-	38,945
Debt securities	-	-	98	-	-	-	98
Equity shares	-	-	5	-	-	-	5
Derivatives (8)	997	-	-	-	-	-	997
Property, plant and equipment	-	-	-	-	-	349	349
Prepayments, accrued income and other assets	-	-	-	-	-	155	155
Retirement benefit assets	-	-	-	-	-	31	31
Deferred taxation	-	-	-	-	-	285	285
	1,018	32	103	46,972	-	820	48,945
Liabilities							
Deposits by banks (4) (12)	59	-	-	-	12,771	-	12,830
Customer accounts (5) (9) (12)	17	1,790	-	-	20,541	-	22,348
Debt securities in issue (6)	-	-	-	-	3,530	-	3,530
Derivatives (10)	1,352	-	-	-	-	-	1,352
Accruals, deferred income and other liabilities	-	-	-	-	-	871	871
Deferred taxation	-	-	-	-	-	18	18
Subordinated liabilities	-	-	-	-	1,183	-	1,183
	1,428	1,790	-	-	38,025	889	42,132
Equity							6,813
							48,945

(1) Cash and balances at central banks includes Bank of England notes held in respect of notes in circulation in Northern Ireland.

(2) Includes reverse repurchase agreements of £nil (2011: £nil) and items in the course of collection from other banks of £187m (2011: £198m).

(3) Ulster Bank Group has advances secured on residential properties and corporate and commercial loans subject to non-recourse funding. Under IAS 39, these securitised mortgages qualify for full recognition on the balance sheet at 31 December 2012. As at 31 December 2012, £10,587m (2011: £11,709m) are included in loans and advances to customers.

(4) Includes repurchase agreements of £1,875m (2011: £1,381m) and items in the course of transmission to other banks of £250m (2011: £159m).

(5) The carrying amount of other customer accounts designated as at fair value through profit or loss is £61m less (2011: £65m less) than the principal amount.

(6) Comprises Bonds and medium term notes of £3,217m (2011: £3,472m) and Certificates of deposit and other commercial paper of £37m (2011: £58m).

(7) For the year ended 31 December 2011 £32m of loans and advances to customers classified as held-for-trading have been reclassified as designated as at fair value through profit or loss to better reflect the classification of loans and advances to customers.

(8) For the year ended 31 December 2011 £337m of derivatives classified as held-for-trading have been reclassified as designated as at fair value through profit or loss to better reflect the classification of derivative assets.

(9) For the year ended 31 December 2011 £99m of customer accounts classified as held-for-trading have been reclassified as designated as at fair value through profit or loss to better reflect the classification of customer accounts.

(10) For the year ended 31 December 2011 £1,170m of derivatives classified as designated as at fair value through profit or loss have been reclassified as held for trading to better reflect the classification of derivative liabilities.

(11) Includes amounts due from parent or fellow RBS Group undertakings.

(12) Includes amounts due to parent or fellow RBS Group undertakings.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

8. Financial instruments (continued)

	Bank						
	Held-for-trading £m	Designated as at fair value through profit or loss £m	Available-for-sale £m	Loans and receivables £m	Other (amortised cost) £m	Non financial assets/liabilities £m	Total £m
2012							
Assets							
Cash and balances at central banks	-	-	-	545	-	-	545
Loans and advances to banks ^{(1), (3)}	-	-	-	7,054	-	-	7,054
Loans and advances to customers ⁽¹⁾	-	-	-	6,020	-	-	6,020
Debt securities	-	-	26	-	-	-	26
Investments in Group undertakings	-	-	-	-	-	2,544	2,544
Derivatives	37	-	-	-	-	-	37
Property, plant and equipment	-	-	-	-	-	64	64
Prepayments, accrued income and other assets	-	-	-	-	-	87	87
Retirement benefit assets	-	-	-	-	-	55	55
Deferred taxation	-	-	-	-	-	2	2
	37	-	26	13,619	-	2,752	16,434
Liabilities							
Deposits by banks ^{(2), (4)}	-	-	-	-	4,540	-	4,540
Customer accounts	3	379	-	-	6,772	-	7,154
Debt securities in issue	-	-	-	-	2	-	2
Derivatives	78	-	-	-	-	-	78
Accruals, deferred income and other liabilities	-	-	-	-	-	668	668
Deferred taxation	-	-	-	-	-	20	20
Subordinated liabilities	-	-	-	-	939	-	939
	81	379	-	-	12,253	688	13,401
Equity							3,033
							16,434

	Bank						
	Held-for-trading £m	Designated as at fair value through profit or loss £m	Available-for-sale £m	Loans and receivables £m	Other (amortised cost) £m	Non financial assets/liabilities £m	Total £m
2011							
Assets							
Cash and balances at central banks	-	-	-	522	-	-	522
Loans and advances to banks ^{(1), (3)}	-	-	-	6,757	-	-	6,757
Loans and advances to customers ⁽¹⁾	-	-	-	6,453	-	-	6,453
Debt securities	-	-	71	-	-	-	71
Investments in Group undertakings	-	-	-	-	-	3,488	3,488
Derivatives ⁽⁵⁾	87	-	-	-	-	-	87
Property, plant and equipment	-	-	-	-	-	81	81
Prepayments, accrued income and other assets	-	-	-	-	-	149	149
Retirement benefit assets	-	-	-	-	-	23	23
Deferred taxation	-	-	-	-	-	1	1
	87	-	71	13,732	-	3,742	17,632
Liabilities							
Deposits by banks ^{(2), (4)}	-	-	-	-	4,365	-	4,365
Customer accounts	10	466	-	-	7,011	-	7,487
Debt securities in issue	-	-	-	-	38	-	38
Derivatives	84	-	-	-	-	-	84
Accruals, deferred income and other liabilities	-	-	-	-	-	639	639
Deferred taxation	-	-	-	-	-	15	15
Subordinated liabilities	-	-	-	-	961	-	961
	94	466	-	-	12,375	654	13,589
Equity							4,043
							17,632

(1) Includes amounts due from parent or fellow RBS Group undertakings.

(2) Includes amounts due to parent or fellow RBS Group undertakings.

(3) Includes items in the course of collection from other banks of £60m (2011: £74m).

(4) Includes items in the course of transmission to other banks of £33m (2011: £40m).

(5) For the year ended 31 December 2011 £29m of derivatives classified as held-for-trading have been reclassified as designated as at fair value through profit or loss to better reflect the classification of derivative assets.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

8. Financial instruments (continued)

The following tables show the financial instruments carried at fair value by valuation method:

	Group							
	2012				2011			
	Level 1 ⁽¹⁾ £m	Level 2 ⁽²⁾ £m	Level 3 ⁽³⁾ £m	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets								
Loans and advances to banks	-	13	-	13	-	21	-	21
Loans and advances to customers	-	25	-	25	-	32	-	32
Debt securities	-	26	-	26	27	71	-	98
Equity shares	-	7	-	7	-	5	-	5
Derivatives ⁽⁴⁾	-	724	-	724	-	997	-	997
Total	-	795	-	795	27	1,126	-	1,153
Liabilities								
Deposits by banks	-	58	-	58	-	59	-	59
Deposits by customers	-	2,073	-	2,073	-	1,807	-	1,807
Derivatives ⁽⁵⁾	-	992	-	992	-	1,352	-	1,352
Total	-	3,123	-	3,123	-	3,218	-	3,218

	Bank							
	2012				2011			
	Level 1 ⁽¹⁾ £m	Level 2 ⁽²⁾ £m	Level 3 ⁽³⁾ £m	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets								
Debt securities	-	26	-	26	-	71	-	71
Derivatives ⁽⁴⁾	-	37	-	37	-	87	-	87
Total	-	63	-	63	-	158	-	158
Liabilities								
Deposits by customers	-	382	-	382	-	476	-	476
Derivatives ⁽⁵⁾	-	78	-	78	-	84	-	84
Total	-	460	-	460	-	560	-	560

(1) Valued using unadjusted quoted prices in active markets for identical financial instruments. This category includes listed equity shares, certain exchange-traded derivatives, G10 government securities and certain US agency securities.

(2) Valued using techniques based significantly on observable market data. Instruments in this category are valued using:
a) quoted prices for similar instruments or identical instruments in markets which are not considered to be active; or
b) valuation techniques where all the inputs that have a significant effect on the valuation are directly or indirectly based on observable market data.

The type of instruments that trade in markets that are not considered to be active, but are based on quoted market prices, broker dealer quotations or alternative pricing sources with reasonable levels of price transparency and those instruments valued using techniques include most government agency securities, investment-grade corporate bonds, certain mortgage products, certain bank and bridge loans, repos and reverse repos, less liquid equities, state and municipal obligations, most physical commodities, investment contracts issued by the Group's life assurance businesses and certain money market securities and loan commitments and most OTC derivatives.

(3) Instruments in this category have been valued using a valuation technique where at least one input (which could have a significant effect on the instrument's valuation) is not based on observable market data. Where inputs can be observed from market data without undue cost and effort, the observed input is used. Otherwise, the Group determines a reasonable level for the input.

Financial instruments included within Level 3 of the fair value hierarchy primarily consist of cash instruments which trade infrequently, certain syndicated and commercial mortgage loans, unlisted equity shares, certain residual interests in securitisations, super senior tranches of high grade and mezzanine collateralised debt obligations (CDO's), and other mortgage-based products and less liquid debt securities, certain structured debt securities in issue and OTC derivatives where valuation depends upon unobservable inputs such as certain credit and exotic derivatives. No gain or loss is recognised on the initial recognition of a financial instrument valued using a technique incorporating significant unobservable data.

(4) For the year ending 31 December 2011 the Group reclassified £528m (Bank: £82m) of derivative assets from level 1 to level 2 to better reflect the valuation method used for derivative assets.

(5) For the year ending 31 December 2011 the Group reclassified £947m (Bank: £83m) of derivative liabilities from level 1 to level 2 to better reflect the valuation method used for derivative liabilities.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

8. Financial instruments (continued)

The following tables show the carrying values and the fair values of financial instruments on the balance sheet carried at amortised cost:

	Group			
	2012 Carrying value £m	2012 Fair value £m	2011 Carrying value £m	2011 Fair value £m
Financial assets				
Cash and balances at central banks	725	725	749	749
Loans and advances to banks				
Loans and receivables	8,177	8,177	7,310	7,310
Loans and advances to customers				
Loans and receivables	34,381	27,807	38,913	30,260
Financial liabilities				
Deposits by banks	7,837	7,837	12,771	12,771
Customer accounts	20,997	21,093	20,541	20,658
Debt securities in issue	3,254	2,160	3,530	2,130
Subordinated liabilities	1,157	1,157	1,183	1,197
	Bank			
	2012 Carrying value £m	2012 Fair value £m	2011 Carrying value £m	2011 Fair value £m
Financial assets				
Cash and balances at central banks	545	545	522	522
Loans and advances to banks				
Loans and receivables	7,054	7,054	6,757	6,757
Loans and advances to customers				
Loans and receivables	6,020	5,417	6,453	4,921
Financial liabilities				
Deposits by banks	4,540	4,540	4,365	4,364
Customer accounts	6,772	6,781	7,011	7,021
Debt securities in issue	2	2	38	38
Subordinated liabilities	939	939	961	961

The fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Quoted market values are used where available; otherwise, fair values have been estimated based on discounted expected future cash flows and other valuation techniques. These techniques involve uncertainties and require assumptions and judgments covering prepayments, credit risk and discount rates.

Changes in these assumptions would significantly affect estimated fair values. The fair values reported would not necessarily be realised in an immediate sale or settlement. As a wide range of valuation techniques are available, it may be inappropriate to compare the Group's fair value information to independent markets or other financial institutions' fair values.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

8. Financial instruments (continued)

The assumptions and methodologies underlying the calculation of fair values of financial instruments at the balance sheet date are set out below:

The fair value of financial instruments that are of short maturity (3 months or less) approximates their carrying value. This applies mainly to cash and balances at central banks, items in the course of collection from other banks, settlement balances, items in the course of transmission to other banks and demand deposits.

The Group uses a number of methodologies to determine the fair values of financial instruments for which observable prices in active markets for identical instruments are not available. These techniques include: relative value methodologies based on observable prices for similar instruments; present value approaches where future cash flows from the asset or liability are estimated and then discounted using a risk-adjusted interest rate; option pricing models (such as Black-Scholes or binomial option pricing models) and simulation models such as Monte-Carlo.

The principal inputs to these valuation techniques are listed below. Values between and beyond available data points are obtained by interpolation and extrapolation. When utilising valuation techniques, the fair value can be significantly affected by the choice of valuation model and by underlying assumptions concerning factors such as the amounts and timing of cash flows, discount rates and credit risk.

- Bond prices - quoted prices are generally available for government bonds, certain corporate securities and some mortgage-related products.
- Credit spreads - where available, these are derived from prices of credit default swaps or other credit based instruments, such as debt securities. For others, credit spreads are obtained from pricing services.
- Interest rates - these are principally benchmark interest rates such as the London Inter-Bank Offered Rate (LIBOR) and quoted interest rates in the swap, bond and futures markets.
- Foreign currency exchange rates - there are observable markets both for spot and forward contracts and futures in the world's major currencies.

Loans and advances to banks and customers

Fair value is estimated by grouping loans into homogeneous portfolios and applying a discount rate to the cash flows. The discount rate is based on the market rate applicable at the balance sheet date for a similar portfolio with similar maturity and credit risk characteristics.

Debt securities

Fair values are determined using quoted prices where available or by reference to quoted prices of similar instruments.

Deposits by banks and customer accounts

The fair values of deposits are estimated using discounted cash flow valuation techniques.

Remaining maturity

	Group		Total £m
	Less than 12 months £m	More than 12 months £m	
2012			
Assets			
Cash and balances at central banks	725	-	725
Loans and advances to banks	6,104	2,086	8,190
Loans and advances to customers	8,679	25,727	34,406
Debt securities	-	26	26
Equity shares	-	7	7
Derivatives	84	640	724
Liabilities			
Deposits by banks	5,013	2,882	7,895
Customer accounts	20,868	2,202	23,070
Debt securities in issue	32	3,222	3,254
Derivatives	67	925	992
Subordinated liabilities	63	1,094	1,157

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

8. Financial instruments (continued)

2011	Group		Total £m
	Less than 12 months £m	More than 12 months £m	
Assets			
Cash and balances at central banks	749	-	749
Loans and advances to banks	5,438	1,893	7,331
Loans and advances to customers	8,769	30,176	38,945
Debt securities	15	83	98
Equity shares	-	5	5
Derivatives ⁽¹⁾	193	804	997
Liabilities			
Deposits by banks	11,100	1,730	12,830
Customer accounts	19,813	2,535	22,348
Debt securities in issue	44	3,486	3,530
Derivatives ⁽²⁾	134	1,218	1,352
Subordinated liabilities	-	1,183	1,183

2012	Bank		Total £m
	Less than 12 months £m	More than 12 months £m	
Assets			
Cash and balances at central banks	545	-	545
Loans and advances to banks	4,548	2,506	7,054
Loans and advances to customers	2,481	3,539	6,020
Debt securities	-	26	26
Derivatives	22	15	37
Liabilities			
Deposits by banks	2,803	1,737	4,540
Customer accounts	6,664	490	7,154
Debt securities in issue	-	2	2
Derivatives	15	63	78
Subordinated liabilities	-	939	939

2011	Bank		Total £m
	Less than 12 months £m	More than 12 months £m	
Assets			
Cash and balances at central banks	522	-	522
Loans and advances to banks	4,289	2,468	6,757
Loans and advances to customers	2,531	3,922	6,453
Debt securities	6	65	71
Derivatives ⁽¹⁾	26	61	87
Liabilities			
Deposits by banks	2,672	1,693	4,365
Customer accounts	6,404	1,083	7,487
Debt securities in issue	38	-	38
Derivatives ⁽²⁾	19	65	84
Subordinated liabilities	-	961	961

(1) For the year ending 31 December 2011 the Group reclassified £364m (Bank: £31m) of derivative assets from less than 12 months to more than 12 months to better reflect the remaining maturity of derivative assets.

(2) For the year ending 31 December 2011 the Group reclassified £847m (Bank: £65m) of derivative liabilities from less than 12 months to more than 12 months to better reflect the remaining maturity of derivative liabilities.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

9. Financial assets – impairments

The following table shows the movement in the provision for impairment losses for loans and advances:

	Group			
	Individually assessed £m	Collectively assessed £m	Latent £m	Total £m
At 1 January 2012	7,157	1,312	582	9,051
Currency translation and other adjustments	(122)	(23)	(12)	(157)
Transfer	(275)	275	-	-
Amounts written-off ⁽¹⁾	(149)	(63)	-	(212)
Charged to the income statement	1,297	802	241	2,340
Unwind of discount	(217)	(31)	-	(248)
At 31 December 2012 ⁽²⁾	7,691	2,272	811	10,774

	Group			
	Individually assessed £m	Collectively assessed £m	Latent £m	Total £m
At 1 January 2011	4,616	753	609	5,978
Currency translation and other adjustments	(164)	(38)	(16)	(218)
Amounts written-off ⁽¹⁾	(131)	(43)	-	(174)
Charged/(credited) to the income statement	3,062	667	(11)	3,718
Unwind of discount	(226)	(27)	-	(253)
At 31 December 2011 ⁽²⁾	7,157	1,312	582	9,051

	Bank			
	Individually assessed £m	Collectively assessed £m	Latent £m	Total £m
At 1 January 2012	1,589	161	71	1,821
Other adjustments	2	-	-	2
Transfer	(101)	101	-	-
Amounts written-off ⁽¹⁾	(83)	(24)	-	(107)
Charged to the income statement	287	67	9	363
Unwind of discount	(44)	(3)	-	(47)
At 31 December 2012 ⁽²⁾	1,650	302	80	2,032

	Bank			
	Individually assessed £m	Collectively assessed £m	Latent £m	Total £m
At 1 January 2011	886	122	126	1,134
Amounts written-off ⁽¹⁾	(3)	(16)	-	(19)
Charged/(credited) to the income statement	754	57	(55)	756
Unwind of discount	(48)	(2)	-	(50)
At 31 December 2011 ⁽²⁾	1,589	161	71	1,821

⁽¹⁾ Amounts written off do not include any loans and advances to banks.

⁽²⁾ Impairment losses at 31 December 2012 and 31 December 2011 do not include any loans and advances to banks.

Loan impairment

At 31 December 2012, the Group's non-accrual loans and loans past due 90 days amounted to £18,850m (2011: £17,134m) and £3,162m (2011: £3,243m) for Bank. Loan impairment provisions of £9,963m (2011: £8,469m) were held against the Group loans and £1,952m (2011: £1,750m) against the Bank loans:

	Group		Bank	
	2012 £m	2011 £m	2012 £m	2011 £m
Gross income not recognised but which would have been recognised under the original terms of non-accrual and restructured loans:				
Domestic	275	183	275	183
Foreign	1,208	814	-	-
	1,483	997	275	183

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

9. Financial assets – impairments (continued)

The Group considers financial assets to be impaired when there is no longer a reasonable prospect of receiving the contractual cash flows in accordance with the contract and the net present value of any security is less than the outstanding amount.

The following table shows analysis of impaired financial assets:

Group	2012			2011		
	Cost £m	Provision £m	Net book value £m	Cost £m	Provision £m	Net book value £m
Impaired financial assets						
Loans and advances to customers	18,219	(9,963)	8,256	16,763	(8,469)	8,294
Equity shares	9	(2)	7	7	(2)	5
	18,228	(9,965)	8,263	16,770	(8,471)	8,299

Bank	2012			2011		
	Cost £m	Provision £m	Net book value £m	Cost £m	Provision £m	Net book value £m
Impaired financial assets						
Loans and advances to customers	3,114	(1,952)	1,162	3,131	(1,750)	1,381

The Group holds collateral in respect of certain loans and advances to banks and to customers that are past due or impaired. Such collateral includes mortgages over property (both personal and commercial); charges over business assets such as plant, inventories and trade receivables; and guarantees of lending from parties other than the borrower.

The following table shows financial and non-financial assets, recognised on the Group and Bank's balance sheets, obtained during the year by taking possession of collateral or calling on other credit enhancements:

	Group		Bank	
	2012 £m	2011 £m	2012 £m	2011 £m
Residential property	36	22	7	5
Other property	32	49	-	-
	68	71	7	5

The following assets were past due at the balance sheet date but not considered impaired:

Group	Past due 1–29 days £m	Past due 30–59 days £m	Past due 60–89 days £m	Past due more than 90 days £m	Total £m
2012					
Loans and advances to customers	1,260	539	370	631	2,800

2011					
Loans and advances to customers	1,390	570	414	371	2,745

Bank	Past due 1–29 days £m	Past due 30–59 days £m	Past due 60–89 days £m	Past due more than 90 days £m	Total £m
2012					
Loans and advances to customers	90	30	14	48	182

2011					
Loans and advances to customers	113	23	10	112	258

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

9. Financial assets – impairments (continued)

	Group		Bank	
	2012 £m	2011 £m	2012 £m	2011 £m
Impaired financial assets – individually assessed:				
Loans and advances to customers	7,691	7,157	1,650	1,589

Loans that have been renegotiated in the past 12 months that would otherwise have been past due or impaired amounted to £2,604m as at 31 December 2012 (2011: £3,008m) for the Group and £42m (2011: £164m) for the Bank.

10. Debt securities

	Group							
	2012				2011			
	Other central and local government £m	Bank and building society £m	Mortgage backed securities £m	Total £m	Other central and local government £m	Bank and building society £m	Mortgage backed securities £m	Total £m
Available-for-sale	-	-	26	26	27	6	65	98
Gross unrealised gains	-	-	-	-	1	-	-	1
Gross unrealised losses	-	-	-	-	-	-	(2)	(2)

	Bank							
	2012				2011			
	Other central and local government £m	Bank and building society £m	Mortgage backed securities £m	Total £m	Other central and local government £m	Bank and building society £m	Mortgage backed securities £m	Total £m
Available-for-sale	-	-	26	26	-	6	65	71
Gross unrealised losses	-	-	-	-	-	-	(2)	(2)

11. Equity shares

	Group					
	2012			2011		
	Listed £m	Unlisted £m	Total £m	Listed £m	Unlisted £m	Total £m
Available-for-sale	-	7	7	-	5	5

As at 31 December 2012, the Bank held £172,048 unlisted equity shares (2011: £154,549). No gains or losses were realised on the available-for-sale equity shares (2011: £nil).

Unquoted equity investments whose fair value cannot be reliably measured are carried at cost and classified as available-for-sale financial assets.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

12. Investments in Group undertakings

Investments in Group undertakings are carried at cost less impairment. Movements during the year were as follows:

	Bank	
	2012 £m	2011 £m
At 1 January	3,488	2,951
Exchange adjustment	(11)	(13)
Additional investments in Group undertakings	2,730	4,068
Impairment in Ulster Bank (Ireland) Holdings	(3,663)	(3,518)
At 31 December	2,544	3,488

The fair value of investments in Group undertakings is calculated using a model based on expected future profits plus future equity requirements. The net equity flows are discounted relative to the number of years from the current year. A terminal value is added to the discounted expected future profits to provide the fair value of the subsidiary. If the fair value of the subsidiary is less than its carrying value, an impairment loss is recognised immediately in profit or loss and the carrying value of the asset reduced by the amount of the loss.

The principal related undertaking of the Bank is shown below. Its capital consists of ordinary shares which are unlisted. It is wholly owned by the Bank through intermediate holding companies.

Undertaking	Nature of business	Country of incorporation
Ulster Bank Ireland Limited (1)	Banking services, corporate and investment banking, foreign exchange services	Republic of Ireland

(1) Ulster Bank Ireland Limited and its subsidiaries also operate in the UK.

The above information is provided in relation to the principal related undertakings as permitted by Section 410(2) of the Companies Act 2006. Full information on all related undertakings will be included in the Annual Return filed with the UK Companies House. All of these undertakings are included in the Group's consolidated financial statements and have an accounting reference date of 31 December.

There are a number of entities in which the Group holds less than half the voting rights which are consolidated when the substance of the relationship between the Group and the entity indicates that the entity is controlled by the Group. Such entities are deemed to be controlled by the Group when relationships with such entities give rise to benefits that are in substance no different from those that would arise were the entity a subsidiary.

13. Intangible assets

Intangible assets comprising goodwill, computer software and other acquired intangibles were fully impaired as at 31 December 2012 and 31 December 2011. No further intangible assets were developed or acquired in the current or the previous year.

ULSTER BANK LIMITED

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14. Property, plant and equipment

	Group					
	Investment properties	Freehold land and buildings	Leases of 50 years or more unexpired	Leases of 50 years or less unexpired	Computer and other equipment	Total
2012	£m	£m	£m	£m	£m	£m
Cost:						
At 1 January 2012	111	151	42	80	235	619
Currency translation and other adjustments	(2)	(3)	(1)	(2)	(3)	(11)
Additions	42	1	1	4	5	53
Disposals	-	(2)	-	(2)	-	(4)
Revaluation	(6)	-	-	-	-	(6)
At 31 December 2012	145	147	42	80	237	651
Accumulated depreciation and amortisation:						
At 1 January 2012	-	57	18	24	171	270
Currency translation and other adjustments	-	-	-	-	(2)	(2)
Disposals	-	-	-	(1)	-	(1)
Impairments	-	16	1	-	-	17
Depreciation charge for the year	-	4	1	7	14	26
At 31 December 2012	-	77	20	30	183	310
Carrying amount at 31 December 2012	145	70	22	50	54	341
	Group					
	Investment properties	Freehold land and buildings	Leases of 50 years or more unexpired	Leases of 50 years or less unexpired	Computer and other equipment	Total
2011	£m	£m	£m	£m	£m	£m
Cost:						
At 1 January 2011	113	170	61	86	237	667
Currency translation and other adjustments	(2)	(3)	(1)	(2)	(3)	(11)
Reclassifications	11	-	(11)	-	-	-
Additions	56	1	-	1	2	60
Disposals	-	(17)	(7)	(5)	(1)	(30)
Revaluation	(67)	-	-	-	-	(67)
At 31 December 2011	111	151	42	80	235	619
Accumulated depreciation and amortisation:						
At 1 January 2011	3	71	13	22	158	267
Currency translation and other adjustments	-	(1)	-	(1)	(3)	(5)
Reclassifications	(3)	-	3	-	-	-
Disposals	-	(17)	-	(5)	-	(22)
Depreciation charge for the year	-	4	2	8	16	30
At 31 December 2011	-	57	18	24	171	270
Carrying amount at 31 December 2011	111	94	24	56	64	349

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NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

14. Property, plant and equipment (continued)

There was no profit on disposal of freehold land and buildings during the year (2011: £nil).

Rental income from investment properties was £7m (2011: £6m). During the year there were £3m direct operating expenses of investment properties (2011: £2m) and £12m direct operating expenses of investment properties not generating rental income (2011: £9m).

	Bank				Total £m
	Freehold land and buildings £m	Leases of 50 years or more unexpired £m	Leases of 50 years or less unexpired £m	Computer and other equipment £m	
2012					
Cost:					
At 1 January 2012	53	21	10	107	191
Additions	-	-	1	1	2
Disposals	(2)	-	-	-	(2)
At 31 December 2012	51	21	11	108	191
Accumulated depreciation and amortisation:					
At 1 January 2012	16	5	3	86	110
Impairments	7	1	-	-	8
Depreciation charge for the year	1	1	1	6	9
At 31 December 2012	24	7	4	92	127
Carrying amount at 31 December 2012	27	14	7	16	64
	Bank				Total £m
	Freehold land and buildings £m	Leases of 50 years or more unexpired £m	Leases of 50 years or less unexpired £m	Computer and other equipment £m	
2011					
Cost:					
At 1 January 2011	52	21	10	107	190
Additions	1	-	-	-	1
At 31 December 2011	53	21	10	107	191
Accumulated depreciation and amortisation:					
At 1 January 2011	15	5	2	78	100
Depreciation charge for the year	1	-	1	8	10
At 31 December 2011	16	5	3	86	110
Carrying amount at 31 December 2011	37	16	7	21	81

There was no profit on disposal of freehold land and building during the year (2011: £nil).

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15. Derivatives

Companies in the Group transact derivatives as principal either as a trading activity or to manage balance sheet foreign exchange, interest rate and credit risk.

	Group					
	2012			2011		
	Notional amounts £m	Assets £m	Liabilities £m	Notional amounts £m	Assets £m	Liabilities £m
Free standing derivatives						
Exchange rate contracts:						
Spot, forwards and futures	1,866	12	17	4,134	128	73
Currency swaps	1,495	55	176	1,537	52	196
Interest rate contracts:						
Interest rate swaps	45,133	551	796	50,722	733	1,071
Options purchased	168	-	-	327	5	-
Options written	190	-	-	216	-	5
Futures and forwards	504	2	3	1,260	7	7
Equity and commodity contracts	1,930	104	-	1,672	72	-
	51,286	724	992	59,868	997	1,352

	Bank					
	2012			2011		
	Notional amounts £m	Assets £m	Liabilities £m	Notional amounts £m	Assets £m	Liabilities £m
Free standing derivatives						
Exchange rate contracts:						
Spot, forwards and futures	152	1	1	220	4	4
Interest rate contracts:						
Interest rate swaps	4,718	36	77	2,821	54	80
Equity and commodity contracts	-	-	-	475	29	-
	4,870	37	78	3,516	87	84

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NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

16. Prepayments, accrued income and other assets

	Group		Bank	
	2012	2011	2012	2011
	£m	£m	£m	£m
Prepayments	16	19	5	5
Accrued income	11	13	3	4
Other assets	96	123	79	140
	123	155	87	149

17. Accruals, deferred income and other liabilities

	Group		Bank	
	2012	2011	2012	2011
	£m	£m	£m	£m
Notes in circulation	578	552	578	552
Accruals	199	227	51	55
Deferred income	3	9	1	3
Other liabilities	130	83	38	29
	910	871	668	639

Provisions of £114m (2011: £82m) for the Group and £41m (2011: £27m) for the Bank are included in other liabilities.

The following amounts are included within provisions:

	Group			
	Property Provision £m	Other Provisions £m	PPI Provisions £m	Total Provisions £m
Provision as at 1 January 2012	67	4	11	82
Charged to income statement	16	64	26	106
Utilised in the year	(20)	(35)	(15)	(70)
Exchange adjustment	(1)	-	-	(1)
Released during the year	(3)	-	-	(3)
Provision as at 31 December 2012	59	33	22	114

	Bank			
	Property Provision £m	Other Provisions £m	PPI Provisions £m	Total Provisions £m
Provision as at 1 January 2012	15	1	11	27
Charged to income statement	7	32	17	56
Utilised in the year	(9)	(18)	(15)	(42)
Provision as at 31 December 2012	13	15	13	41

Payment Protection Insurance (PPI)

The PPI provision was established to reflect current experience of PPI complaints received. The eventual cost is dependent upon complaint volumes, uphold rates and average redress costs. Assumptions relating to these are inherently uncertain and the ultimate financial impact may be different from the amount provided. The Group will continue to monitor the position closely and refresh its assumptions as more information becomes available.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

18. Deferred taxation

Provision for deferred taxation has been made as follows:

	Group		Bank	
	2012	2011	2012	2011
	£m	£m	£m	£m
Deferred tax asset	71	285	2	1
Deferred tax liability	(23)	(18)	(20)	(15)
Net deferred tax asset/(liability)	48	267	(18)	(14)

	Group						
	Pension	Accelerated capital allowances	Deferred gains	Fair value on financial instruments	Other	Tax losses	Total
	£m	£m	£m	£m	£m	£m	£m
At 1 January 2011	3	-	(15)	1	(3)	226	212
(Charge) / credit to income statement	(9)	2	5	-	-	66	64
Charge to equity directly	(1)	-	-	-	-	-	(1)
Other	-	-	1	-	-	(9)	(8)
At 1 January 2012	(7)	2	(9)	1	(3)	283	267
(Charge) / credit to income statement	(8)	(1)	3	-	-	(203)	(209)
Charge to equity directly	(2)	-	-	-	-	-	(2)
Other	-	-	-	-	(1)	(7)	(8)
At 31 December 2012	(17)	1	(6)	1	(4)	73	48

Deferred tax assets are recognised depending on the availability of future taxable profits in excess of profits arising from the reversal of other temporary differences. Economic and market pressures have continued to have a negative impact on future profit projections. Business projections prepared for impairment reviews indicate it is probable that sufficient future taxable income will be available against which to offset deferred tax assets of £73m in respect of losses within seven years. Therefore it has been appropriate to de-recognise the deferred tax asset carried at 1 January 2012 by £203m. In jurisdictions where doubt exists over the availability of future taxable profits, deferred tax assets of £886m (2011: £494m) have not been recognised in respect of tax losses carried forward.

Deferred tax liabilities of £113m (2011: £132m) have not been recognised in respect of retained earnings of overseas subsidiaries and held-over gains on the incorporation of overseas branches. Retained earnings of overseas subsidiaries are expected to be reinvested indefinitely or remitted to the UK free from further taxation. No taxation is expected to arise in the foreseeable future in respect of held-over gains.

	Bank
	£m
Provisions for Deferred Tax	
Balance at 1 January 2011	(7)
Charge to income statement	(6)
Charge directly to equity	(1)
At 1 January 2012	(14)
Charge to income statement	(4)
At 31 December 2012	(18)

The Finance Act 2012 has reduced the corporation tax rate from 25% to 23% with effect from 1 April 2013. As a consequence the closing deferred tax assets and/or liabilities of the Bank have been recognised at an effective rate of 23%.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

19. Subordinated liabilities

	Group		Bank	
	2012	2011	2012	2011
	£m	£m	£m	£m
Dated loan capital	923	944	841	861
Undated loan capital	98	100	98	100
Dated subordinated bonds	63	64	-	-
Undated perpetual subordinated bonds	73	75	-	-
	1,157	1,183	939	961
	Group		Bank	
	2012	2011	2012	2011
	£m	£m	£m	£m
Dated loan capital:				
Repayable 2014				
– held by immediate parent company	20	20	20	20
Repayable 2015				
– held by immediate parent company	20	20	20	20
Repayable 2019				
– held by RBS plc	100	100	100	100
Euro loan capital repayable 2017				
– held by RBS plc	326	335	326	335
Euro loan capital repayable 2020				
– held by RBS plc	147	151	147	151
Euro loan capital repayable 2022				
– held by RBS plc	310	318	228	235
	923	944	841	861
Undated loan capital:				
– held by RBS plc	98	100	98	100
	98	100	98	100
Dated subordinated bonds				
£60m 6.375% subordinated bonds 2018 (callable April 2013)	63	64	-	-
	63	64	-	-
Undated perpetual subordinated bonds				
€38m 11.375% perpetual tier two capital	46	47	-	-
£20m 11.75% perpetual tier two capital	25	26	-	-
£1.3m floating rate perpetual tier two capital	2	2	-	-
	73	75	-	-
Total	1,157	1,183	939	961

Dated loan capital

Claims in respect of the Group's and the Bank's loan capital are subordinate to the claims of other creditors. None of the loan capital is secured.

Interest on the Sterling-denominated dated loan capital held by fellow subsidiary undertakings, the immediate parent company and the ultimate holding company are payable quarterly at a margin over London Interbank Offer rates. Interest on Euro-denominated loan capital is payable quarterly at a margin over Euro Interbank Offer rates.

Early repayment of the dated loan capital may take place at any time with a notice period of at least 30 days, subject to the prior agreement of the Financial Services Authority (FSA).

Undated Loan Capital

The Sterling loan stock, which is perpetual, is held by another company within the RBS Group and is repayable at the option of the Bank only with prior consent of the Central Bank of Ireland.

Dated subordinated bonds

The Sterling fixed subordinated bonds mature on 4 April 2018 but are callable in April 2013. The claims of the holders of the bonds are subordinate to the claims of all creditors of First Active plc other than the holders of the perpetual subordinated bonds.

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NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

19. Subordinated liabilities (continued)

Perpetual subordinated bonds

The subordinated perpetual bonds were issued by First Active plc, in the Republic of Ireland, at par on conversion of First National Building Society to a public limited company pursuant to Section 107 of the Building Societies Act, 1989 to replace the issued fixed and floating rate permanent interest bearing shares of the Society. The claims of the holders of the bonds are subordinate to the claims of all creditors of Ulster Bank Ireland Limited.

20. Share capital

	Group and Bank			
	Allotted, called up and fully paid		Authorised	
	1 January 2012 £m	31 December 2012 £m	2012 £m	2011 £m
<i>Equity shares:</i>				
Ordinary shares of £1	1,208	1,208	2,000	2,000
<i>Equity preference shares:</i>				
Non-cumulative redeemable preference shares of €1 each	297	297	346	346
Total share capital	1,505	1,505	2,346	2,346

	Allotted, called up and fully paid		Authorised	
	2012 Millions	2011 Millions	2012 Millions	2011 Millions
Number of shares				
<i>Equity shares:</i>				
Ordinary shares of £1	1,208	1,208	2,000	2,000
<i>Equity Preference shares:</i>				
Non-cumulative redeemable preference shares of €1 each	450	450	500	500
Total share capital	1,658	1,658	2,500	2,500

The non-cumulative redeemable preference shares entitle the holders thereof to receive periodic non-cumulative cash dividends, at the discretion of the directors, at a specified floating rate payable out of distributable profits of the Bank. In a winding-up the holders of the preference shares have the right to repayment in priority to the holders of any other class of shares in the capital of the Bank. Any surplus assets available after repayment of the preference shares will be distributable to the holders of the £1 ordinary shares.

The non-cumulative redeemable preference shares do not confer on the holder a right to attend or vote at general meetings of the Bank unless the business of the meeting includes the consideration of a resolution for winding up of the Bank or reducing its share capital or varying any of its special rights attached to the preference shares.

Subject to the provisions of company law and to the consent of the FSA, the Bank shall have the right to redeem the preference shares at any time by notice to the holders provided that no such notice may be issued in respect of any preference share prior to the day following the fifth anniversary of the date of its allotment.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

21. Leases

Amounts receivable under finance lease contracts and hire purchase agreements:

Year in which receipt will occur:	Group					
	2012			2011		
	Gross amounts £m	Present value adjustments £m	Present value £m	Gross amounts £m	Present value adjustments £m	Present value £m
Within 1 year	61	-	61	4	-	4
After 1 year but within 5 years	83	(5)	78	9	-	9
After 5 years	1	-	1	-	-	-
	145	(5)	140	13	-	13

The Group provides asset finance to its customers through acting as a lessor. It purchases plant and equipment renting them to customers under lease arrangements that qualify as finance leases.

Minimum amounts payable under non-cancellable leases:

Year in which payment will occur:	Group							
	2012				2011			
	Within 1 year £m	After 1 year but within 5 years £m	After 5 years £m	Total £m	Within 1 year £m	After 1 year but within 5 years £m	After 5 years £m	Total £m
<i>Operating lease obligations:</i>								
Future minimum lease payables:								
Premises	20	70	147	237	22	80	182	284
Equipment	2	1	-	3	2	2	-	4
	22	71	147	240	24	82	182	288

Year in which payment will occur:	Bank							
	2012				2011			
	Within 1 year £m	After 1 year but within 5 years £m	After 5 years £m	Total £m	Within 1 year £m	After 1 year but within 5 years £m	After 5 years £m	Total £m
<i>Operating lease obligations:</i>								
Future minimum lease payables:								
Premises	2	4	88	94	2	6	89	97
Equipment	1	-	-	1	-	-	-	-
	3	4	88	95	2	6	89	97

	Group		Bank	
	2012 £m	2011 £m	2012 £m	2011 £m
Amounts recognised as income and expense				
Operating lease payables – minimum payments	22	23	3	3

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NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

22. Collateral and securitisations

Securities repurchase agreements and lending transactions

The Group enters into securities repurchase agreements and securities lending transactions under which it receives or transfers collateral in accordance with normal market practice. Generally, the agreements require additional collateral to be provided if the value of the securities fall below a predetermined level.

Under standard terms for repurchase transactions in the United Kingdom and Republic of Ireland, the recipient of collateral has an unrestricted right to sell or repledge it, subject to returning equivalent securities on settlement of the transaction.

The fair value (and carrying value) of securities transferred under repurchase transactions included within debt securities on the balance sheet were £nil (2011: £nil). Securities received as collateral under reverse repurchase agreements amounted to £nil (2011: £nil).

Other collateral given

	Group	
	2012	2011
	£m	£m
Group assets charged as security for liabilities		
Loans and advances to customers	13,089	14,912
Investment properties	1	19
Derivatives	8	9
	13,098	14,940
	Group	
	2012	2011
	£m	£m
Liabilities secured by charges on assets		
Debt securities in issue	3,217	3,472
Deposits by banks	1,884	1,380
Derivatives	26	19
Other liabilities	2	20
	5,129	4,891

Of the assets above, £11.3 billion (2011: £12.7 billion) relates to securitisations.

Included in deposits by banks is Ulster Bank Ireland Limited's obligation to the Central Bank of Ireland (CBI) under the terms of a Mortgage Backed Promissory Note programme. These obligations are secured by way of a floating charge to the CBI over all its right, title, interest and benefit.

Securitisations and other asset transfers

The Group undertakes securitisations to fund specific portfolios of assets. In a securitisation, assets, or interests in a pool of assets, are transferred generally to a special purpose entity (SPE) which then issues liabilities to third party investors. SPEs are vehicles established for a specific, limited purpose, usually do not carry out a business or trade and typically have no employees. They take a variety of legal forms - trusts, partnerships and companies - and fulfill many different functions.

It is primarily the extent of risks and rewards assumed that determines whether these entities are consolidated in the Group's financial statements. The following section aims to address the significant exposures which arise from the Group's activities through specific types of SPEs.

The table below sets out the asset categories together with the carrying amounts of the assets and associated liabilities for those securitisations where substantially all the risks and rewards of the asset have been retained by the Group and continue to be presented in its balance sheet.

	2012		2011	
	Assets	Liabilities	Assets	Liabilities
	£m	£m	£m	£m
Residential mortgages	10,587	3,217	11,709	3,472
Corporate and commercial loans	738	-	951	-

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management

The major risks associated with the Group's businesses are market, liquidity, credit, regulatory, reputational, conduct, operational and sovereign risk. The Group has established a comprehensive framework for managing these risks which is continually evolving as the Group's business activities change in response to market, credit, product and other developments. The Group is also exposed to risks from its defined benefit pension schemes.

The Group has established clear risk policies, including limits, reporting lines and control procedures. This framework is designed to provide tight control and is reviewed regularly by both Executive and Board Committees.

Market risk

Market risk is defined as the risk of loss as a result of adverse changes in market factors. The risk factors include interest rates, foreign currency and equity prices together with related parameters such as market volatilities.

The principal market risks to which the Group is exposed are interest rate risk and foreign exchange risk. The RBS Group manages market risk within its trading and non-trading portfolios through a comprehensive market risk management framework. This framework includes limits based on, but not limited to Value at Risk ("VaR"), scenario analysis, position and sensitivity analysis. The Group in conjunction with the RBS Group Market Risk and Group Treasury annually agree sub limits based on the Group's approved market risk appetite.

At the RBS Group level, the risk appetite is expressed in the form of a combination of VaR, sensitivity and scenario limits. VaR is a technique that produces estimates of the potential change in the market value of a portfolio over a specified time horizon at given confidence levels. For internal risk management purposes, the Group's VaR assumes a time horizon of one trading day and confidence level of 99% as it is considered that this provides greater clarity in respect of more severe potential economic outcomes. The Group's VaR model is based on a historical simulation model utilising data from the previous two years' trading results.

The VaR disclosure is broken down into trading and non-trading, where trading VaR relates to the trading activities and non-trading reflects the VaR associated with reclassified assets, money market business and the management of internal funds flow within the Group's businesses.

The Group calculates VaR using historical simulation models but does not make any assumption about the nature or type of underlying loss distribution other than implied by history. The methodology uses the previous 500 trading days of market data and calculates both general market risk (the risk due to movement in general market benchmarks) and idiosyncratic market risk (the risk due to movements in the value of securities by reference to specific issuers). The Group VaR should be interpreted in light of the limitations of the methodology used as follows:

- Historical simulation VaR may not provide the best estimate of future market movements. It can only provide a prediction of the future based on events that occurred in the time series horizon. Therefore, events that are more severe than those in the historical data series cannot be predicted;
- VaR that uses a 99% confidence level does not reflect the extent of potential losses beyond that percentile;
- VaR that uses a one-day time horizon will not fully capture the profit or loss implications of positions that cannot be liquidated or hedged within one day; and
- The Group computes the VaR of trading portfolios and non-trading money markets portfolio at the close of business. Treasury Interest Rate Risk VaR is computed monthly.

A 'Risks not in VaR' framework has been developed to address those market risks not adequately captured by the market standard VaR methodology. Where risks are not included in the model, various non-VaR controls (for example, position monitoring, sensitivity limits, triggers or stress limits) are in place. These limitations mean that the Group cannot guarantee that losses will not exceed the VaR.

(i) Trading Portfolios

The Group eliminates its market risk in these portfolios by entering into back-to-back positions with its ultimate parent company, The Royal Bank of Scotland Group plc.

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NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – market risk (continued)

(ii) Non-trading

The principal market risks arising from the Group's non-trading activities are interest rate risk and currency risk. Non-trading risk is managed by both the Money Market Desk and Treasury, and arises from mismatches between the repricing of assets and liabilities in its wholesale markets, retail business and corporate bank.

Total VaR

The short term markets and financing (STMF) desk is responsible for raising funding in the international wholesale and repo markets and funding the corporate loan book.

The total VaR for the Group's dealing is presented in the table below:

	31 December 2012 £m	Maximum £m	Minimum £m	Average £m
Value-at-Risk	0.4	1.3	0.3	0.6
	31 December 2011 £m	Maximum £m	Minimum £m	Average £m
Value-at-Risk	0.8	1.1	0.4	0.7

Interest Rate VaR

The Interest Rate VaR limit is a sub limit of the Total VaR limit and is monitored daily.

Interest Rate VaR is presented in the table below:

	31 December 2012 £m	Maximum £m	Minimum £m	Average £m
Value-at-Risk	0.4	1.3	0.3	0.7
	31 December 2011 £m	Maximum £m	Minimum £m	Average £m
Value-at-Risk	0.8	1.0	0.3	0.6

Treasury interest rate risk

The Group's portfolio of non-trading financial instruments principally comprises retail and commercial banking loans and deposits, debt securities issued, capital and hedging instruments.

Non-trading interest rate risk is calculated on the basis of establishing the repricing behaviour of each asset, liability and off-balance sheet product. For many products, the actual interest rate repricing characteristics differ from the contractual repricing. In most cases, the repricing maturity is determined by the market interest rate that most closely fits the historical behaviour of the product interest rate. For example with non-interest bearing current accounts, the repricing maturity is determined by the stability of the portfolio. The repricing maturities used are approved by RBS Group Treasury and the Ulster Bank Asset and Liability Committee (ALCO) at least annually. Key conventions are reviewed annually by ALCO. Short-term exposures are reviewed in terms of net interest income sensitivity over 12 months to a 1% parallel movement in interest rates. Risk is managed through arm's length cash transactions, bonds and derivatives, principally interest rate swaps.

A static maturity gap report is produced as at the month-end, in each functional currency based on the behaviouralised repricing for each product. It is Group policy to include in the gap report non-financial assets and liabilities, mainly property, plant and equipment and the Group's capital and reserves, spread over medium and longer term maturities. This report also includes hedge transactions, principally derivatives.

Any residual non-trading interest rate exposures are controlled by limiting repricing mismatches in the balance sheets. Potential exposures to interest rate movements in the medium to long term are measured and controlled using a version of the same VaR methodology that is used for the Group's trading portfolios but without discount factors. Net accrual income exposures are measured and controlled in terms of sensitivity over time to movements in interest rates.

Risk is managed within VaR limits approved by ALCO through the execution of cash and derivative instruments. Execution of the hedging is carried out by the relevant division through the Group's Treasury function. The residual risk position is reported to ALCO and RBS Group Treasury on a monthly basis.

Non-trading interest rate VaR is split between Euro and Sterling currency balances to which separate risk limits are applied. At 31 December 2012, Sterling VaR was calculated to be £175,000 (2011: £362,000). Euro VaR was calculated to be £203,000 (2011: £388,000).

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – market risk (continued)

Treasury interest rate risk (continued)

Principal amounts only are included. Average balances are used for products where this is considered to provide a more accurate representation of the exposure. A separate ladder is produced for each material currency.

Option risk in the non-trading businesses principally occurs in certain fixed rate assets and liabilities. It arises where businesses undertake to provide funding to, or to accept deposits from, customers at a future date at a pre-determined fixed interest rate. Derivatives are used to manage the risk of interest rate movements from the date a commitment is made to a customer to the date the transaction closes. Option risk also arises where customers can repay fixed rate loans or withdraw fixed rate deposits prior to their maturity. In managing this risk, historic early repayment rates are taken into account.

The Group generally seeks to protect itself from early repayment risk through the imposition of contract breakage fees.

Foreign Exchange Risk in the Banking Book represents exposures to changes in the values of current holdings and future cash flows denominated in other currencies. Hedging instruments used to mitigate these risks include foreign currency options, currency swaps, futures, forwards and deposits. Foreign exchange risk results from the Group's investments in overseas subsidiaries, associates and branches in three principal forms:

- Structural foreign currency exposures that arise from net investment in overseas subsidiaries, associates and branches;
- Transactional/commercial foreign currency exposures that arise from mismatches in the currency balance sheet; and
- Foreign currency profit streams.

The Group does not maintain material non-trading open currency positions other than the structural foreign currency translation exposures arising from its investments in foreign subsidiaries and associated undertakings and their related currency funding. The Group's policy in relation to structural positions is to match fund the structural foreign currency exposure arising from net asset value, including goodwill, in foreign subsidiaries, equity accounted investments and branches, except where doing so would materially increase the sensitivity of either the Group's or the subsidiary's regulatory capital ratios to currency movements. The policy requires structural foreign exchange positions to be reviewed regularly by ALCO.

Foreign exchange differences arising on the translation of foreign operations are recognised directly in equity together with the effective portion of foreign exchange differences arising on hedging liabilities.

The table below sets out the Group's structural foreign currency exposures as at 31 December 2012:

2012						
	Net assets of overseas investment £m	Minority interest £m	Net investments £m	Currency borrowings £m	Economic hedges £m	Structural foreign currency exposures £m
Euro	6,767	(20)	6,747	(408)	(1,624)	4,715
2011						
	Net assets of overseas investment £m	Minority interest £m	Net investments £m	Currency borrowings £m	Economic hedges £m	Structural foreign currency exposures £m
Euro	6,112	(23)	6,089	(418)	(1,667)	4,004

At 31 December 2012, a 5% strengthening of foreign currencies would result in a structural foreign currency gain of £235 million in equity (2011: £196m gain) and a 5% weakening of foreign currencies would result in a structural foreign currency loss of £235 million in equity (2011: £196m loss).

Changes in foreign exchange rates affect the Group's earnings and equity through differences on the retranslation of the net assets and related funding of overseas subsidiaries from the local functional currency to Sterling. Gains or losses on foreign currency investments in subsidiary and associated undertakings, net of any losses or gains on related foreign currency funding, are recognised in reserves. In 2012 exchange losses of £145m (2011: £241m) have been charged to reserves.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management (continued)

Liquidity Risk

Safety and soundness of the balance sheet is one of the central pillars of the Group's restructuring strategy. The Group's ability to serve customers well and create value for shareholders is being built upon the foundations of a solid and strong balance sheet. Effective management of liquidity risk is central to the safety and soundness agenda.

Liquidity risk is the risk that the Group is unable to meet its financial obligations, including financing wholesale maturities or customer deposit withdrawals as and when they fall due. Liquidity risk is highly dependent on company specific characteristics such as the maturity profile and composition of the Group's asset and liabilities, the quality and marketable value of its liquidity buffer and broader market factors, such as wholesale market conditions alongside depositor and investor behaviour.

The Group has in place a comprehensive set of policies to manage liquidity risk that reflected best market practice and complies with prevailing regulatory strictures. These policies have been comprehensively updated since 2008, reflecting:

- the Group's restructuring plan,
- regulatory developments and enhancements,
- ongoing instability in global financial markets, and
- more conservative expectations from the Group's various stakeholders.

These policies are designed to address three broad issues which ensure that:

- the Group maintains adequate liquidity resources to meet liabilities as and when they fall due;
- the Group maintains an adequate liquidity buffer appropriate to the business activities of the Group and their risk profile; and
- the Group has in place robust strategies, policies, systems and procedures for identifying, measuring, monitoring and managing liquidity risk.

At its simplest these policies determine the sources of liquidity risk and the steps the Group can take when these risks exceed certain tolerances. These include not only when and how to use the Group's liquidity buffer but also what other adjustments to the Group's balance sheet could be undertaken to manage these risks back within Group appetite. These policies are reviewed at least annually or sooner if the Group's own liquidity position changes or if market conditions and/or regulatory rules warrant further amendment or refinement.

Policy, framework and governance

The Group has in place a robust and comprehensive set of policies and procedures for assessing, measuring and managing the liquidity risk within the Group. This ensures that the Group always maintain sufficient eligible and appropriate financial resources to meet its forward looking financial commitments as they fall due.

ALCO is responsible for defining and approving the Group's liquidity policy and setting acceptable parameters and risk limits that align with the overall RBS Group standard and risk appetite. The Group's liquidity buffer is managed by the Treasury function who monitor and control the Group's funding and liquidity position.

Similar provisions and requirements exist for each entity within the Group, whereby they must comply with both internal standards and local regulatory frameworks.

Regulatory oversight

The Group operates in both the United Kingdom and the Republic of Ireland and is subject to regulatory oversight in both jurisdictions. The Group's lead regulator is the FSA. The FSA implemented a new liquidity regime on 1 June 2010. The new rules provide a standardised approach applied to all UK banks. At the RBS Group, the rules focus on the UK Defined Liquidity Group (a subset comprising the Group's five UK banks, The Royal Bank of Scotland plc, National Westminster Bank Plc, Ulster Bank Limited, Coutts & Co and Adam & Co) and cover adequacy of liquidity resources, controls, stress testing and the Individual Liquidity Adequacy Assessment (ILAA). The ILAA informs the Group Board and the FSA of the assessment and quantification of the Group's liquidity risks and their mitigation, and how much current and future liquidity is required. In the Republic of Ireland, the Group's operations must meet liquidity requirements set out by the Central Bank of Ireland.

Liquidity Measurement and Monitoring

Liquidity risk is measured and assessed on a daily basis at the RBS Group level in compliance with requirements laid out by the FSA. The Group use a set of internal metrics and analysis to assess liquidity risk.

The Group uses limits to manage and control the overall extent of liquidity risk within the balance sheet. Limits will

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management - liquidity risk (continued)

Liquidity Measurement and Monitoring (continued)

focus on the aggregate amount and composition of particular sources of liabilities, asset liability mismatches and third party counterparty concentrations.

As further described herein, stress testing is used to help inform a broader understanding of liquidity risk as well as to model specific liquidity risk events; for example the secession of a country from the Euro.

The Group actively monitors a range of market and firm specific indicators on an ongoing basis which are designed to act as early warning indicators that liquidity stresses are emerging. Some of these indicators will be based upon actual performance of the business against pre-agreed limits, for example customer deposit outflows. Others will be based around general or specific market movements.

Liquidity risk performance reports are reviewed by ALCO. Any breach or material deterioration of these metrics will set in motion a series of actions and escalations.

The Group's liquidity risk framework is subject to internal oversight, challenge and governance both at Board level and via internal control functions such as Internal Audit. The Group is also subject to regulatory review and challenge.

Stress testing

In determining the adequacy of the Group's liquidity resources as part of the RBS Group UK Defined Liquidity Group, the Group evaluates its ability to survive when subjected to simulated stress conditions.

Simulated liquidity stress testing is regularly performed. Stress tests are designed to look at the impact of a variety of firm-specific and market-related scenarios on the adequacy of the Group's liquidity resources at various points in time. Stress tests can therefore be run on an ad hoc basis in response to the emergence of one of these risks.

Scenarios include assumptions about significant changes in key funding sources, external credit ratings, contingent uses of funding and political and economic conditions or events in particular countries. Stress scenarios are applied to both on-balance sheet instruments and off-balance sheet activities to provide a comprehensive view of potential cash flows.

In determining the adequacy of the Group's liquidity resources the Group focuses on the stressed outflows it could anticipate experiencing as a result of any stress scenario occurring. These outflows are measured as occurring over certain time periods which extend from any given day, out to two weeks or to as long as three months. The Group is expected to be able to withstand these stressed outflows through its own resources (principally the use of the liquidity buffer) over these time horizons without having to revert to extraordinary central bank or governmental assistance.

Stress tests are augmented from time to time to reflect firm specific or emerging market risks that could have a material impact on the Group's liquidity position.

The results of stress testing are an active part of management and strategy in balance sheet management and inform allocation, target and limit discussions. In short, limits in the business-as-usual environment are bounded by capacity to satisfy the Group's liquidity needs in the stress environments.

Funding risk

Balance sheet composition

The Group's balance sheet composition is a function of the broad array of product offerings and diverse markets served. The structural composition of the balance sheet is enhanced as needed through active management of both asset and liability portfolios. The objective of these activities is to optimise liquidity transformation in normal business environments, while ensuring adequate coverage of all cash requirements under extreme stress conditions.

The Group also accesses professional markets funding by way of public and private debt issuances on an unsecured and secured basis. These debt issuance programmes are spread across multiple currencies and maturities, to appeal to a broad range of investor types and preferences around the world. This market-based funding supplements the Group's structural liquidity needs and, in some cases, achieves certain capital objectives.

The Group is part of the RBS Group and receives ongoing capital, funding and liquidity resources which, coupled with other sources of funding and liquidity, enable the Group to meet its obligations as they fall due. Other sources of funding and liquidity include retail, wholesale and central bank liquidity facilities.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – liquidity risk (continued)

Balance sheet composition (continued)

The tables below analyse the contractual undiscounted cash flows receivable and payable up to a period of twenty years including future receipts and payments of interest on the balance sheet items by contractual maturity. The balances in the tables below do not agree directly to the Group or Bank balance sheet as the tables include all cash flows relating to principal and future coupon payments presented on an undiscounted basis.

	Group					
	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
2012						
Assets by contractual maturity						
Cash and balances at central banks	725	-	-	-	-	-
Loans and advances to banks	5,992	111	1,079	1,007	-	-
Debt securities	-	-	-	-	1	2
Finance leases	8	21	32	7	1	-
Total maturing assets	6,725	132	1,111	1,014	2	2
Loans and advances to customers	3,240	8,522	5,241	3,842	7,326	11,496
Total assets	9,965	8,654	6,352	4,856	7,328	11,498
Liabilities by contractual maturity						
Deposits by banks	5,005	13	2,885	2	2	-
Debt securities in issue	20	12	6	-	-	-
Subordinated liabilities	-	63	41	-	981	-
Other liabilities	580	89	-	-	-	-
Total maturing liabilities	5,605	177	2,932	2	983	-
Customer accounts	16,267	4,742	1,500	559	160	-
Total liabilities	21,872	4,919	4,432	561	1,143	-
Maturity gap	(11,907)	3,735	1,920	4,295	6,185	11,498
Cumulative maturity gap	(11,907)	(8,172)	(6,252)	(1,957)	4,228	15,726
	Group					
	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
2011						
Assets by contractual maturity						
Cash and balances at central banks	749	-	-	-	-	-
Loans and advances to banks	5,132	306	1,093	780	20	-
Debt securities	15	1	19	1	4	15
Finance leases	-	2	5	1	-	-
Total maturing assets	5,896	309	1,117	782	24	15
Loans and advances to customers	5,107	8,105	6,531	4,275	8,483	13,082
Total assets	11,003	8,414	7,648	5,057	8,507	13,097
Liabilities by contractual maturity						
Deposits by banks	11,086	17	1,712	16	3	-
Debt securities in issue	8	36	15	-	-	-
Subordinated liabilities	-	4	81	20	586	234
Other liabilities	552	-	-	-	-	-
Total maturing liabilities	11,646	57	1,808	36	589	234
Customer accounts	15,477	4,452	1,970	453	187	-
Total liabilities	27,123	4,509	3,778	489	776	234
Maturity gap	(16,120)	3,905	3,870	4,568	7,731	12,863
Cumulative maturity gap	(16,120)	(12,215)	(8,345)	(3,777)	3,954	16,817

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – liquidity risk (continued)

2012	Bank					
	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
Assets by contractual maturity						
Cash and balances at central banks	545	-	-	-	-	-
Loans and advances to banks	4,437	111	1,079	1,007	420	-
Debt securities	-	-	-	-	1	2
Total maturing assets	4,982	111	1,079	1,007	421	2
Loans and advances to customers	1,446	1,312	851	489	1,122	1,526
Total assets	6,428	1,423	1,930	1,496	1,543	1,528
Liabilities by contractual maturity						
Deposits by banks	2,801	2	1,737	-	-	-
Debt securities in issue	-	-	3	-	-	-
Subordinated liabilities	-	-	40	-	899	-
Other liabilities	574	80	-	-	-	-
Total maturing liabilities	3,375	82	1,780	-	899	-
Customer accounts	5,146	1,543	349	144	26	-
Total liabilities	8,521	1,625	2,129	144	925	-
Maturity gap	(2,093)	(202)	(199)	1,352	618	1,528
Cumulative maturity gap	(2,093)	(2,295)	(2,494)	(1,142)	(524)	1,004
2011	Bank					
	0-3 months £m	3-12 months £m	1-3 years £m	3-5 years £m	5-10 years £m	10-20 years £m
Assets by contractual maturity						
Cash and balances at central banks	522	-	-	-	-	-
Loans and advances to banks	3,986	313	1,260	789	128	364
Debt securities	7	1	1	1	4	7
Total maturing assets	4,515	314	1,261	790	132	371
Loans and advances to customers	1,515	1,654	909	493	1,263	1,566
Total assets	6,030	1,968	2,170	1,283	1,395	1,937
Liabilities by contractual maturity						
Deposits by banks	2,671	-	1,693	-	-	-
Debt securities in issue	8	30	-	-	-	-
Subordinated liabilities	-	-	20	20	586	235
Other liabilities	552	-	-	-	-	-
Total maturing liabilities	3,231	30	1,713	20	586	235
Customer accounts	5,399	1,053	918	145	47	-
Total liabilities	8,630	1,083	2,631	165	633	235
Maturity gap	(2,600)	885	(461)	1,118	762	1,702
Cumulative maturity gap	(2,600)	(1,715)	(2,176)	(1,058)	(296)	1,406

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – liquidity risk (continued)

Other contractual cash obligations

2012	Group					
	0–3 months £m	3–12 months £m	1–3 years £m	3–5 years £m	5–10 years £m	10–20 years £m
Operating leases	5	16	39	33	41	20
Contractual obligations to purchase goods or services	1	2	4	-	-	-
	6	18	43	33	41	20

2011	Group					
	0–3 months £m	3–12 months £m	1–3 years £m	3–5 years £m	5–10 years £m	10–20 years £m
Operating leases	6	17	43	39	65	28
Contractual obligations to purchase goods or services	1	3	4	-	-	-
	7	20	47	39	65	28

2012	Bank					
	0–3 months £m	3–12 months £m	1–3 years £m	3–5 years £m	5–10 years £m	10–20 years £m
Operating leases	1	2	3	2	2	2
Contractual obligations to purchase goods or services	-	1	2	-	-	-
	1	3	5	2	2	2

2011	Bank					
	0–3 months £m	3–12 months £m	1–3 years £m	3–5 years £m	5–10 years £m	10–20 years £m
Operating leases	1	2	3	2	2	2
Contractual obligations to purchase goods or services	-	1	2	-	-	-
	1	3	5	2	2	2

Financial assets have been reflected in the time band of the latest date on which they could be repaid unless earlier repayment can be demanded by the Group; financial liabilities are included at the earliest date on which the counterparty can require repayment regardless of whether or not such early repayment results in a penalty.

If the repayment of a financial asset or liability is triggered by, or is subject to, specific criteria such as market price hurdles being reached, the asset is included in the latest date on which it can repay regardless of early repayment whereas the liability is included at the earliest possible date that the conditions could be fulfilled without considering the probability of the conditions being met. For example, if a structured note is automatically prepaid when an equity index exceeds a certain level, the cash outflow will be included in the less than three months period whatever the level of the index at the year end. The settlement date of debt securities in issue issued by certain securitisation vehicles consolidated by the Group depends on when cash flows are received from the securitised assets. Where these assets are prepayable, the timing of the cash outflow relating to securities assumes that each asset will be prepaid at the earliest possible date. As the repayment of assets and liabilities are linked, the repayment of assets in securitisations are shown on the earliest date that the asset can be prepaid as this is the basis used for liabilities.

The principal amounts of financial assets and liabilities that are repayable after 20 years or where the counterparty has no right to repayment of the principal are excluded from the table as are interest payments after 20 years.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management (continued)

Credit risk

Credit risk is the risk of financial loss due to the failure of a customer to meet its obligation to settle outstanding amounts. The credit risk that the Group faces arises mainly from wholesale and retail lending, provision of contingent obligations (such as letters of credit and guarantees) and counterparty credit risk arising from derivative contracts entered into with customers. Other material risks covered by the Group's credit risk management framework are:

- *Concentration risk* - The risk of an outsized loss due to the concentration of credit risk to a specific asset class or product, industry sector, customer or counterparty, or country.
- *Settlement risk* - The intra-day risk that arises where the Group releases funds prior to confirmed receipt of value from a third party.
- *Issuer risk* - The risk of loss on a tradable instrument (e.g. bond, equity or synthetic instrument such as a credit default swap) due to default by the issuer.
- *Wrong way risk* - The risk of loss that arises when the risk factors driving the exposure to a counterparty are positively correlated with the probability of default for that counterparty.
- *Credit mitigation risk* - The risk that credit risk mitigation is not enforceable or that the value of such mitigation decreases, thereby leading to unanticipated losses.

Objectives, organisation and governance

The existence of a strong credit risk management function is vital to support the ongoing profitability of the Group. The potential for loss through economic cycles is mitigated through the embedding of a robust credit risk culture within the business units and through a focus on the importance of sustainable lending practices. The role of the credit risk management function is to own the credit approval, concentration and credit risk control frameworks and to act as the ultimate authority for the approval of credit. This, together with strong independent oversight and challenge, enables the business to maintain a sound lending environment within risk appetite.

Responsibility for development of RBS Group-wide policies, credit risk frameworks, RBS Group-wide portfolio management and assessment of provision adequacy resides with the Group Credit Risk (GCR) function under the management of the Group Chief Risk Officer. Responsibility for application of these policies within the Group resides with the Group Chief Risk Officer.

Ulster Bank Credit Risk ("UBCR") works together with GCR to ensure that the expressed risk appetite is met, within a clearly defined and managed control environment. UBCR operates under the management of the Group Chief Risk Officer.

Material aspects of the Group's credit risk management framework, such as credit risk appetite and limits for portfolios of strategic significance, are considered and approved by the Executive Risk Forum (ERF). The ERF has delegated authority to the Group Credit Risk Committee, a functional sub-committee of Group Risk Committee, to act on credit risk matters. These include, but are not limited to, credit risk appetite and limits (within the overall risk appetite set by the Board and the ERF), credit risk strategy and frameworks, credit risk policy and the oversight of the credit profile across the Group.

The FSA has highlighted the shortcomings of the Commercial Real Estate models used by all UK regulated entities. It has advised the Group to adopt the "Specialised Lending" approach to determine capital requirements. This approach was introduced during the year and is due to be fully embedded by the end of 2013.

Credit risk management framework

The Group has established an appropriate and comprehensive framework for the management of credit risk that includes governance structures, risk appetite and concentration frameworks, policies, measurement and reporting tools and independent assurance.

In order to strengthen this framework and ensure consistent application, risk appetite statements and a set of credit control standards were launched to supplement the existing policy suite. These standards address divisional governance and policy requirements and reflect a set of behavioural, organisational and management norms that will drive a sound control environment and embed a strong risk culture.

Risk appetite and concentration risk management

Risk appetite has been expressed by the Board through the setting of specific quantitative risk appetite targets under stress. Of particular relevance in the management of credit risk are the targets for earnings volatility and capital adequacy. The Group's credit risk framework has therefore been designed around the factors that influence the Group's ability to meet these targets. These include the limiting of excess credit risk concentrations which generate higher volatility under stress and, if not adequately controlled, can undermine capital adequacy.

The Group's credit concentration frameworks are designed to limit concentration by product/asset class, industry

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

Risk appetite and concentration risk management (continued)

sector, customer or counterparty (i.e. single name) and country.

The frameworks are supported by a suite of policies that set out the risk parameters within which business units may operate.

The management of concentration risk and associated limits are now firmly embedded in the risk management processes of the Group and form a pivotal part of the Risk function's engagement with the businesses on the appropriateness of risk appetite choices. In the three years since the new concentration frameworks were rolled out across the Group, UBCR has reviewed all material industry and product portfolios and agreed a risk appetite commensurate with the franchises represented in these reviews. In particular, limits have been reviewed and re-sized, to refine the Group's risk appetite in areas where it faces significant balance sheet concentrations or franchise challenges.

Notwithstanding the need for the Group to control credit risk volatility, the Group's businesses and credit functions pay careful consideration to the need to ensure sufficient capacity within credit limits to support customers of sound credit quality, in particular within retail and small business customer segments.

During 2012, the Group expanded the scope of its credit risk appetite controls through the active management of non-financial risks in the Group's lending decisions. The development of Environmental, Social and Ethical (ESE) risk policies for sectors considered to present a higher reputational risk allow the Group to manage its reputational risks. The policies set the Group's reputational risk appetite for clients operating in higher-risk sectors and help to shape wider sector management strategies. The ESE framework forms part of a wider initiative by the Group to improve reputational risk management and build trust with its stakeholders (for more information on reputational risk management, refer to page 76).

Product/asset class

- **Retail** - A formal framework establishes Group-level statements and thresholds that are cascaded to all business lines. These include measures that relate both to aggregate portfolios and to asset quality at origination, which are tracked frequently to ensure consistency with Group standards and appetite. This appetite setting and tracking then informs the processes and parameters employed in origination activities, which require a large volume of small-scale credit decisions, particularly those involving an application for a new product or a change in facilities on an existing product. The majority of these decisions are based upon automated strategies utilising credit and behaviour scoring techniques. Scores and strategies are typically segmented by product, brand and other significant drivers of credit risk. These data-driven strategies utilise a wide range of credit information relating to a customer including, where appropriate, information across customer holdings. A small number of credit decisions are subject to additional manual underwriting by authorised approvers in specialist units. These include higher-value, more complex, small business and personal unsecured transactions and some residential mortgage applications.
- **Wholesale** - Formal policies, specialised tools and expertise, tailored monitoring and reporting and, in certain cases, specific limits and thresholds are deployed to address certain lines of business across the Group, where the nature of credit risk incurred could represent a concentration or a specific/heightened risk in some other form. Those portfolios identified as potentially representing a concentration or heightened risk are subject to formal governance, including periodic review.

Sector concentration

Across wholesale portfolios, exposures are assigned to, and reviewed in the context of, a defined set of industry sectors. Through this sector framework, appetite and portfolio strategies are agreed and set at aggregate and more granular levels, where exposures have the potential to represent excessive concentration or where trends in both external factors and internal portfolio performance give cause for concern. Formal periodic reviews are undertaken, depending on materiality, these may include an assessment of the Group's franchise in a particular sector, an analysis of the outlook (including downside outcomes), identification of key vulnerabilities and stress/scenario tests.

The focus during 2012 was on embedding sector and sub-sector specific appetite and on setting appropriate controls. This includes strengthening portfolio controls on key metrics and lending parameters, and the ongoing development of sector-specific lending policies.

Single-name concentration

Within wholesale portfolios, much of the activity undertaken by the credit risk function is organised around the assessment, approval and management of the credit risk associated with a borrower or group of related borrowers.

A formal single name concentration framework addresses the risk of outsized exposure to a borrower or borrower

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23. Risk management – credit risk (continued)

Single-name concentration (continued)

group. The framework includes specific and sometimes elevated approval requirements, additional reporting and monitoring, and the requirement to develop plans to address and reduce excess exposures over an appropriate timeframe.

Credit approval authority is discharged by way of a framework of individual delegated authorities, which requires at least two individuals to approve each credit decision, one from the business and one from the credit risk management function. Both parties must hold sufficient delegated authority under the Group-wide authority grid. While both parties are accountable for the quality of each decision taken, the credit risk management approver holds ultimate sanctioning authority. The level of authority granted to individuals is dependent on their experience and expertise, with only a small number of senior executives holding the highest authority provided under the framework. Daily monitoring of individual counterparty limits is undertaken.

At a minimum, credit relationships are reviewed and re-approved annually. The renewal process addresses: borrower performance, including reconfirmation or adjustment of risk parameter estimates; the adequacy of security; and compliance with terms and conditions. For certain counterparties, early warning indicators are also in place to detect deteriorating trends in limit utilisation or account performance, and to prompt additional oversight.

Since 2009, the Group has been managing its corporate exposures to reduce concentrations and align its appetite for future business to the Group's broader strategies for its large corporate franchises. The Group is continually reviewing its single name concentration framework to ensure that it remains appropriate for current economic conditions and in line with improvements in the Group's risk measurement models.

In 2012, the Group implemented further refinements to the single name exposure management controls already in place, which brings them more closely in line with market best practice and which allows the Group to differentiate more consistently between the different risk types.

Country

Country risk arises from sovereign events (for example, default or restructuring); economic events (for example, contagion of sovereign default to other parts of the economy, cyclical economic shock); political events (for example, convertibility restrictions and expropriation or nationalisation); and natural disaster or conflict. Such events have the potential to impact elements of the Group's credit portfolio that are directly or indirectly linked to the affected country and can also give rise to market, liquidity, operational and franchise risk related losses. Sovereign risk is discussed on page 77.

Global Restructuring Group (GRG)

GRG manages problem and potential problem exposures in the Group's wholesale credit portfolios. Its primary function is to actively manage the exposures to minimise loss for the Group and, where feasible, to return the exposure to the Group's mainstream loan book.

Originating business units consult with GRG prior to transferring exposures to it when a potentially negative event or trend emerges that might affect a customer's ability to service its debt or increase the Group's risk exposure to that customer. Such circumstances include deteriorating trading performance, likely breach of covenant, challenging macroeconomic conditions, a missed payment or the expectation of a missed payment to the Group or another creditor.

On transfer of the relationship, GRG aim to devise a bespoke strategy that optimises recoveries from the debt. This strategy may also involve GRG reviewing the business operations and performance of the customer. A number of alternative approaches will typically be considered including:

- **Covenant relief:** the temporary waiver or recalibration of covenants may be granted to mitigate a potential or actual covenant breach. Such relief is usually granted in exchange for fees, increased margin, additional security, or a reduction in maturity profile of the original loan.
- **Amendment of restrictive covenants:** restrictions in loan documents may be amended or waived as part of an overall remedial strategy to allow: additional indebtedness; the granting of collateral; the sale of a business; the granting of junior lien on the collateral; or other fundamental change in capital or operating structure of the enterprise.
- **Variation in margin:** contractual margin may be amended to bolster the customer's day-to-day liquidity, with the aim of helping to sustain the customer's business as a going concern. This would normally be accompanied by the Group receiving an exit payment, payment in kind or deferred fee.

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23. Risk management – credit risk (continued)

- *Payment holidays and loan rescheduling:* payment holidays or changes to the contracted amortisation profile including extensions in contracted maturity or roll-overs may be granted to improve customer liquidity. Such concessions often depend on the expectation that liquidity will recover when market conditions improve or from capital raising initiatives that access alternative sources of liquidity. Recently, these types of concessions have become more common in commercial real estate transactions in situations when a shortage of market liquidity rules out immediate refinancing and makes short-term forced collateral sales unattractive
- *Forgiveness of all or part of the outstanding debt:* debt may be forgiven or exchanged for equity where a fundamental shift in the customer's business or economic environment means that other forms of restructuring strategies are unlikely to succeed in isolation and the customer is incapable of servicing current debt obligations. Debt forgiveness is often an element in leveraged finance transactions which are typically structured on the basis of projected cash flows from operational activities rather than underlying tangible asset values. Maintaining the business as a going concern with a sustainable level of debt is the preferred option rather than realising value of the underlying assets, provided that the underlying business model and strategy are considered viable.

Depending on the case in question, GRG may employ a combination of these options in order to achieve the best outcome. It may also consider alternative approaches, either alone or together with the options listed above.

The following are generally considered as options of last resort:

- *Examinership:* In the Republic of Ireland in a limited number of cases the option of examinership may prove to be effective in delivering a restructuring under the protection of the courts where a decision of multiple creditor groups is required.
- *Enforcement of security or otherwise taking control of assets:* where the Group holds underlying collateral or other security interest and is entitled to enforce its rights, it may take ownership or control of the assets. The Group's preferred strategy is to consider other possible options prior to exercising these rights.
- *Insolvency:* where there is no suitable restructuring option or the business is no longer regarded as sustainable, insolvency will be considered. Insolvency may be the only option that ensures that the assets of the business are properly and efficiently distributed to relevant creditors.

As discussed above, GRG will consider a range of possible restructuring strategies. At the time of execution, the ultimate outcome of the strategy adopted is unknown and highly dependent on the cooperation of the borrower and the continued existence of a viable business. The customer's financial position, its anticipated future prospects and the likely effect of the restructuring including any concessions are considered by the GRG relationship manager to establish whether an impairment provision is required, subject to divisional and Group governance.

Retail collections and recoveries

There are collections and recoveries functions in each of the consumer businesses. Their role is to provide support and assistance to customers who are currently experiencing difficulties meeting their financial obligations. Where possible, the aim of the collections and recoveries teams is to return the customer to a satisfactory position, by working with them to restructure their finances. If this is not possible, the team has the objective of reducing the loss to the Group.

Forbearance

Within the Group's retail businesses, forbearance generally occurs when the business, for reasons relating to the actual or potential financial stress of a borrower, grants a permanent or temporary concession to that borrower. Forbearance is granted principally to customers with mortgages. Granting of forbearance to unsecured customers is less extensive.

Mortgage Arrears Resolution Strategies ("MARS") is a CBI sponsored initiative for all banks in the Republic of Ireland that aims to increase the level of engagement and options available to mortgage customers in financial difficulty. Ulster Bank Ireland Limited started to develop new MARS contact strategies and treatments in September 2011 and presented for approval to the Board in October 2012. The MARS strategies went live in December 2012.

Identification of forbearance

Mortgages are identified for forbearance treatment following initial contact from the customer, in the event of payment arrears or when the customer is transferred to collections or recoveries.

Forbearance is granted following an assessment of the customer's ability to pay. Customers receiving these types of treatment whilst in collections or recoveries are typically showing signs of financial difficulties. Within the Group, requests by customers for an amendment to their contractual terms whilst they are fully up-to-date with payments are considered to be a potential impairment indicator.

Types of retail forbearance

A number of forbearance options are utilised by the Group's retail businesses. These include, but are not limited to, reduced repayments, payment holidays, capitalisation of arrears, term extensions and temporary conversions to interest only.

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NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

For those loans classified as non-performing, the Group's objective in granting forbearance is to minimise the loss on these accounts and, wherever possible, return the customer to a performing state. The Group's aim is to enable customers who are current on their payments to continue to service the loan.

The mortgage forbearance population is reviewed regularly to ensure that customers are meeting the agreed terms of the arrangement. Key metrics have been developed to record the proportion of customers who fail to meet the agreed terms over time as well as the proportion of customers who return to a performing state with no arrears.

The mortgage arrears information for retail accounts in forbearance and related provisions are shown in the table below:

Arrears status and provisions	2012		2011	
	Balance	Provisions	Balance	Provisions
	£m	£m	£m	£m
No missed payments	915	100	893	78
1-3 months in arrears	546	60	516	45
>3 months in arrears	527	194	421	124
Total	1,988	354	1,830	247

The incidence of the main types of retail forbearance on the balance sheet as at 31 December 2012 is analysed below. Definitions are based on those used within the Financial Services Authority forbearance guidelines. For a small proportion of mortgages, more than one forbearance type applies.

	2012	2011
	£m	£m
Interest only	924	795
Term extensions – capital repayment & interest only	183	58
Payment concession/holidays	762	876
Capitalisation of arrears	119	101
Total	1,988	1,830
% of total mortgage stock	10.4	9.1

Provisioning for retail customers

Provisions are assessed in accordance with the Group's provisioning policies which comply with IAS 39 'Financial Instruments: Recognition and Measurement' (refer to section on provision methodology on page 65). For the non-performing population, a collective assessment is made. Within the performing book, latent loss provisions are held for those loans that are impaired but not yet identified.

The majority of mortgage accounts subject to forbearance remains in the performing book but these accounts are identified and monitored separately from other performing accounts. They are subject to higher provisioning rates than the remainder of the performing book (currently approximately eight times higher). These rates are reviewed monthly. Once forbearance is granted, the account continues to be assessed separately for latent provisioning until the forbearance period expires. After that point, the account is no longer separately identified for latent provisioning. Non-performing mortgage accounts that have been granted forbearance carry the same provision rate as non-forborne accounts.

Controls and assurance

The Group's credit control and assurance framework comprises three key components: credit policy, policy compliance assurance and independent assurance.

The foundation is the RBS Group Credit Policy Standard, which as part of the Group Policy Framework ("GPF"), sets out the rules the Group's businesses must follow to ensure that credit risks are identified and effectively managed through the credit lifecycle. During 2012, a major revision of the RBS Group's key credit policies was completed. This revision has provided support in ensuring that the Group's control environment is appropriately aligned to the approved risk appetite, and provides a sound basis for the Group's independent audit and assurance activities across the credit risk function.

The second component is a policy assurance activity that GCR undertakes to provide the Group Chief Credit Officer with evidence of the effectiveness of the controls in place across the Group to manage credit risk. The results of these reviews are presented to the Group Credit Risk Committee on a regular basis in support of the self-certification that GCR is obliged to complete under the GPF.

Lastly, a strong independent assurance function is an important element of a sound control environment. During 2011,

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NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

the RBS Group took the decision to strengthen its Credit Quality Assurance (CQA) activities and moved all divisional CQA resources under the centralised management of GCR. The benefits of this action are already apparent in greater consistency of standards and cross-utilisation of resources, ensuring that subject matter experts bring their expertise to bear where relevant.

Reviews undertaken consistently address the four underlying risk pillars of: risk management, risk appetite, ratings and data integrity, and asset quality. Appropriate identification, escalation, remediation and related tracking of control breaches and improvements in operational processes are firmly embedded in the assurance process to ensure that divisions act upon review findings.

Credit risk measurement

Credit risk models are used throughout the Group to support the quantitative risk assessment element within the credit approval process, ongoing credit risk management, monitoring and reporting and portfolio analytics.

The Group is undertaking a significant programme of updates and improvements to its Wholesale credit risk models, including the incorporation of more recent data and reflecting updated regulatory requirements applying to some aspects of Wholesale Internal Ratings Based (IRB) modelling. Material updates to certain models, notably those used in Sovereign and Financial Institution asset classes, have been implemented during 2012 and are reflected in measures of risk reported in the Group's disclosures. Further updates, primarily in the Corporate asset class, are planned for 2013. In addition, in accordance with the instruction from the FSA, the Group has begun to transition relevant Commercial Real Estate assets to the slotting approach, under which modelled measures play no role in the determination of Risk Weighted Assets and capital requirements.

The model updates are generally in segments of the portfolio where risk experience has remained limited even in recent periods and primarily result in increases to measures that still remain within ranges representing lower risk business relative to the Group's broader risk profile; in terms of Probability of Default models, for example, the changes occur largely within ranges equivalent to Investment Grade ratings.

Material aspects of these changes have been anticipated in risk frameworks and in other areas that are dependent on these measures, notably including the Group's Risk Appetite framework. In some portfolios the anticipated impact on Risk Weighted Assets has been realised, as part of a process defined with regulators, prior to introduction of the updated models.

These models assess the probability that a customer will fail to make full and timely repayment of its obligations. The probability of a customer failing to do so is measured over a one year period through the economic cycle, although certain retail scorecards use longer periods for business management purposes.

Wholesale businesses - As part of the credit assessment process, each counterparty is assigned an internal credit grade derived from a default probability. There are a number of different credit grading models in use across the Group, each of which considers risk characteristics particular to that type of customer. The credit grading models score a combination of quantitative inputs (for example, recent financial performance) and qualitative inputs (for example, management performance or sector outlook).

Retail businesses - Each customer account is separately scored using models based on the most material drivers of default. In general, scorecards are statistically derived using customer data. Customers are assigned a score, which in turn is mapped to a probability of default. The probabilities of default are used to support automated credit decision making and to group customers into risk pools for regulatory capital calculations.

Exposure at default

Facility usage models estimate the expected level of utilisation of a credit facility at the time of a borrower's default. For revolving and variable draw-down type products which are not fully drawn, the exposure at default (EAD) will typically be higher than the current utilisation. The methodologies used in EAD modelling provide an estimate of potential exposure and recognise that customers may make more use of their existing credit facilities as they approach default.

Counterparty credit risk exposure measurement models are used for derivatives and other traded instruments, where the amount of credit risk exposure may be dependent upon one or more underlying market variables, such as interest or foreign exchange rates. These models drive internal credit risk management activities such as limit and excess management.

Loss given default

These models estimate the economic loss that may be experienced (the amount that cannot be recovered) by the Group on a credit facility in the event of default. The Group's loss given default models take into account both borrower and facility characteristics for unsecured or partially unsecured facilities, as well as the quality of any risk mitigation that may be in place for secured facilities, the cost of collections and a time discount factor for the delay in cash recovery.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

Credit risk assets

In the tables and commentary below, exposure refers to credit risk assets, which consist of:

- *Lending* - Comprises gross loans and advances to: central and local governments; central banks, including cash balances; other banks and financial institutions, incorporating overdraft and other short-term credit lines; corporations, in large part loans and leases; and individuals, comprising mortgages, personal loans and credit card balances. Lending includes both impaired loans and those loans where an impairment event has taken place, but no impairment provision is recognised.
- *Derivatives* - Comprises the mark-to-market (mtm) value of such contracts after the effect of enforceable netting agreements, but before the effect of collateral. In the event of a counterparty default, this is the amount due from the counterparty. Figures shown apply counterparty netting within the regulatory capital model used.
- *Contingent obligations* - Comprises primarily letters of credit and guarantees.

Credit risk assets exclude issuer risk (primarily debt securities) and reverse repurchase arrangements. They take account of legal netting arrangements that provide a right of legal set-off, but do not meet the offset criteria under IFRS.

Asset quality

Internal reporting and oversight of risk assets is principally differentiated by credit grades. Customers are assigned credit grades based on various credit grading models that reflect the key drivers of default for each customer type. All credit grades across the Group map to both a Group level asset quality scale, used for external financial reporting, and a master grading scale for wholesale exposures, used for internal management reporting across portfolios. Accordingly, measures of risk exposure may be readily aggregated and reported at increasing levels of granularity depending on stakeholder or business need.

The table below shows credit risk assets by asset quality (AQ) band:

Asset Quality Grade	Minimum	Maximum
AQ1	0.000	0.034
AQ2	0.034	0.048
AQ3	0.048	0.095
AQ4	0.095	0.381
AQ5	0.381	1.076
AQ6	1.076	2.153
AQ7	2.153	6.089
AQ8	6.089	17.222
AQ9	17.222	100.000
AQ10	100.000	100.000

The following table provides an analysis of the credit quality of third party financial assets by probability of default.

	Group					
	Cash and balances at central banks	Loans and advances to banks	Loans and advances to customers	Derivatives	Commitments	Contingent liabilities
2012	£m	£m	£m	£m	£m	£m
AQ1	725	8,039	293	404	168	1
AQ2	-	3	17	43	165	47
AQ3	-	4	81	39	40	35
AQ4	-	142	794	43	896	123
AQ5	-	2	893	5	523	29
AQ6	-	-	4,548	2	608	59
AQ7	-	-	9,918	6	423	60
AQ8	-	-	2,222	67	155	45
AQ9	-	-	5,395	115	80	15
AQ10	-	-	-	-	354	82
Accruing past due	-	-	2,800	-	-	-
Non-accrual	-	-	18,219	-	-	-
Impairment provisions	-	-	(10,774)	-	-	-
Total	725	8,190	34,406	724	3,412	496

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NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

	Group					
	Cash and balances at central banks	Loans and advances to banks	Loans and advances to customers	Derivatives	Commitments	Contingent liabilities
2011	£m	£m	£m	£m	£m	£m
AQ1	749	7,297	506	681	304	43
AQ2	-	-	63	11	126	35
AQ3	-	-	233	38	225	35
AQ4	-	22	1,073	10	515	108
AQ5	-	-	3,178	27	751	45
AQ6	-	-	6,431	7	640	96
AQ7	-	12	9,254	29	406	122
AQ8	-	-	2,559	88	196	15
AQ9	-	-	5,191	106	112	30
AQ10	-	-	-	-	381	105
Accruing past due	-	-	2,745	-	-	-
Non-accrual	-	-	16,763	-	-	-
Impairment provisions	-	-	(9,051)	-	-	-
Total	749	7,331	38,945	997	3,656	634

	Bank					
	Cash and balances at central banks	Loans and advances to banks	Loans and advances to customers	Derivatives	Commitments	Contingent liabilities
2012	£m	£m	£m	£m	£m	£m
AQ1	545	6,963	254	34	43	-
AQ2	-	2	3	3	8	-
AQ3	-	1	14	-	21	3
AQ4	-	87	148	-	161	10
AQ5	-	1	154	-	321	5
AQ6	-	-	816	-	207	10
AQ7	-	-	1,777	-	118	10
AQ8	-	-	426	-	45	2
AQ9	-	-	1,164	-	29	7
AQ10	-	-	-	-	61	20
Accruing past due	-	-	182	-	-	-
Non-accrual	-	-	3,114	-	-	-
Impairment provisions	-	-	(2,032)	-	-	-
Total	545	7,054	6,020	37	1,014	67

	Bank					
	Cash and balances at central banks	Loans and advances to banks	Loans and advances to customers	Derivatives	Commitments	Contingent liabilities
2011	£m	£m	£m	£m	£m	£m
AQ1	522	6,754	84	86	41	-
AQ2	-	-	1	-	2	-
AQ3	-	-	22	-	31	2
AQ4	-	-	628	-	88	2
AQ5	-	-	1,615	1	422	12
AQ6	-	-	638	-	205	6
AQ7	-	3	570	-	134	49
AQ8	-	-	588	-	69	4
AQ9	-	-	739	-	49	7
AQ10	-	-	-	-	91	7
Accruing past due	-	-	258	-	-	-
Non-accrual	-	-	3,131	-	-	-
Impairment provisions	-	-	(1,821)	-	-	-
Total	522	6,757	6,453	87	1,132	89

Loans and advances to customers, past due at balance sheet date but not considered impaired are shown in Note 9.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

Credit risk assets by industry and geography

Industry analysis plays an important part in assessing the potential for concentration risk in the loan portfolio. Particular attention is given to industry sectors where the Group believes there is a high degree of risk or potential for volatility in the future. The table below analyses credit risk assets by industry sector and geography.

	Group				
	Gross loans and advances to banks and customers £m	Debt securities and equity shares £m	Derivatives £m	Total £m	Netting and offset ⁽¹⁾ £m
2012					
UK					
Manufacturing	304	-	1	305	8
Construction	325	-	-	325	17
Finance	7,984	24	389	8,397	-
Service industries and business activities	746	-	16	762	48
Agriculture, forestry and fishing	295	-	-	295	54
Property	3,450	-	57	3,507	21
Individuals					
Home mortgages	2,298	-	-	2,298	-
Other	457	-	-	457	-
Interest accruals	8	-	-	8	-
Total UK	15,867	24	463	16,354	148
Rest of Europe					
Central and local government	42	-	-	42	-
Manufacturing	771	-	17	788	9
Construction	514	-	-	514	21
Finance	429	9	96	534	-
Service industries and business activities	5,056	-	70	5,126	60
Agriculture, forestry and fishing	705	-	1	706	29
Property	12,092	-	77	12,169	5
Individuals					
Home mortgages	16,882	-	-	16,882	1
Other	983	-	-	983	-
Interest accruals	29	-	-	29	-
Total Rest of Europe	37,503	9	261	37,773	125
Total					
Central and local government	42	-	-	42	-
Manufacturing	1,075	-	18	1,093	17
Construction	839	-	-	839	38
Finance	8,413	33	485	8,931	-
Service industries and business activities	5,802	-	86	5,888	108
Agriculture, forestry and fishing	1,000	-	1	1,001	83
Property	15,542	-	134	15,676	26
Individuals					
Home mortgages	19,180	-	-	19,180	1
Other	1,440	-	-	1,440	-
Interest accruals	37	-	-	37	-
	53,370	33	724	54,127	273

(1) This column shows the amount by which the Group's credit risk exposures is reduced through arrangements, such as master netting agreements, which give the Group a legal right to set-off the financial asset against a financial liability due to the same counterparty. In addition, the Group holds collateral in respect of individual loans and advances to banks and customers. This collateral includes mortgages over property (both personal and commercial); charges over business assets such as plant, inventories and trade receivables; and guarantees of lending from parties other than the borrower. The Group obtains collateral in the form of securities in reverse repurchase agreements. Cash and securities are received as collateral in respect of derivative transactions.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

	Group				
2011	Gross loans and advances to banks and customers £m	Debt securities and equity shares £m	Derivatives ⁽²⁾ £m	Total £m	Netting and offset ⁽¹⁾ £m
UK					
Manufacturing	300	-	2	302	6
Construction	320	-	-	320	15
Finance	5,729	71	628	6,428	-
Service industries and business activities	787	-	19	806	41
Agriculture, forestry and fishing	296	-	1	297	42
Property	3,803	-	55	3,858	21
Individuals					
Home mortgages	2,264	-	-	2,264	-
Other	414	-	-	414	-
Interest accruals	11	-	-	11	-
Total UK	13,924	71	705	14,700	125
Rest of Europe					
Central and local government	44	-	-	44	-
Manufacturing	868	-	11	879	9
Construction	543	-	-	543	24
Finance	1,885	33	102	2,020	2
Service industries and business activities	5,361	-	55	5,416	68
Agriculture, forestry and fishing	697	-	-	697	31
Property	13,189	-	124	13,313	9
Individuals					
Home mortgages	17,775	-	-	17,775	-
Other	984	-	-	984	-
Interest accruals	57	-	-	57	-
Total Rest of Europe	41,403	33	292	41,728	143
Total					
Central and local government	44	-	-	44	-
Manufacturing	1,168	-	13	1,181	15
Construction	863	-	-	863	39
Finance	7,614	104	730	8,448	2
Service industries and business activities	6,148	-	74	6,222	109
Agriculture, forestry and fishing	993	-	1	994	73
Property	16,992	-	179	17,171	30
Individuals					
Home mortgages	20,039	-	-	20,039	-
Other	1,398	-	-	1,398	-
Interest accruals	68	-	-	68	-
	55,327	104	997	56,428	268

(1) This column shows the amount by which the Group's credit risk exposures is reduced through arrangements, such as master netting agreements, which give the Group a legal right to set-off the financial asset against a financial liability due to the same counterparty. In addition, the Group holds collateral in respect of individual loans and advances to banks and customers. This collateral includes mortgages over property (both personal and commercial); charges over business assets such as plant, inventories and trade receivables; and guarantees of lending from parties other than the borrower. The Group obtains collateral in the form of securities in reverse repurchase agreements. Cash and securities are received as collateral in respect of derivative transactions.

(2) 2011 Derivatives have been reclassified to better reflect the geographical split of balances.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

	Bank				
	Gross loans and advances to banks and customers £m	Debt securities and equity shares £m	Derivatives £m	Total £m	Netting and offset ⁽¹⁾ £m
2012					
UK					
Central and local government	-	-	-	-	-
Manufacturing	304	-	-	304	8
Construction	325	-	-	325	17
Finance	7,285	26	35	7,346	-
Service industries and business activities	746	-	-	746	48
Agriculture, forestry and fishing	295	-	-	295	54
Property	3,450	-	-	3,450	21
Individuals					
Home mortgages	2,298	-	-	2,298	-
Other	395	-	-	395	-
Interest accruals	8	-	-	8	-
Total UK	15,106	26	35	15,167	148
Rest of Europe					
Central and local government	-	-	-	-	-
Manufacturing	-	-	-	-	-
Construction	-	-	-	-	-
Finance	-	-	2	2	-
Service industries and business activities	-	-	-	-	-
Agriculture, forestry and fishing	-	-	-	-	-
Property	-	-	-	-	-
Individuals					
Home mortgages	-	-	-	-	-
Other	-	-	-	-	-
Interest accruals	-	-	-	-	-
Total Rest of Europe	-	-	2	2	-
Total					
Central and local government	-	-	-	-	-
Manufacturing	304	-	-	304	8
Construction	325	-	-	325	17
Finance	7,285	26	37	7,348	-
Service industries and business activities	746	-	-	746	48
Agriculture, forestry and fishing	295	-	-	295	54
Property	3,450	-	-	3,450	21
Individuals					
Home mortgages	2,298	-	-	2,298	-
Other	395	-	-	395	-
Interest accruals	8	-	-	8	-
	15,106	26	37	15,169	148

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

	Bank				
	Gross loans and advances to banks and customers £m	Debt securities and equity shares £m	Derivatives ⁽²⁾ £m	Total £m	Netting and offset ⁽¹⁾ £m
2011					
UK					
Central and local government	-	-	-	-	-
Manufacturing	300	-	1	301	6
Construction	320	-	-	320	15
Finance	6,836	72	83	6,991	-
Service industries and business activities	787	-	-	787	41
Agriculture, forestry and fishing	296	-	-	296	42
Property	3,803	-	-	3,803	21
Individuals					
Home mortgages	2,264	-	-	2,264	-
Other	414	-	-	414	-
Interest accruals	11	-	-	11	-
Total UK	15,031	72	84	15,187	125
Rest of Europe					
Finance	-	-	3	3	-
Total Rest of Europe	-	-	3	3	-
Total					
Central and local government	-	-	-	-	-
Manufacturing	300	-	1	301	6
Construction	320	-	-	320	15
Finance	6,836	72	86	6,994	-
Service industries and business activities	787	-	-	787	41
Agriculture, forestry and fishing	296	-	-	296	42
Property	3,803	-	-	3,803	21
Individuals					
Home mortgages	2,264	-	-	2,264	-
Other	414	-	-	414	-
Interest accruals	11	-	-	11	-
Total	15,031	72	87	15,190	125

⁽¹⁾ This column shows the amount by which the Bank's credit risk exposures is reduced through arrangements, such as master netting agreements, which give the Bank a legal right to set-off the financial asset against a financial liability due to the same counterparty. In addition, the Bank holds collateral in respect of individual loans and advances to banks and customers. This collateral includes mortgages over property (both personal and commercial); charges over business assets such as plant, inventories and trade receivables; and guarantees of lending from parties other than the borrower. The Bank obtains collateral in the form of securities in reverse repurchase agreements. Cash and securities are received as collateral in respect of derivative transactions.

⁽²⁾ 2011 Derivatives have been reclassified to better reflect the geographical split of balances.

Credit risk mitigation

Approaches and methodologies

The Group employs a number of structures and techniques to mitigate credit risk. Netting of debtor and creditor balances is undertaken in accordance with relevant regulatory and internal policies. Exposure on over-the-counter derivative and secured financing transactions is further mitigated by the exchange of financial collateral and the use of market standard documentation. Further mitigation may be undertaken in a range of transactions, from retail mortgage lending to large wholesale financing. This can include: structuring a security interest in a physical or financial asset; use of credit derivatives, including credit default swaps, credit-linked debt instruments and securitisation structures; and use of guarantees and similar instruments (for example, credit insurance) from related and third parties. Such techniques are used in the management of credit portfolios, typically to mitigate credit concentrations in relation to an individual obligor, a borrower group or a collection of related borrowers.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

The use and approach to credit risk mitigation varies by product type, customer and business strategy. Minimum standards applied across the Group cover:

- The suitability of qualifying credit risk mitigation types and any conditions or restrictions applicable to those mitigants;
- The means by which legal certainty is to be established, including required documentation, supportive independent legal opinions and all necessary steps required to establish legal rights;
- Acceptable methodologies for initial and any subsequent valuations of collateral and the frequency with which collateral is to be revalued and the use of collateral haircuts;
- Actions to be taken in the event that the value of mitigation falls below required levels;
- Management of the risk of correlation between changes in the credit risk of the customer and the value of credit risk mitigation;
- Management of concentration risks, for example, by setting thresholds and controls on the acceptability of credit risk mitigants and on lines of business that are characterised by a specific collateral type or structure; and
- Collateral management to ensure that credit risk mitigation remains legally effective and enforceable.

Secured portfolios

Within its secured portfolios, the Group has recourse to various types of collateral and other credit enhancements to mitigate credit risk and reduce the loss to the Group arising from the failure of a customer to meet its obligations. These include: cash deposits; charges over residential and commercial property, debt securities and equity shares; and third-party guarantees. The existence of collateral may affect the pricing of a facility and its regulatory capital requirement.

When a collateralised financial asset becomes impaired, the impairment charge directly reflects the realisable value of collateral and any other credit enhancements.

Corporate exposures

The type of collateral taken by the Group's commercial and corporate businesses and the manner in which it is taken will vary according to the activity and assets of the customer.

- *Physical assets* - These include business assets such as stock, plant and machinery, vehicles, ships and aircraft. In general, physical assets qualify as collateral only if they can be unambiguously identified, located or traced, and segregated from uncharged assets. Assets are valued on a number of bases according to the type of security that is granted.
- *Real estate* - The Group takes collateral in the form of real estate, which includes residential and commercial properties. The loan amount will typically exceed the market value of the collateral at origination date. The market value is defined as the estimated amount for which the asset could be sold in an arms length transaction by a willing seller to a willing buyer.
- *Receivables* - When taking a charge over receivables, the Group assesses their nature and quality and the borrower's management and collection processes. The value of the receivables offered as collateral will typically be adjusted to exclude receivables that are past their due dates.

The security charges may be floating or fixed, with the type of security likely to impact: (i) the credit decision; and (ii) the potential loss upon default. In the case of a general charge such as a mortgage debenture, balance sheet information may be used as a proxy for market value if the information is deemed reliable.

The Group does not recognise certain asset classes as collateral: for example, short leasehold property and equity shares of the borrowing company. Collateral whose value is correlated to that of the obligor is assessed on a case-by-case basis and, where necessary, over-collateralisation may be required.

The Group uses industry-standard loan and security documentation wherever possible. Non-standard documentation is typically prepared by external lawyers on a case-by-case basis. The Group's business and credit teams are supported by in-house specialist documentation teams.

The existence of collateral has an impact on provisioning. Where the Group no longer expects to recover the principal and interest due on a loan in full or in accordance with the original terms and conditions, it is assessed for impairment. If exposures are secured, the current net realisable value of the collateral will be taken into account when assessing the need for a provision. No impairment provision is recognised in cases where all amounts due are expected to be settled in full on realisation of the security.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

Residential Mortgages

The Group's residential mortgage portfolio totalled £19.2 billion at 31 December 2012, with 88% in the Republic of Ireland and 12% in Northern Ireland. At constant exchange rates, the portfolio decreased 2.0% from 31 December 2011 as a result of natural amortisation and limited growth due to low market demand.

The table below shows how the continued decrease in property values has affected the distribution of residential mortgages by loan-to-value (LTV) (indexed). LTV is based upon gross loan amounts and, whilst including defaulted loans, does not take account of provisions made.

	Group	
	2012	2011
	%	%
Residential mortgages – distribution by average LTV ⁽¹⁾ indexed⁽²⁾		
<=50%	36.3	38.0
>50% and <=60%	5.6	5.7
>60% and <=70%	5.3	5.4
>70% and <=80%	5.3	5.4
>80% and <=90%	5.5	5.4
>90% and <=100%	5.5	6.0
>100%	36.5	34.1
Total portfolio average LTV at 31 December	85.5	81.4
Average LTV on new originations during the year	69.4	67.3

Note:

(1) The above table uses unweighted LTV averages calculated by transaction volume.

(2) Amendments have been made to the comparative percentages for the year ended 31 December 2011 in order to better reflect the 2011 residential mortgages distribution by average LTV analysis.

The table below details residential mortgages three months or more in arrears (by volume):

	Group	
	2012	2011
	%	%
Personal		
Mortgages	13.2	9.2

Collateral and other credit enhancements received

Due to the challenging economic conditions a substantial proportion of Commercial Real Estate portfolio is in excess of 100% LTV. The market conditions make it extremely challenging to obtain appropriate market valuations and there can be significant differences in values based on geographic location and asset type. Consequently, 72% (£11.0bn) (2011: 72% (£12.3bn)) of the Commercial Real Estate portfolio is actively managed by Non Core of which £10.1bn (2011: £10.5bn) is categorised REIL with a provision coverage of 61% (2011: 54%).

	2012		2011	
	Loans £m	Provisions £m	Loans £m	Provisions £m
Non-performing corporate loans (excluding commercial real estate)				
Secured	428	226	2,364	1,072
Unsecured	3,063	1,720	627	492

In the year to 31 December 2012 the guidelines determining which balances are considered as secured debt were made more stringent. This has resulted in a significant increase in balances which are classified as unsecured.

Retail exposures

All borrowing applications, whether secured or not, are subject to appropriate credit risk underwriting processes including affordability assessments. Pricing is typically higher on unsecured than secured loans. For secured loans, pricing will typically vary by LTV: higher-LTV products are typically subject to higher interest rates commensurate with the associated risk.

The value of a property intended to secure a mortgage is assessed during the loan underwriting process using industry-standard methodologies. Property values supporting home equity lending reflect either an individual appraisal or valuations generated by statistically valid automated valuation models. Property values are updated each quarter using the relevant house price index (Nationwide House Price Index in Northern Ireland and Central Statistics Office Residential Property Price Index in Republic of Ireland).

The existence of collateral has an impact on provisioning levels. Once a secured loan is classified as non-performing, the present realisable value of the underlying collateral and the costs associated with repossession are used to estimate the provision required.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management – credit risk (continued)

The tables below shows period-end weighted LTVs for the Group's residential mortgage portfolio split between performing and non-performing.

	2012 £m	2011 £m
Non-performing residential mortgages by average loan to value (LTV)⁽¹⁾		
<70%	471	379
>70% and <=90%	294	223
>90% and <=110%	330	258
>110% and <=130%	397	322
>130%	1,764	1,117
Total portfolio average by LTV	132.2%	124.8%
Performing residential mortgages by average loan to value (LTV)⁽¹⁾		
<70%	3,815	4,442
>70% and <=90%	2,019	2,279
>90% and <=110%	2,358	2,837
>110% and <=130%	2,412	2,750
>130%	5,301	5,401
Total portfolio average by LTV	107.7%	104.1%

(1) Amendments have been made to the comparative amounts and percentages for the year ended 31 December 2011 in order to better reflect the 2011 non-performing and performing residential mortgages by average LTV analysis.

Aside from the lending portfolios, the Group receives collateral and other credit enhancements on other financial assets on its balance sheet as detailed in the following table.

	2012 £m	2011 £m
Reverse repurchase agreements	-	-
Securities received as collateral	-	-
Derivative assets gross exposure	26	19

Regulatory risk

Regulatory risk is the risk of material loss or liability, legal or reputational sanctions, or reputational damage, arising from the failure to comply with (or adequately plan for changes to) relevant official sector policy, laws, regulations, or major industry standards, in any location in which the Group operates. The Group believes that maintaining a strong regulatory risk framework is fundamental to protecting sustainable growth, rebuilding its reputation and maintaining stakeholder confidence.

The regulatory environment remained highly challenging during 2012, as policymakers and regulators continued to strengthen regulation and supervision in response to the events of 2007 and 2008 and subsequent economic and financial stress.

The Group's approach to regulatory risk has three distinct elements:

- The review of potential changes in regulation to ensure that the Group addresses the risks arising from such changes and responds appropriately;
- The monitoring of compliance with existing rules and regulations and the mitigation of the consequences of any inadvertent non-compliance; and
- The management of effective relationships with regulators to ensure constructive engagement.

Reputational risk

Reputational risk is the risk of brand damage and/or financial loss due to a failure to meet stakeholders' expectations of the Group's conduct and performance.

Stakeholders include customers, investors, rating agencies, employees, suppliers, government, politicians, regulators, special interest groups, consumer groups, media and the general public. Brand damage can be detrimental to the business in a number of ways, including an inability to build or sustain business relationships, low staff morale or reduced access to funding sources.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management (continued)

Reputational risk (continued)

One of the most fundamental stakeholder expectations is that a bank is financially prudent, safe and sound. The Group has made significant progress in restructuring its balance sheet and improving its capital and funding position. Major reforms have also been made to strengthen its risk evaluation and management processes. Further work remains, but the Group is now in a much stronger financial position to face challenges and uncertainties in its economic and operating environment.

The Group has put the focus on serving customers well at the heart of its strategic objectives that, combined with a safe and sound bank, will build a culture and reputation in line with our stakeholder expectations. There are still legacy issues to work through, but dealing with them in an open and direct manner is a necessary part of the ability to move forward.

The Group's reputational risk management framework is aligned with its strategic objectives and its risk appetite. It is designed to embed, at different points of decision-making processes, a series of customer-related and reputational filters and controls that examine products, services and activities through the lens of sustainability, transparency and fairness.

This approach recognises that reputational risk can arise across a range of actions taken (or, in some cases, not taken) by the Group, as well as its wider conduct, policies and practices. Therefore, it is aligned with the management of a range of risk types that have a high reputational sensitivity.

The Board has ultimate responsibility for managing the Group's reputation, though all parts of the Group have responsibility for any reputational impact arising from their operations.

Conduct risk

Conduct risk is the risk that the conduct of the Group and its staff towards its customers, or within the markets in which it operates, leads to reputational damage and/or financial loss by breaching regulatory rules or laws, or failing to meet customers' or regulators' expectations of the Group. Activities through which conduct risk may arise include: personal

account dealing; privacy and data protection; conflicts of interest; and product design.

Effective conduct risk management is not only a commercial imperative for the Group; customers, clients and counterparties demand it as a precursor to building trust. It also reflects the changing regulatory environment.

The RBS Group's Compliance function manages conduct risk facing the Group, including Anti-Money Laundering (AML); Sanctions and Terrorist Financing; and Anti-Bribery and Corruption. In doing so, Group Compliance is responsible for the design, implementation and maintenance of an effective management framework to enable consistent identification, assessment, management, monitoring and reporting of conduct risk.

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. It is an integral and unavoidable part of the Group's business as it is inherent in the processes it operates to provide services to customers and meet strategic objectives.

The objective of operational risk management is not to remove operational risk altogether, but to manage it to an acceptable level, taking into account the cost of minimising the risk against the resultant reduction in exposure. Strategies to manage operational risk include avoidance, transfer, acceptance and mitigation by controls.

In 2012, the Group continued to make good progress in enhancing its operational risk framework and risk management capabilities.

The standards, which are incorporated in the Group Policy Framework, provide the direction for delivering effective operational risk management and are designed to allow the consistent identification, assessment, management, monitoring and reporting of operational risk across the Group.

Operational risk appetite, policy and frameworks are tabled regularly at the Executive Risk Forum to satisfy oversight responsibilities and, as appropriate, to other senior committees.

Sovereign risk

The Group's sovereign portfolio comprises central governments, central banks and sub-sovereigns such as local authorities, primarily in the Group's key markets in the UK and Republic of Ireland. Exposure predominantly comprises cash balances placed with central banks such as the Bank of England, the Central Bank of Ireland and consequently, the asset quality of this portfolio is high. Exposure to sovereigns fluctuates according to the Group's liquidity requirements and cash positions, which determine the level of cash placed with central banks.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

23. Risk management (continued)

Pension risk

The Group is exposed to risk from its defined benefit pension schemes to the extent that the assets of the schemes do not fully match the timing and amount of the schemes' liabilities. Pension scheme liabilities vary with changes to long-term interest rates, inflation, pensionable salaries and the longevity of scheme members as well as changes in legislation. Ultimate responsibility for the Group's pension schemes is separate from Group management. The Group is exposed to the risk that the market value of the schemes' assets, together with future returns and any additional future contributions could be considered insufficient to meet the liabilities as they fall due. In such circumstances, the Group could be obliged, or may choose, to make additional contributions to the schemes or be required to hold additional capital to mitigate such risk.

The Ulster Bank Pension Scheme (UBPS) and the Ulster Bank Pension Scheme (Republic of Ireland) (UBPSROI) are the largest of the schemes and the main sources of pension risk. They both operate under trust deeds under which the corporate trustees are wholly owned subsidiaries of the Group. Both trustee boards comprise six directors selected by the Group and three directors nominated by members.

The trustee boards are solely responsible for the investment of the schemes' assets which are held separately from the assets of the Group. The Group and the trustee board must agree on the investment principles and the funding plan.

In November 2009, both schemes were closed to new employees. In April 2010, the Group confirmed that it was making changes to both of these schemes and the Group's other defined benefit scheme, the First Active Pension Scheme (FAPS). For some members, the Group has limited the amount by which pensionable salary would increase in future (the "pensionable salary cap") to 2% per annum (or CPI inflation, if lower). For those who decided not to accept terms which included the pensionable salary cap, and were not in the Provident Fund sections of the schemes, the Group agreed with the trustees of the schemes a reduction in the accrual rate from 60ths to 80ths for future service, in return for improvements in future funding of the schemes. In 2011 a further contract offer was made and this has reduced the number of employees who are subject to the lower accrual rate and increased the number subject to the pensionable earnings cap.

Risk appetite and investment policy are agreed by the trustees with quantitative and qualitative input from the scheme actuaries and investment advisers. The trustees also consult with the Group to obtain its view on the appropriate level of risk within the pension funds. The Group independently monitors risk within its pension funds as part of the Internal Capital Adequacy Assessment Process ("ICAAP").

All schemes are invested in diversified portfolios of quoted and private equity, government and corporate fixed-interest and index-linked bonds, and other assets including property, derivatives and hedge funds.

The most recent funding valuations of the schemes were carried out at 31 December 2010 (UBPS) and 31 December 2009 (UBPSROI). Further details are given in Note 4 to the accounts. A new funding valuation is due for UBPS with an effective date of 31 December 2013. In addition, as a result of a change in the funding framework in the Republic of Ireland, new funding plans for the UBPSROI and FAPS need to be submitted by 30 June 2013. These revised funding plans may result in a change in the level of contributions payable to the schemes.

With effect from 1 January 2013, the revised International Accounting Standard for Pensions (IAS19R) will apply to the schemes. As a result the current "corridor" methodology adopted by the Group which permitted deferral of recognition of gains and losses within a 10% corridor will be abolished. From 2013 onwards, gains and losses will be immediately recognised, resulting in increased balance sheet volatility.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

24. Capital resources

	2012 £m	2011 £m
<i>Shareholders' equity (excluding non-controlling interests)</i>		
Shareholders' equity per balance sheet	6,894	6,301
Preference shares – equity	(959)	(959)
	5,935	5,342
<i>Non-controlling interests</i>		
Non-controlling interests per balance sheet	500	512
Other adjustments to non-controlling interests for regulatory purposes	(477)	(489)
	23	23
<i>Regulatory adjustments and deductions</i>		
Defined benefit pension adjustment	(82)	(134)
50% excess of expected losses over impairment provisions (net of tax)	(1,088)	(1,219)
	(1,170)	(1,353)
Core tier 1 capital	4,788	4,012
<i>Other tier 1 capital</i>		
Preference shares – equity	1,436	1,448
<i>Deductions</i>		
Tax on excess of expected losses over impairment provisions	353	439
Excess of Tier 2 50:50 deduction	(314)	(494)
	39	(55)
Total tier 1 capital	6,263	5,405
<i>Qualifying tier 2 capital</i>		
Undated subordinated debt	98	100
Dated subordinated debt - net of amortisation	1,029	1,060
Collectively assessed impairment provisions	-	4
	1,127	1,164
<i>Tier 2 deductions</i>		
50% excess of expected losses over impairment provisions	(1,441)	(1,658)
Excess Tier 2 50:50 deduction to transfer to Tier 1	314	494
	(1,127)	(1,164)
Total tier 2 capital	-	-
Total regulatory capital	6,263	5,405
Key capital ratios	%	%
Tier 1	15.2	12.9
Total capital	15.2	12.9
Risk weighted assets by risk		
Credit risk	37,400	38,300
Counterparty risk	1,500	1,100
Market risk	200	300
Operational risk	2,000	2,200
Total risk weighted assets	41,100	41,900

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

24. Capital resources (continued)

In the management of capital resources, the Group is governed by the Ulster Bank and the RBS Group policies which are to maintain a strong capital base, to expand it as appropriate and to utilise it efficiently throughout its activities to optimise the return to shareholders while maintaining a prudent relationship between the capital base and the underlying risks of the business.

In carrying out these policies the Group has regard to and has complied with the supervisory requirements of the FSA. The FSA uses Risk Asset Ratio (RAR) as a measure of capital adequacy for banks, comparing a bank's capital resources with its risk-weighted assets (the assets and off-balance sheet exposures are 'weighted' to reflect the inherent credit and other risks); by international agreement, the RAR should not be less than 8% with a Tier 1 component of not less than 4%. The FSA has highlighted the shortcomings of the Commercial Real Estate models used by all UK regulated entities. It has advised the Group to adopt the "Specialised Lending" approach to determine capital requirements of Ulster Bank Limited. This approach was introduced during the year by Ulster Bank Limited and is due to be fully embedded by the end of 2013.

25. Memorandum items

Contingent liabilities and commitments

The amounts shown in the table below are intended only to provide an indication of the volume of business outstanding at 31 December 2012. Although the Group is exposed to credit risk in the event of non-performance of the obligations undertaken by customers, the amounts shown do not, and are not intended to, provide any indication of the Group's expectation of future losses.

	Group		Bank	
	2012 £m	2011 £m	2012 £m	2011 £m
Contingent liabilities:				
Guarantees and assets pledged as collateral security	261	397	29	41
Other contingent liabilities	235	237	38	48
	496	634	67	89
Commitments:				
Documentary credits and other short-term trade related transactions	9	7	2	3
Commitments to lend:				
- less than one year	2,406	2,642	945	991
- one year and over	997	1,007	67	138
	3,412	3,656	1,014	1,132

Banking commitments and contingent obligations, which have been entered into on behalf of customers and for which there are corresponding obligations from customers, are not included in assets and liabilities. The Group's maximum exposure to credit loss, in the event of non-performance by the other party and where all counterclaims, collateral or security proves valueless, is represented by the contractual nominal amount of these instruments included in the table. These commitments and contingent obligations are subject to the Group's normal credit approval processes and any potential loss is taken into account in assessing provisions for bad and doubtful debts in accordance with the Group's provisioning policy.

Contingent liabilities

Guarantees - the Group gives guarantees on behalf of customers. A financial guarantee represents an irrevocable undertaking that the Group will meet a customer's obligations to third parties if the customer fails to do so. The maximum amount that the Group could be required to pay under a guarantee is its principal amount as disclosed in the table above. The Group expects most guarantees it provides to expire unused.

Other contingent liabilities - these include standby letters of credit, supporting customer debt issues and contingent liabilities relating to customer trading activities such as those arising from performance and customs bonds, warranties and indemnities.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

25. Memorandum items (continued)

Commitments

Commitments to lend - under a loan commitment the Group agrees to make funds available to a customer in the future. Loan commitments, which are usually for a specified term may be unconditionally cancellable or may persist, provided all conditions in the loan facility are satisfied or waived. Commitments to lend include commercial standby facilities and credit lines, liquidity facilities to commercial paper conduits and unutilised overdraft facilities.

Other commitments - these include documentary credits, which are commercial letters of credit providing for payment by the Group to a named beneficiary against presentation of specified documents, forward asset purchases, forward deposits placed and undrawn note issuance and revolving underwriting facilities, documentary credits and other short-term trade related transactions.

Contractual obligations for future expenditure not provided in the financial statements

The following table shows contractual obligations for future expenditure not provided for in the financial statements at the year end:

	Group		Bank	
	2012	2011	2012	2011
	£m	£m	£m	£m
Property, plant and equipment				
Other capital expenditure	-	1	-	1
Contracts to purchase goods or services	8	8	4	3
	8	9	4	4

Litigation and investigations

The Group is involved in litigation in the United Kingdom and the Republic of Ireland. The litigation involves claims by and against Group companies which arise in the ordinary course of business. No material adverse effect on the net assets of the Group is expected to arise from the ultimate resolution of these claims.

Interest rate hedging products

In June 2012, following an industry wide review, the FSA announced that the RBS Group, including Ulster Bank Limited, and other UK banks had agreed to a redress exercise and past business review in relation to the sale of interest rate hedging products to some small and medium sized businesses who were classified as retail clients under FSA rules. On 31 January 2013, the FSA issued a report outlining the principles to which it wishes the RBS Group and other UK banks to adhere in conducting the review and redress exercise.

The RBS Group will provide fair and reasonable redress to non-sophisticated customers classified as retail clients, who were sold structured collars. Ulster Bank Group made a provision of £10 million in 2012 for the redress it expects to offer to these customers. As the actual amount that the Group will be required to pay, if any, will depend on the facts and circumstances of each case, there is no certainty as to the eventual costs of redress.

The Group has written to non-sophisticated customers classified as retail clients sold other interest rate products (other than interest rate caps) on or after 1 December 2001 offering a review of their sale and, if it is appropriate in the individual circumstances, the Group will propose fair and reasonable redress on a case by case basis. Furthermore, non-sophisticated customers classified as retail clients who have purchased interest rate caps will be entitled to approach the Group and request a review. At this stage, the Group is not able to estimate reliably the cost of redress for these customers.

The redress exercise and the past business review is being scrutinised by an independent reviewer, who will review and agree any redress, and will be overseen by the FSA.

Ulster Bank Ireland Limited (which is not within the scope of the FSA review) has recently been served with two litigation claims in relation to interest rate hedging products in the Republic of Ireland.

Capital Support Deed

The Bank, together with other members of the RBS Group, is party to a capital support deed (CSD). Under the terms of the CSD, the Bank may be required, if compatible with its legal obligations, to make distributions on, or repurchase or redeem, its ordinary shares. The amount of this obligation is limited to the Bank's capital resources in excess of the capital and financial resources needed to meet its regulatory requirements. The Bank may also be obliged to make onward distribution to its ordinary shareholders of dividends or other capital distributions received from subsidiaries that are party to the CSD. The CSD also provides that, in certain circumstances, funding received by the Bank from other parties to the CSD becomes immediately repayable, such repayment being limited to the Bank's available resources.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

26. Net cash flow from operating activities

	Group		Bank	
	2012	2011	2012	2011
	£m	£m	£m	£m
Operating loss before tax	(2,091)	(3,072)	(4,032)	(4,165)
Depreciation, amortisation and impairment	43	30	17	10
Interest on subordinated liabilities	27	34	13	19
Charge for defined benefit pension schemes	26	27	7	6
Cash contribution to defined benefit pension schemes	(77)	(75)	(40)	(39)
Loan impairment provisions net of recoveries	2,128	3,544	256	737
Impairment of investments in Group undertaking	-	-	3,663	3,518
Elimination of foreign exchange differences	(194)	(411)	(9)	(7)
Other non-cash items	(244)	(295)	(33)	(51)
Net cash (outflow)/inflow from trading activities	(382)	(218)	(158)	28
Decrease/(increase) in loans and advances to banks and customers	2,782	3,492	348	(3,271)
Increase in debt securities	(16)	(74)	(9)	(87)
Decrease in other assets	5	37	1	30
Decrease/(increase) in derivative assets	273	(35)	50	62
Decrease in assets held for sale	-	1	-	-
Changes in operating assets	3,044	3,421	390	(3,266)
(Decrease)/increase in deposits by banks and customers	(4,213)	(3,114)	(158)	1,520
Decrease in debt securities in issue	(276)	(3,312)	(36)	(76)
Increase/(decrease) in other liabilities	41	(179)	21	(176)
Decrease in derivative liabilities	(360)	(44)	(6)	(78)
Changes in operating liabilities	(4,808)	(6,649)	(179)	1,190
Total taxes received	124	182	155	137
Net cash (outflow)/inflow from operating activities	(2,022)	(3,264)	208	(1,911)

27. Interest received and paid

	Group		Bank	
	2012	2011	2012	2011
	£m	£m	£m	£m
Interest received	1,226	1,071	344	293
Interest paid	(459)	(599)	(177)	(156)
	767	472	167	137

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

28. Analysis of changes in financing during the year

	Group					
	Share capital and share premium		Capital contribution reserve		Subordinated liabilities	
	2012 £m	2011 £m	2012 £m	2011 £m	2012 £m	2011 £m
At 1 January	2,412	2,412	10,576	5,918	1,183	1,215
Net cash inflows from financing	-	-	2,931	4,658	-	-
Currency translation and other adjustments	-	-	-	-	(26)	(32)
At 31 December	2,412	2,412	13,507	10,576	1,157	1,183

	Bank					
	Share capital and share premium		Capital contribution reserve		Subordinated liabilities	
	2012 £m	2011 £m	2012 £m	2011 £m	2012 £m	2011 £m
At 1 January	2,412	2,412	10,576	5,918	961	986
Net cash inflows from financing	-	-	2,931	4,658	-	-
Currency translation and other adjustments	-	-	-	-	(22)	(25)
At 31 December	2,412	2,412	13,507	10,576	939	961

29. Analysis of cash and cash equivalents

	Group		Bank	
	2012 £m	2011 £m	2012 £m	2011 £m
At 1 January				
Cash	749	854	522	613
Cash equivalents	4,948	3,326	2,441	3,563
	5,697	4,180	2,963	4,176
Net cash inflow/(outflow)	945	1,587	443	(1,213)
Effect of exchange rate changes on cash and cash equivalents	(117)	(70)	(2)	-
At 31 December	6,525	5,697	3,404	2,963
Comprising:				
Cash and balances at central banks	725	749	545	522
Loans and advances to banks and debt securities	5,800	4,948	2,859	2,441

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

30. Divisional analysis

The Group operates in the financial services industry in the United Kingdom and the Republic of Ireland and provides an integrated service to its customers. The directors manage the Group primarily by class of business and present the divisional analysis on that basis. Divisions charge market prices for services rendered to other parts of the Group; funding charges between divisions are determined by Group Treasury, having regard to commercial demands.

The Group reports on a divisional basis as follows:

Retail Banking provides loan and deposit products through a network of branches and direct channels.

Corporate Banking provides services to business and corporate customers.

Both Retail Banking and Corporate Banking are supported by business services, finance, human resources and head office divisions.

Other comprises Non-Core and Central functions. Non-Core consists of assets that the Group intends to run off or dispose. Central functions comprise Group and corporate functions such as treasury, funding and finance, risk management, legal, communications and human resources.

Divisional information by class of business and geographical area is set out below:

Class of Business	Total income			Operating expenses before depreciation	Depreciation and amortisation	Impairment losses	Operating loss before tax
	Interest income	Non-interest income	Total				
2012	£m	£m	£m	£m	£m	£m	£m
Retail Banking	284	76	360	(157)	-	(699)	(496)
Corporate Banking	240	120	360	(112)	-	(665)	(417)
Other	171	64	235	(411)	(26)	(976)	(1,178)
Total	695	260	955	(680)	(26)	(2,340)	(2,091)

Class of Business	Total income			Operating expenses before depreciation	Depreciation and amortisation	Impairment losses	Operating loss before tax
	Interest income	Non-interest income	Total				
2011	£m	£m	£m	£m	£m	£m	£m
Retail Banking	337	91	428	(114)	(1)	(626)	(313)
Corporate Banking	321	113	434	(98)	(1)	(758)	(423)
Other	182	242	424	(398)	(28)	(2,334)	(2,336)
Total	840	446	1,286	(610)	(30)	(3,718)	(3,072)

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

30. Divisional analysis (continued)

Class of Business	2012		2011	
	Assets £m	Liabilities £m	Assets £m	Liabilities ⁽¹⁾ £m
Retail Banking	18,488	(10,142)	20,164	(9,658)
Corporate Banking	10,857	(14,268)	13,768	(13,931)
Other	15,350	(12,891)	15,013	(18,543)
Total	44,695	(37,301)	48,945	(42,132)

(1) For the year ended 31 December 2011 certain amounts have been reclassified between Retail Banking, Corporate Banking and Other divisions in order to better reflect the divisional liability analysis.

Geographical divisions	2012			2011 ⁽¹⁾		
	United Kingdom £m	Republic of Ireland £m	Total £m	United Kingdom £m	Republic of Ireland £m	Total £m
Total Income	137	818	955	234	1,052	1,286
Operating loss before tax	(590)	(1,501)	(2,091)	(1,094)	(1,978)	(3,072)
Net Assets	(1,147)	8,541	7,394	(1,325)	8,138	6,813
Total Assets	13,331	31,364	44,695	13,489	35,456	48,945

(1) For the year ended 31 December 2011 certain amounts have been reclassified between the United Kingdom and Republic of Ireland in order to better reflect the geographical divisional analysis.

31. Transactions with directors

At 31 December 2012, the amounts outstanding in relation to transactions, arrangements and agreements entered into by authorised institutions in the Group, as defined in UK legislation, were £705,045 (2011: £1,082,168) in respect of loans to any persons who were directors at any time during the financial period.

32. Related parties

The Bank's immediate parent company is National Westminster Bank Plc, which is incorporated in Great Britain.

The Bank's ultimate holding company, and the parent of the largest group into which the Company is consolidated, is The Royal Bank of Scotland Group plc which is incorporated in Great Britain and registered in Scotland. Copies of the accounts for The Royal Bank of Scotland Group plc can be obtained from The Secretary, The Royal Bank of Scotland Group plc, Gogarburn, Edinburgh, EH12 1HQ.

The smallest subgroup into which the Bank is consolidated has as its parent company National Westminster Bank Plc, a company incorporated in Great Britain. Copies of the accounts for this subgroup can be obtained from The Secretary, The Royal Bank of Scotland Group plc, Gogarburn, Edinburgh, EH12 1HQ.

UK Government

On 1 December 2008, the UK Government through HM Treasury became the ultimate controlling party of The Royal Bank of Scotland Group plc. The UK Government's shareholding is managed by UK Financial Investments Limited, a company wholly-owned by the UK Government. As a result the UK Government and UK Government controlled bodies became related parties of the Group.

The Funding for Lending Scheme

The Bank of England launched the new Funding for Lending Scheme (FLS), aimed at increasing lending to the real UK economy. FLS opened for drawings in August and Ulster Bank Limited launched FLS-related offerings to businesses. FLS provides an opportunity to offer interest rate benefits to customers. Over £60 million of business loans have been offered under the scheme by the end of 2012, and approximately 27% of those loans relate to 'new to bank' customers. Over 140 customers benefited from this offer by the end of 2012, with around £10 million of funds allocated.

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

32. Related parties (continued)

(a) Directors and key managers

At 31 December 2012, amounts advanced by the Group were £705,045 in respect of loans to 8 persons who served as directors during the financial period.

The aggregate transactions between the Group and its directors, key managers, their close families and companies which they control were:

	Number of directors	Number of key managers	Connected parties	Transaction £
Transactions during the year				
Loans made during the year:				
– at a commercial rate	-	3	1	6,393,953
Balances outstanding at the end of the year				
Loans:				
– at a commercial rate	8	8	16	11,973,753
– at a preferential rate	-	5	1	599,080
Customer accounts:				
– Savings	9	12	52	8,678,667

ULSTER BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS for the year ended 31 December 2012

32. Related parties (continued)

(b) Related party transactions

Included in the Group and Bank's balance sheet are the following balances with related parties at the year end:

	Group		Bank	
	2012	2011	2012	2011
	£m	£m	£m	£m
Assets				
Loans and advances:				
Parent companies	7,557	5,253	6,654	6,320
Key management	2	2	-	1
Other related parties, including fellow subsidiaries	7	-	210	52
	7,566	5,255	6,864	6,373
Derivatives:				
Parent companies	388	628	67	83
Total assets	7,954	5,883	6,931	6,456
Liabilities				
Deposits:				
Parent companies	5,543	11,055	4,503	4,289
Key management	1	4	-	1
Other related parties, including fellow subsidiaries	867	333	79	24
	6,411	11,392	4,582	4,314
Subordinated loans:				
Parent companies	1,021	1,044	939	961
Other related parties, including fellow subsidiaries	136	139	-	-
	1,157	1,183	939	961
Derivatives:				
Parent companies	926	1,237	77	83
Total liabilities	8,494	13,812	5,598	5,358

(c) Compensation of key management

The aggregate remuneration of directors and other members of key management during the year was as follows:

	Group	
	2012	2011
	£	£
Short term benefits	4,560,754	4,691,379
Termination benefit	-	584,265
Long term benefit	956,269	1,089,045
	5,517,023	6,364,689

33. Post balance sheet events

There have been no significant events between the year end and the date of approval of the financial statements which would require a change or additional disclosure or amendment in the financial statements.

ULSTER BANK LIMITED

DIRECTORS AND EXECUTIVES

Chairman

Sean Dorgan (61)

was appointed deputy Chairman in July 2008 and subsequently Chairman in September 2008. He also serves on the governing board of Dublin Institute of Technology and CRANN Nanoscience Institute at Trinity College, Dublin. He is a board member of Short Bros and FBD Holdings plc. Previously he was on the Board of Fineos Corporation and was Chairman of Tesco Ireland until 2011, and from 1999 – 2007 he was Chief Executive of IDA Ireland, one of the world's leading inward investment agencies. He has also been Secretary General of the government departments responsible for industry, commerce, tourism and trade, and Chief Executive of the Institute of Chartered Accounts in Ireland.

EXECUTIVE DIRECTORS

Group Chief Executive

Jim Brown (52)

was appointed Chief Executive Officer of Ulster Bank Group in April 2011. Prior to taking up his role in Ulster Bank, Jim was Chief Executive Officer for Retail and Commercial Markets in Asia and Middle East with responsibility for the RBS retail and commercial banking franchise in nine markets. He formerly worked in ABN AMRO holding a variety of senior positions including Head of Consumer Clients Asia and Country Manager for Taiwan. He also worked in Citibank holding various key positions in retail and commercial banking in Taiwan, Australia and New Zealand.

Stephen Bell (48)

was appointed Chief Risk Officer in March 2012. He joined the Bank from PwC from where he was most recently seconded to the role of Chief Risk Officer at Allied Irish Banks plc in the aftermath of the substantial nationalisation of the bank. Prior to that he established and ran the Business Support & Recoveries operation for Barclays Western Europe, based in Madrid. Before that he was Strategy & Change Director at Royal and Sun Alliance. He joined R&SA from Transamerica Commercial Finance where he was Vice President & Managing Director, EMEA. Earlier in his career he was Chief Risk Officer in GE's Auto Financial Services business. He started his career with National & Provincial Building Society and over a 9 year period held a variety of senior risk and collections roles. He is a member of the Ulster Bank Executive Committee and all relevant sub-committees, the UBL and UBIL Boards, the UBL and UBIL Board Risk Committees and is a member of the RBS Group Risk Management Committee.

NON-EXECUTIVE DIRECTORS

Trevor Bowen (63)

joined the Bank Board in 2004. He had been a First Active director since 2003. A Chartered Accountant, he is a Partner in Principle Management and holds a number of other non-executive directorships including Ardmore Studios Limited, Amphitheatre Ireland Limited, Grand Canal Theatre Company Limited and Kennedy Wilson Europe Limited.

Eileen Gleeson (52)

joined the Bank Board in 2004. She joined First Active Board in 2003 and subsequently Ulster Bank Ireland Limited Board in 2009. A Chartered Director, she is an Assessor with the Institute of Directors Board Performance Evaluation Service. She is a non-executive director of the Coombe Woman and Infants University Hospital and the DCU Ryan Academy for Entrepreneurship. Formerly she was Chairman of communications company Weber Shandwick Ireland, and a non-executive director of Sustainable Energy Authority of Ireland. She was Special Adviser to the former President of Ireland, Mary McAleese from 1997 to 2004.

Christopher Mills (65)

retired as Group Chief Executive Officer of Ulster Carpet Mills where he played a leadership role since 1988. He began his career with Esso Petroleum, spending 18 years in a variety of management positions. He has been President of the Northern Ireland Chamber of Commerce, Chairman of Business in the Community and President of the European Carpet Manufacturers Association.

Dr Philip Nolan (59)

was educated at Queen's University Belfast where he graduated with a PhD in Geology. Beginning his career as a Geology Lecturer, he joined British Petroleum as a Geologist in 1981. He spent 15 years with the company before joining British Gas (BG) in 1996 where he subsequently became Chief Executive of Lattice Group, which de-merged from BG in 1999. He was Chief Executive Officer at Eircom Group from 2002 to 2006 and Chairman of Infinis Limited and Sepura plc from 2007 to 2010. He currently is Chairman of the Irish Management Institute and John Laing plc. He is also a non-executive director of Providence Resources and EnQuest plc and senior advisor to Warburg Pincus Private Equity Group.

ULSTER BANK LIMITED

DIRECTORS AND EXECUTIVES (continued)

NON-EXECUTIVE DIRECTORS (continued)

Ian Webb (65)

is Chairman of John Hogg and Company, a privately owned family firm, which operates a range of businesses including textiles, travel, fuel oils and property. He joined the company in 1970.

Sir Nigel Hamilton (64)

joined the Ulster Bank Board in April 2009, after retiring from his role as Head of the Northern Ireland Civil Service in July 2008. During his time as Head of the Northern Ireland Civil Service he was also Head of the Office of the First Minister and Deputy First Minister and Secretary to the Northern Ireland Executive. He is a non-executive director of Belfast City Airport, and Chairman of the Northern Ireland Council of the Prince's Trust. He is also Vice Lord Lieutenant for the City and Borough of Belfast.

Dr Andrew McLaughlin (44)

is a member of the RBS Group's Management Committee holding the position of Director of Communications and Group Chief Economist. His overall experience as a senior RBS executive and his expertise in communications, reputation management and the economic field are particularly relevant to the Bank given the challenging banking and economic markets in which it operates. He is also leading the Bank's work in regards to the UK Independent Commission on Banking.

Christopher (Chris) Campbell (54)

joined RBS Group in August 2005 as Deputy General Counsel and Director, Group Legal and became Group General Counsel in May 2010. Prior to joining RBS Group, he was a partner for 18 years in Scotland's largest law firm, Dundas & Wilson, and was Managing Partner from 1996 until he joined RBS Group in 2005. In his role as Group General Counsel, Mr. Campbell has overall responsibility for advising the RBS Group Board and Executive Committee and for the provision of legal support to all of RBS's businesses globally. His responsibilities also include the Group Secretariat and Regulatory Affairs & Compliance functions. He is an Honorary Professor in Commercial Law at the University of Glasgow.

Bridget Rosewell (61)

is an economist with degrees from Oxford University, where she also taught until 1984. She has founded two economics consultancies, and is Chair of Volterra Partners. She has advised the Chancellor of the Exchequer, Treasury Select Committee and the Mayor of London. She has been responsible for the economic analysis of major infrastructure projects and is currently a Non-Executive Director of Network Rail and a Member of the With Profits Committee for Co-Operative Financial Services.

Des O'Shea (56)

was appointed to the Board of Ulster Bank in November 2012. He is also a Director of OJSC Orient Express Bank, a leading Russian Retail Bank. In November 2011 he retired from GE Capital after 14 years during which he held a variety of senior roles including Chief Risk Officer, Chief Commercial Officer and Head of Mergers & Acquisitions for GE Money Europe which was GE Capital's largest and most profitable business in Europe. In the period 2008-2011 he was responsible for GE's investments and partnerships in banks in high growth emerging markets such as Turkey, Thailand, Taiwan, Central America and Colombia and served on the Boards of these Banks. He also led a major divestment programme for GE Capital Global Banking. In 1981 - 1991 Des worked for Ulster Investment Bank Limited in Corporate Banking and headed up its IFSC activities. He also worked with Woodchester Investments plc; Cambridge Group and Arthur Andersen. Des has a B.Comm Degree from UCC and is a Fellow of the Institute of Chartered Accountants in Ireland

GROUP AUDIT COMMITTEE

Trevor Bowen, Chairman

Chris Campbell

Sir Nigel Hamilton

Dr Philip Nolan

Des O'Shea

Bridget Rosewell

ULSTER BANK LIMITED

DIRECTORS AND EXECUTIVES (continued)

DIVISIONAL HEADS

R Donnan	Retail Markets
D Thomas	Corporate Markets
S Daniels	Group Human Resources
E Graham	Business Services
R Bergin	Communications & Corporate Affairs
J McAdam	Global Restructuring Group/Non-Core Ireland
C Pierce	Group Strategy

COMPANY SECRETARIES

R Bergin
E Dignam (Deputy)
R Curran (Assistant)

HEAD OFFICE

11-16 Donegall Square East, Belfast, BT1 5UB