Company Registered Number: 00036695

COUTTS & COMPANY
ANNUAL REPORT AND ACCOUNTS
For the year ended 31 December 2019

Coutts

STRATEGIC REPORT

The directors of Coutts & Company ("the Bank") present their Annual Report, together with audited consolidated financial statements of the Bank and its subsidiaries (together "the Group") for the year ended 31 December 2019. The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and as adopted by the European Union (EU), which constitutes a body of generally accepted accounting principles (GAAP).

Principal activities

The principal activity of the Group is to provide a wide range of banking, lending and wealth management services to high net worth individuals and their businesses.

The Bank has a clear vision to be the Best Private Bank in the UK. This is measured through three metrics: client satisfaction, colleague engagement and financial returns. To achieve this vision, we have prioritised digitising our client experience, investing in our people, simplifying our business and delivering innovation to our clients. Successful implementation of these will allow us to continue to generate sustainable growth.

The Bank is a subsidiary of The Royal Bank of Scotland Group plc (RBS Group), which provides support and access to all central resources. The Bank leverages its relationship with its immediate parent National Westminster Bank Plc (NWB), NatWest Holdings Limited (NWH), the parent of the ring-fenced sub-group and the RBS Group to continue to improve the quality and efficiency of the services and products provided. Copies of the annual report of RBS Group can be obtained from Corporate Governance and Regulatory Affairs, RBS Gogarburn, Edinburgh EH12 1HQ, the Registrar of Companies or through the RBS Group website, www.rbs.com.

Business review

The directors are pleased with the progress made against our key performance indicators: we have seen improvements in our client satisfaction and colleague engagement metrics which are at their highest levels in recent history. Our return on equity (RoE) is now 16.3%, down by 1% point over last year, as we are not receiving the same level of funding deposit benefit due to the lower interest rate environment. The cost of services provided by NWB Group companies (comprising National Westminster Bank Plc and its subsidiaries) have also increased.

We continue to innovate across our business, investing in the online Coutts Invest pension product, e-signing for lending products, voice biometrics for Coutts 24, and in the way we align our personal client touch points to meet client needs. Over 70% of our eligible client base are now enrolled for digital banking and we are piloting new functionality whereby clients are able to interact with advisors digitally. Coutts Connect, an exclusive online client networking service, has been developed to enable clients to interact digitally for their mutual benefit.

In addition to our strong financial performance, we are delivering on being 'more than a bank'.

Our clients' increasing awareness of our investment expertise and performance as their investment manager is demonstrated by the strong adoption of our discretionary investment services.

The Banks net promoter score grew 8 points in 2019 to end at 43 exceeding internal targets and reflecting its continued commitment to be the Best Private Bank in the UK for its clients.

The Bank continues to be recognised externally, winning awards during 2019 including:

- Best Private Bank in the UK and Best Private Bank for Philanthropy (Global Finance),
- Best UK Private Bank (Spears Management),
- Best Private Bank for innovation (Global Finance - World's Best Private Bank Awards),
- Best Private Bank for Philanthropic Services (Global Finance – World's Best Private Bank Awards).

STRATEGIC REPORT

Performance highlights	2019 £m	2018 £m
Total income	690	681
Operating expenses	(397)	(367)
Loan impairment release	7	7
Operating profit before tax	300	321
Tax charge	(80)	(86)
Profit and total comprehensive income for the year	220	235
Loans to customers - amortised cost	14,792	13,566
Customer deposits	26,390	26,527
Assets under Management and Administration (AuMA)	28,473	24,758
Customer loan:deposit ratio	56.1%	51.1%
RoE[1]	16.3%	17.3%
Cost:income ratio (C:I ratio)	57.5%	53.9%
Net Interest Margin (NIM)	3.19%	3.36%

Note:
(1) Return on equity is calculated using annual profit for the period attributable to ordinary shareholders' and owners equity at the year end.

Financial performance

The Group's financial performance is presented in the Consolidated statement of comprehensive income on page 42.

RoE has decreased 1% point, down from 17.3% to 16.3% reflecting a lower operating profit.

Operating profit before tax has declined by 6.5%, £21 million, from £321 million to £300 million driven by increased expenses, partially offset by higher revenue.

Despite an uncertain economic environment, income has grown by £9 million in the year. Income growth is predominately as a result of higher loan balances. This has been offset in part by a decrease in NIM from 3.36% to 3.19% due to reduced deposit funding benefits from NWB.

We have continued to grow our loan book with balances increasing from £13.6 billion to £14.8 billion driven primarily by an increase in mortgage lending to clients. Deposit balances have remained consistent over the year.

The Bank is the Centre of Excellence (CoE) for client investment AuMA for the whole of RBS Group. It manages portfolios totalling £28.5 billion as at 31 December 2019 (2018 - £24.8 billion), £7.2 billion of these assets relate to clients of other RBS Group companies for which the Bank receives a management fee. The £3.7 billion increase is as a result of strong business performance including £0.9 billion net new business, and financial market recovery in our investment business, following the sharp market fall in Q4 2018.

Based on indicative peer group analysis and comparison of our investment portfolios over the financial year, we remain within the top quartile for investment performance on all Sterling portfolios over 1, 3 and 5 years. We continue to focus on Responsible Investing and embedding environmental, social and governance metrics across our decision making and investment process. We are proud to have been awarded an 'A' grade or above in each of the key categories except one as assessed by the UN's Principles of Responsible Investment and achieved the highest possible rating for investment strategy and governance.

Operating expenses increased £30 million from £367 million to £397 million. £17 million of this was due to higher service charges from NWB and £3 million due to the first full year of consolidation of RBS Asset Management Holdings Limited (acquired 1 March 2018). The remainder came from one off operational expenses. The C:I ratio has increased 3.6% points from 53.9% to 57.5%.

Continued improvements to the modelling of IFRS 9 Expected credit loss (ECL) impairments and the release of specific client provisions have contributed to a net loan impairment release of £7 million in 2019 (2018 - £7 million).

The Common Equity Tier 1 (CET1) ratio was 12.0%. Profits earned during the period helped support payment of dividends to the parent company NWB of £215 million. Risk Weighted Assets (RWAs) increased by £0.8 billion in 2019 to £9.3 billion primarily reflecting an increase in lending.

At the end of the year, the balance sheet, on page 43, showed total assets of £34.0 billion (2018 - £34.3 billion), reflecting £14.8 billion of loans to customers (2018 - £13.6 billion) and £18.7 billion (2018 - £20.2 billion) of funds placed with NWB.

The principal source of funds for the Bank is its client deposits. At the end of the year, the balance sheet showed total liabilities and equity of £34.0 billion (2018 - £34.3 billion) including customer deposits of £26.4 billion (2018 - £26.5 billion).

Ring-fencing

UK ring-fencing legislation required the separation of essential banking services from investment banking services from 1 January 2019 within the RBS Group. The Bank forms part of the NWH Group ring-fenced banking group and is in compliance with the legislation.

Outlook

The Bank provides banking, lending and wealth management services predominantly to clients in the UK and engages with it's clients in new and innovative ways to deliver a premium service. The Bank continues to undertake preparations to seek to ensure that any potential business disruption as a result of Brexit is minimised.

STRATEGIC REPORT

Prevailing uncertainty regarding the terms of the UK's withdrawal from the European Union

Following the EU Referendum in June 2016, and pursuant to the exit process triggered under Article 50 of the Treaty on European Union in March 2017 and the ratification of the withdrawal agreement by the UK Parliament and the European Parliament, the UK ceased to be a member of the EU and the European Economic Area ('EEA') on 31 January 2020 ('Brexit') and entered a transition period, currently due to expire on 31 December 2020. During this transition period, the UK retains the benefits of membership of the EU's internal market and the customs union but loses its representation in the EU's institutions and its role in EU decision-making.

The UK and EU are currently seeking to determine the terms of their future relationship by the end of the transition period, and the resulting economic, trading and legal relationships with both the EU and other counterparties currently remain unclear and subject to uncertainty. If the UK and EU do not agree a new comprehensive trade agreement by the end of the transition period and the transition period is not extended, then it is expected that the UK will default to World Trade Organization terms.

The direct and indirect effects of the UK's exit from the EU and the EEA could have a potential impact on the Bank's operations and as a result may potentially impact the Bank's profitability, competitive position, business model and product offering. The longer term effects of Brexit on the Bank's operating environment are difficult to predict, and are subject to wider global macro-economic trends and events, but may impact the Bank and its clients and counterparties who are themselves dependent on trading with, or personnel from, the EU and may result in or be exacerbated by periodic financial volatility and slower economic growth in the Crown Dependencies, the UK, the rest of Europe and potentially the global economy. The extent of the impact of Brexit remains highly uncertain and will be linked to the nature and form of the UK's future relationship with the EU.

Uncertainty regarding the commercial and operational impacts arising from Coronavirus Disease 2019 (Covid-19)

Coronaviruses are a large family of viruses that cause illness ranging from the common cold to more severe diseases causing death.

The Bank is actively monitoring the current and potential impact on the Bank's activities and the wider macroeconomic environment.

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 estimation uncertainty are included in the accounting policies on page 50.

Stakeholder engagement and s.172 (1) statement

The Board's 2019 objectives prioritised stakeholder engagement, specifically understanding and considering the stakeholder voice in Board decision-making. During 2019 the Board undertook a variety of activities to engage with key stakeholders and bring their voice into the Boardroom. These activities were guided by a Board planning session which identified the Bank's key stakeholder groups. Further details are set out below.

This section of the Strategic report describes how the directors have had regard to the matters set out in section 172(1) (a) to (f), and forms the directors' statement required under section 414CZA, of The Companies Act 2006.

Board Training and support on s.172(1) duties

Directors are supported in the discharge of their duties by the Company Secretary. All directors receive guidance on their statutory duties including Section 172(1) and were briefed on the reporting requirements introduced by the Companies (Miscellaneous Reporting) Regulations 2018 in advance of the effective date, and continue to be briefed on relevant matters on an ongoing basis. A new approach to Board and committee papers has been introduced across RBS Group, including the Bank, with greater focus on ensuring relevant stakeholder interests are clearly articulated; guidance on documenting decisions has also been refreshed to ensure these are recorded in a consistent manner across RBS Group.

Clients

Meeting the needs of clients is central to the Bank's long-term success and is a constant feature of Board discussions and decisions. Client Net Promoter Scores are regularly reviewed by the Board and Executive Committee, and represent a key performance metric. In addition, the directors meet a wide range of clients through the course of the year, at client events and individual meetings.

The Bank also operates a Client Council, bringing together circa 600 clients from across the spectrum of our client base. Through the Client Council, the Bank undertakes research several times a year, to better understand clients' views and to help it evolve in line with clients' needs.

Colleagues

Our colleagues

As at 31 December 2019, NWB had seconded 1,584 colleagues to Bank (2018 – 1,537) (full time equivalent basis, including temporary workers). Details of related costs are included in note 3 to the consolidated accounts.

Engaging our colleagues

A highly engaged workforce is crucial in helping the Bank to achieve its vision to be the 'Best Private Bank in the UK'. To achieve this the Bank is striving to ensure it is a really great place to work.

Every year colleagues are asked to share their views on what it is like to work for the Bank, via a collective opinion survey. Over the last 3 to 4 years levels of engagement have improved year on year, with 2019 results being the most positive seen to date. Key measures of engagement, leadership and culture have increased further and the Bank is now ahead of Global Financial Services standards in almost all categories.

Colleague voice

The Board promotes colleague voice in the Boardroom through a variety of channels, including the operation of an 'open chair', which provides the opportunity for junior colleagues to attend Board meetings. The Bank also established a People Council in 2018 to represent colleagues at all levels and to act as custodian of the Bank's culture plan. The Council is made up of circa 50 individuals from across all parts of the Bank and is instrumental in shaping the agenda following the outputs of colleague surveys. It also provides an opportunity for the Executive Committee and Board to engage directly with colleagues and hear first hand about what it is like to work for the Bank, what is working well, where we could improve and any challenges we face.

Colleague consultation

The Bank's work with the People Council is further supplemented by RBS Group's colleague listening strategy. A Colleague Advisory Panel (made up of circa 30 colleagues, including representation from trade unions, works councils, colleague volunteers and colleague led-networks, from across the Group), was established in 2018 and allows direct input from colleagues on a range of issues. The outputs of these sessions are also shared with the Bank.

Speak Up
Where colleagues wish to report any concerns relating to wrong doing or misconduct, one of the ways they can do this is by raising their concerns via Speak Up, RBS Group's whistleblowing service. The 2019 colleague opinion survey showed the highest ever score when asking colleagues if they feel safe to speak up, as well as understanding the process of how they do that. In 2019, 27 cases were raised in the Bank, compared to 19 in 2018. No systemic issues were identified.

Building a healthy culture
The Board views building a high performing and healthy culture as also essential to the Bank's long-term success. The Bank's culture plan focusses on the themes of 'Our Way of Life', 'Our Potential' and 'Our Communities'. It is underpinned by the Bank's vision to be the 'Best Private Bank in the UK' and by 'Our Values'.

Our Values guide the way we serve our clients, how we manage and mitigate risk and they help us to focus on the long term rather than the short term.

Data from RBS Group's participation in the Banking Standard Board ('BSB') annual independent culture assessments further supports improving colleague sentiment and the building of a healthy culture. The data shows we have continued to make good progress, with improvements in all nine BSB categories.

The Bank also maintains a risk culture plan, aligned to the RBS Group's target of achieving a generative risk culture whereby "risk is simply part of the way people work and think".

Rewarding our colleagues
Individual performance objectives are clearly linked to our vision and strategy. We take a balanced approach to managing performance that is linked to reward. This includes the conduct and behaviour of individuals in addition to financial performance. Delivering for our clients is key, as is the management of risk. This balanced approach to reward recognises both what the individual has achieved and how they have achieved it. The overall contribution is underpinned by Our Values and we hold colleagues and leaders to account for performance and behaviours both of themselves and their team.

Health and wellbeing of our colleagues
Also part of our culture plan is 'Our Way of Life' - we believe that the wellbeing of colleagues forms a large part of making the Bank a great place to work. As an employer we want to make sure our colleagues have the right support to be healthy and happy at work and feel able to bring their whole self to work.

Within the Bank we have a network of over 90 Wellbeing Ambassadors. They are there for colleagues to reach out to and can provide practical support and advice. The Bank has a programme of events throughout the year that focus on physical, mental and financial wellbeing with a host of resources and tool kits available to colleagues.

Developing our colleagues
At the heart of our culture plan is Our Potential – we believe everyone has the potential to grow, and the right to be supported to perform to the best of their abilities. We invest in the future with ongoing coaching, training, support and encouragement. Each individual has a personal development plan and core requirements for Continued Professional Development (CPD) are mandatory.

Community, Environment and Sustainability
Another important element in our culture plan is 'Our Communities'. We care about the environment and our local communities and we encourage everyone to get involved in a bigger purpose and make a difference. Every colleague is able to take three days paid leave per year to volunteer in their local community or for a charity of their choice. We also encourage charitable donations through the use of payroll giving.

The Bank has a colleague nominated charity on which we focus fund raising efforts and events throughout the year. During 2019 the chosen theme was mental health.

We have a long and distinguished history of supporting philanthropic causes derived from the work of Angela Burdett-Coutts. Angela was a progressive 19th century philanthropist who was concerned with breaking cycles of poverty and the provision of basic human need. The Bank draws on this legacy through the work of the Coutts Charitable Foundation ('the Foundation'). The Foundation was established to support sustainable solutions which tackle the causes and consequences of poverty. The core focus of the Foundation is supporting women and girls in the UK.

The Board is committed to managing the wider social, environmental and economic impacts of the Bank's operations. This includes the way it deals with sustainability issues in its supply chain. RBS Group's Modern Slavery Statement and details of the Supplier Code of Conduct, both of which apply to the Bank, are available on the Group's website (www.rbs.com).

The challenge posed by climate change is recognised by the Board. During 2019, activity was mobilised within the Bank to respond to the climate challenge. This included a client event in July 2019 focused on the climate crisis, with Sir David Attenborough, Bank of England Governor Mark Carney, Chair of the UK Committee on Climate Change Chris Stark and Sue Garrard, formerly of Unilever, all attending as guest speakers. Updates are being provided to the Board and the Bank is playing a full part in RBS Group's response to climate crisis. Details on RBS Group's response to climate change can be found within the RBS Group Annual Report & Accounts 2019.

Youth employment
In September 2019 we welcomed 15 graduates into the Private Banking graduate scheme plus 9 interns over the summer for 10 weeks. Gender balance and diversity is critical for these schemes in order to support a balanced workforce for the future. In 2019 we had a 50:50 gender balance on both the graduate and intern schemes. To support an inclusive workforce and social mobility we hold two insight weeks per year to encourage young people from all backgrounds, gender and ethnicity to come along and find out about career options within the Bank. Following these weeks we offered 8 candidates a place on our Internship programme for 2020, of which 6 where female, 2 male and all were Black, Asian and Minority Ethnic ('BAME').

Employment of people with disabilities
Within the RBS Group we have a network called Enable that is dedicated to making sure we are fully inclusive and that everyone is valued as an individual, regardless of disability.

In line with RBS Group policy, the Bank ensures that prospective candidates with disabilities are considered for employment. Once they become a colleague we are committed to training, career development and promotion based on merit. If a colleague becomes disabled during their career, it is the Bank's policy, wherever possible, to retain them in their existing role or to re-deploy to a more suitable role. Training is available for all line managers to help raise disability awareness across the Bank.

Inclusion

We know that more diverse and inclusive organisations perform better – inclusivity is not only the right thing to do but there is a strong business case for it.

Our vision to be the Best Private Bank in the UK is dependent on having the best people that reflect our client base and wider society. It is therefore essential that we continue to build a diverse and inclusive organisation - this means that everyone has a seat at the table and everyone's voice is heard.

We have a strong and active Respect, Diversity and Inclusion Council ('RD&I Council') that is led by a group of colleagues who do a great job at grass roots level. The strands of the RD&I Council include faith, disability, ethnicity, age, gender, LGBT+ and social mobility.

The Board monitors diversity and inclusion, to check progress against key measures. Internal policies, such as on recruitment and promotion, support this agenda.

Following the change of employer to NWB for our colleagues, published metrics on the gender pay gap now form part of NWB's reporting, as these are determined by the legal entity employer. The Bank nonetheless remains committed to ensuring a balanced gender representation across roles in the business. The RD&I Council continues to work towards helping the Bank achieve its goal of a gender balanced workforce by 2030.

Suppliers

The Board recognises the key role suppliers play in ensuring the Bank delivers a reliable service to clients. During the year, the Board held a 'teach-in' session with RBS Group's Supply Chain Services function, which manages the Bank's material third party suppliers, and also considered a paper at Board regarding the framework for managing intra-group as well as third party suppliers. The Board will continue to focus on the provision of services to the Bank by its supplier community.

Regulators

The Board recognises the importance of open and continuous dialogue with regulators. The Chair, CEO and Chair of the Risk and Audit Committees meet regularly with the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA), through Continuous Assessment and Proactive Engagement meetings.

Shareholder

The Bank recognises the benefits that being part of a wider Group provides, for example in terms of the ability to call on extensive IT and other specialist resources, for instance on cyber-crime defenses. The shareholder's perspective is provided through interactions at management and Board levels. Cross referrals between clients of the Bank and customers of NWH have continued to increase.

How stakeholder interests have influenced decision making

The Bank's key stakeholders and the range of engagement methods used by directors to understand their views and interests are described above.

The Bank recognises the importance of engaging with stakeholders to help inform it's strategy and Board decision-making. Relevant stakeholder interests, including those of colleagues, suppliers, customers and others, are considered by the Board when it takes decisions.

The Bank defines principal decisions as those that are material or of strategic importance, but also those that are significant to any of its key stakeholder groups.

In making its decisions, the Board considers the outcomes of relevant stakeholder engagement as well as the need to maintain a reputation for high standards of business conduct, and to consider the long-term consequences of its decisions. An example of such a decision related to the approval of a discretionary investment to enhance parts of the Bank's premises at 440 Strand. Factors considered in the decision and options looked at, included: creating better client facilities, enhancing facilities for colleagues working in the building and meeting the needs of the Bank's shareholder. The Board also reviewed the potential impacts on tenants in the property's retail units and on the wider community, a further consideration being to ensure that any changes enhanced the immediate neighbourhood surrounding the building and was in keeping with the Bank's value of being a 'good neighbour'.

In reaching its decision, the Board was focused on ensuring that a solution was found that considered these stakeholder considerations and in a way that would reflect Coutts' commitment to developing as a sustainable and responsible business.

By order of the Board:

The Rt Hon Lord Waldegrave of North Hill
Chair

Date: 12 March 2020

Coutts & Company is registered in England and Wales No. 00036695

BOARD OF DIRECTORS AND SECRETARY

Chair and Independent Non-Executive Director
The Rt Hon Lord Waldegrave of North Hill
Remuneration, Nominations (Chair)

Executive Directors
Peter Gordon Flavel
Chief Executive

Andrew Richard Kyle
Finance Director

Independent Non-Executive Directors
Francesca Barnes
Audit (Chair), Risk (Chair), Remuneration, Nominations

Mark Joseph Lund
Audit, Risk, Remuneration, Nominations

Linda Hamilton Urquhart OBE
Audit, Risk, Remuneration (Chair), Nominations

Non-Independent Non-Executive Director
Matthew Edward James Waymark
Audit, Risk

Company Secretary
Ralph Ricks

Audit	Member of the Audit Committee
Risk	Member of the Risk Committee
Remuneration	Member of the Performance and Remuneration Committee
Nominations	Member of the Nominations Committee

For additional detail on the activities of the Committees above, refer to the Report of the directors.

Appointments & Resignations
Michael Robert Regan (Finance Director) resigned on 31 January 2019

Andrew Richard Kyle (Finance Director) appointed on 21 February 2019

Marie Claire Baird (Non-Executive Director) resigned on 21 May 2019

Matthew Edward James Waymark (Non- Executive Director) appointed on 9 March 2020

Auditors
Ernst & Young
Statutory Auditor
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Coutts & Company
Registered in England and Wales No. 00036695

CAPITAL AND RISK MANAGEMENT

Risk management framework

The Bank operates an integrated risk management framework, centred around the embedding of a strong risk culture. The framework ensures the tools and capability are in place to facilitate risk management and decision-making across the organisation.

The Bank's strategy is informed and shaped by an understanding of the risk landscape, including a range of significant risks and uncertainties in the external economic, political and regulatory environment. Identifying these risks and understanding how they affect the Bank informs risk appetite and risk management practice.

Presentation of information

Risk management is generally conducted on an overall basis within RBS Group such that common policies, procedures, frameworks and models apply across the RBS Group. Therefore, for the most part, discussion on these qualitative aspects reflects those in the RBS Group as relevant for the businesses and operations in the Bank.

During 2019, a number of enhancements to the risk management framework were developed. The increasing significance of climate risk was considered as part of these developments and will be fully integrated as part of the implementation of the enhanced framework in 2020.

Risk culture is essential if the Bank is to achieve its ambition to build a truly client-focused bank. The Bank's risk culture target is to make risk simply part of the way that colleagues work and think.

A focus on leaders as role models, and action to build clarity, develop capability and motivate employees to reach the required standards of behaviour are key to achieving the risk culture target. Colleagues are expected to:

- Take personal responsibility for understanding and proactively managing the risks associated with individual roles.
- Respect risk management and the part it plays in daily work.
- Understand the risks associated with individual roles.
- Align decision-making to the RBS Group's risk appetite.
- Consider risk in all actions and decisions.
- Escalate risks and issues early; taking action to mitigate risks and learning from mistakes and near-misses.
- Challenge others' attitudes, ideas and actions.
- Report and communicate risks transparently.

The Bank's target risk culture behaviours are embedded in Our Standards and are clearly aligned to the core values of "serving customers", "working together", "doing the right thing" and "thinking long term". These act as an effective basis for a strong risk culture because Our Standards are used for performance management, recruitment and development.

Risk governance underpinned by the three lines of defence model, is essential to ensure the right decisions are being made by the right people at the right time. Governance includes regular and transparent risk reporting as well as discussion and decision-making at senior management committees, which informs management strategies across the organisation.

Risk appetite supported by a robust set of principles, policies and practices, defines our levels of tolerance for a variety of risks and provides a structured approach to risk-taking within agreed boundaries.

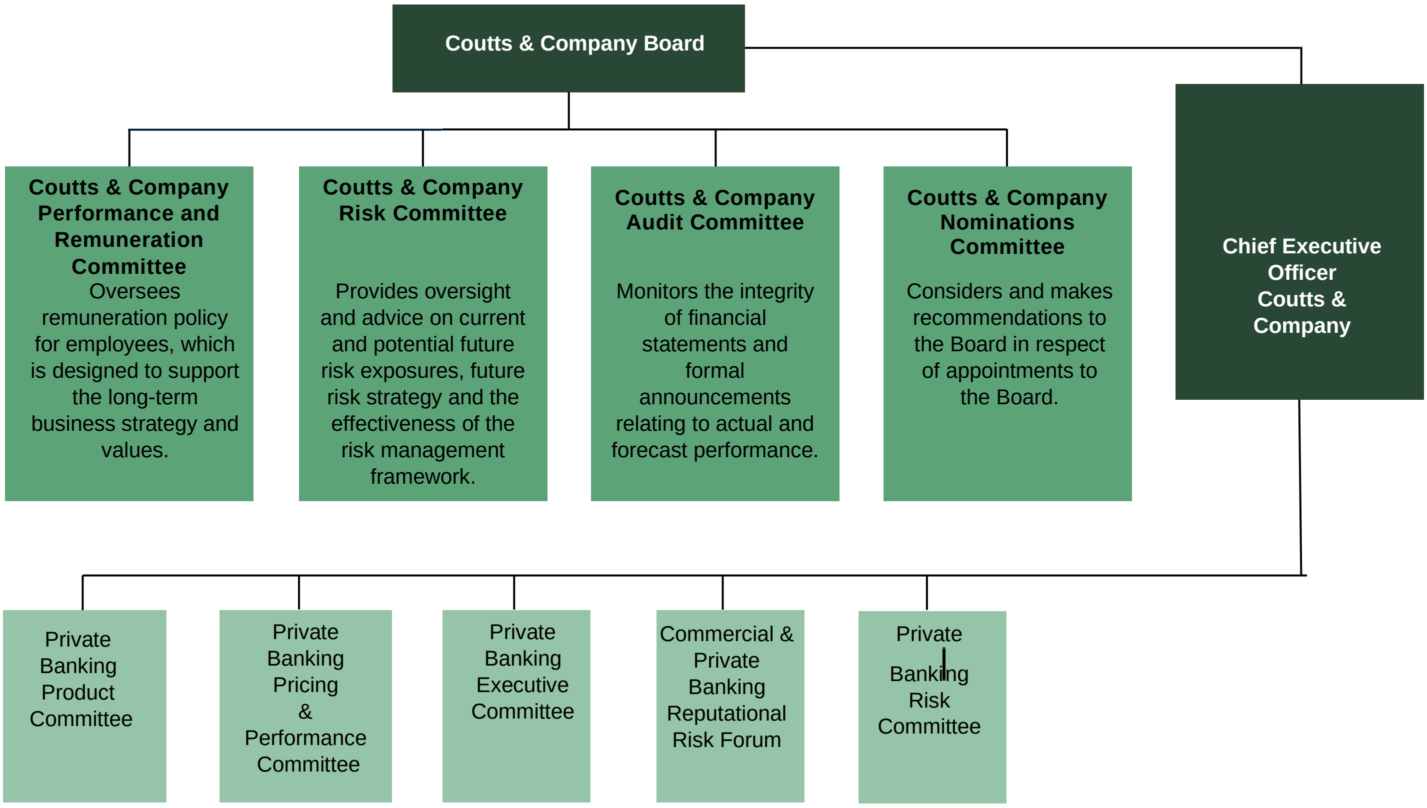
Training is supported by a wide range of learning, both technical and behavioural, across the risk disciplines. This training can be mandatory, role-specific or for personal development and enables colleagues to develop the capabilities and confidence to manage risk effectively.

Code of Conduct is in place across all entities within RBS Group. It provides guidance on the behaviour expected of colleagues and describes the principles that must be followed. For more information, refer to page 112 of the RBS Group Annual Report & Accounts.

Risk management framework continued

Committee structure

The diagram illustrates the Bank's Board and committee structure in 2019 and the purposes of the main committees.



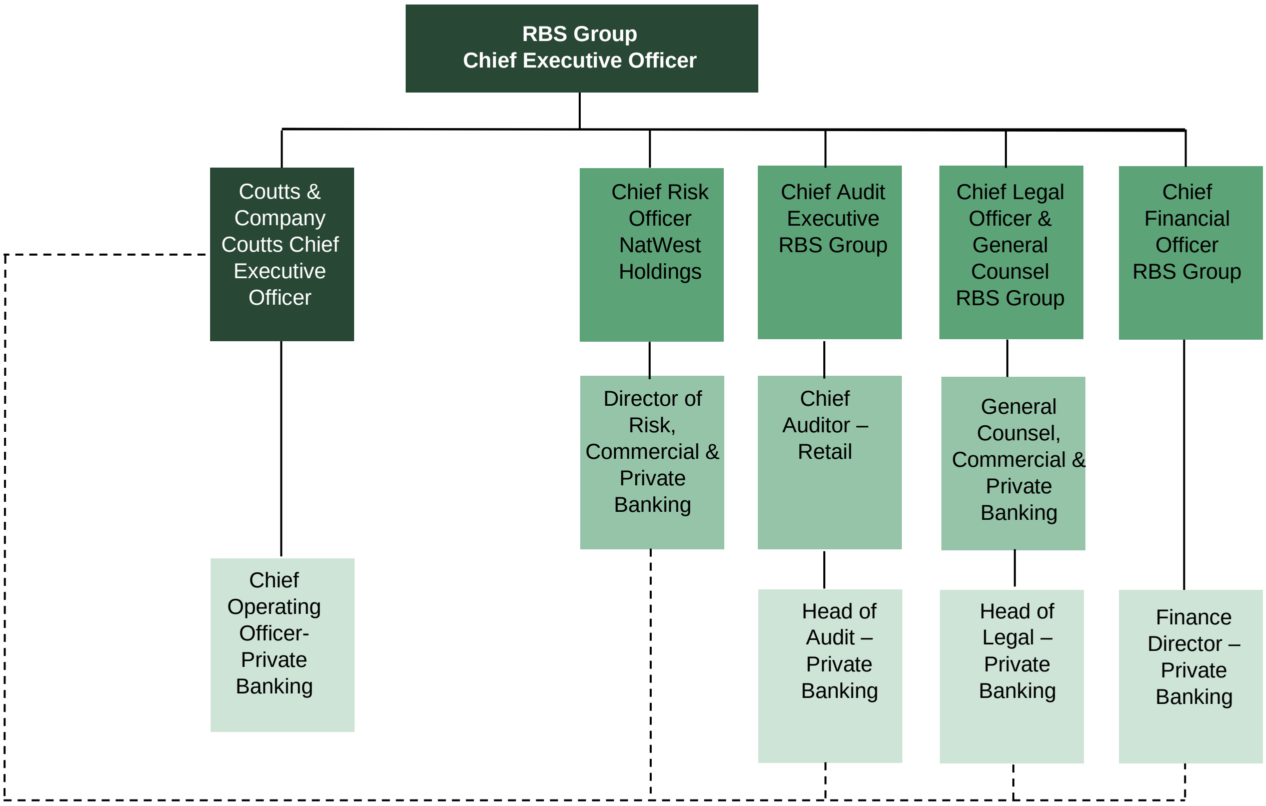
Notes:

(1) The Commercial & Private Banking Reputational Risk Forum is accountable to the Chief Executive Officer, Coutts & Company and the Chief Executive Officer, Commercial Banking.

Risk management framework continued

Risk management structure

The diagram illustrates RBS Group's and the Bank's risk management structure in 2019.



Notes:

(1) The Director of Risk, Commercial & Private Banking reports directly to the Chief Risk Officer NatWest Holdings, with a secondary reporting line to the Coutts & Company Chief Executive Officer. The Director of Risk, Commercial & Private Banking has an additional reporting line to the chair of the Coutts & Company Risk Committee, and a right of access to the committee. As of January 2020, the Director of Risk, Commercial & Private Banking role was split into two roles (Director of Risk, Commercial Banking and Director of Risk, Private Banking).

(2) The Head of Audit – Private Banking reports directly to the Chief Auditor – Retail, with a secondary reporting line to the Coutts & Company Chief Executive Officer. The Head of Audit – Private Banking, also has a right of access to the Coutts & Company Audit Committee.

(3) The Head of Legal – Private Banking reports directly to the General Counsel, Commercial & Private Banking, with a secondary reporting line to the Coutts & Company Chief Executive Officer.

(4) The Finance Director – Private Banking reports directly to the Chief Financial Officer, with a secondary reporting line to the Coutts & Company Chief Executive Officer.

CAPITAL AND RISK MANAGEMENT

Risk management framework continued

Three lines of defence is used across RBS Group to articulate accountabilities and responsibilities for managing risk.

The first line is accountable for managing its own risks within the appetite set by the Board. It incorporates most roles in the Bank. It includes those in the client-facing roles, Technology and Services as well as some support functions such as Human Resources, Communications & Marketing and Finance.

The second line is responsible for oversight and challenge of first line risk management as well as leading the articulation, design and development of risk culture and appetite. It comprises the Risk function as well as the policy and control elements of Human Resources, Legal and Finance.

The third line of defence is Internal Audit, which provides assurance on the appropriateness of the design and operational effectiveness of governance, risk management and internal controls to monitor and mitigate material risks.

Risk controls and limits are an integral part of the risk appetite approach and a key part of embedding risk appetite in day-to-day risk management decisions. A clear tolerance for material risk types is set in alignment with business activities.

Risk identification and measurement within the risk management process comprise:

- Regular assessment of the overall risk profile, incorporating market developments and trends, as well as external and internal factors.
- Monitoring of the risks associated with lending and credit exposures.
- Assessment of trading and non-trading portfolios.
- Review of potential risks in new business activities and processes.
- Analysis of potential risks in any complex and unusual business transactions.

Risk treatment and mitigation is an important aspect of ensuring that risk profile remains within risk appetite. Risk mitigation strategies are discussed and agreed with the businesses. When evaluating possible strategies, costs and benefits, residual risks (risks that are retained) and secondary risks (those caused by the risk mitigation actions) are considered. Monitoring and review processes are in place to track results. Significant and emerging risks that could affect future results and performance are reviewed and monitored. Action is taken to mitigate potential risks as and when required. Further in-depth analysis, including the stress testing of exposures relative to the risk, is also carried out.

Stress testing is a key risk management tool and a fundamental component of the approach to capital management. It is used to quantify, evaluate and understand the potential impact of specified changes to risk factors on the financial strength of the Bank, including its capital position.

Stress testing includes:

- Scenario testing, which examines the impact of a hypothetical future state to define changes in risk factors.
- Sensitivity testing, which examines the impact of an incremental change to one or more risk factors.

The process for stress testing consists of four broad stages:

Define scenarios

- Identify business specific vulnerabilities and risks.
- Define and calibrate scenarios to examine risks and vulnerabilities.
- Formal governance process to agree scenarios.

Assess impact

- Translate scenarios into risk drivers.
- Assess impact to current and projected P&L and balance sheet.

Calculate results and assess implications

- Aggregate impacts into overall results.
- Results form part of risk management process.
- Scenario results are used to inform business and capital plans.

Develop and agree management actions

- Scenario results are analysed by subject matter experts and appropriate management actions are then developed.
- Scenario results and management actions are reviewed and agreed by senior management through executive committees including Executive Risk Committee, Board Risk Committee and the Board.

Stress testing is used widely across RBS Group. Specific areas that involve capital management include:

- *Strategic financial and capital planning* – by assessing the impact of sensitivities and scenarios on the capital plan and capital ratios.
- *Risk appetite* – by gaining a better understanding of the drivers of, and the underlying risks associated with, risk appetite.
- *Risk identification* – by better understanding the risks that could potentially affect the Bank's financial strength and capital position.
- *Risk mitigation* – by identifying actions to mitigate risks, or those that could be taken, in the event of adverse changes to the business or economic environment. Key risk mitigating actions are documented in the Group's recovery plan.

Reverse stress testing is also carried out in order to identify circumstances that may lead to specific, defined outcomes such as business failure. Reverse stress testing allows potential vulnerabilities in the business model to be examined more fully.

Capital, liquidity and funding risk

Definitions

Capital

Capital consists of reserves and instruments issued that are available, have a degree of permanency and are capable of absorbing losses. A number of strict conditions set by regulators must be satisfied to be eligible as capital.

Capital adequacy risk is the risk that there is or will be insufficient capital and other loss absorbing debt instruments to operate effectively including meeting minimum regulatory requirements, operating within Board approved risk appetite and supporting its strategic goals.

Capital, liquidity and funding risk continued

Liquidity and Funding
Liquidity consists of assets that can be readily converted to cash within a short timeframe at a reliable value. Liquidity risk is the risk of being unable to meet financial obligations as and when they fall due.

Funding consists of on-balance sheet liabilities that are used to provide cash to finance assets. Funding risk is the risk of not maintaining a diversified, stable and cost-effective funding base.

Liquidity and funding risks arise in a number of ways, including through the maturity transformation role that the Bank performs. The risks are dependent on factors such as:
- Maturity profile;
- Composition of sources and uses of funding;
- The quality and size of the liquidity portfolio;
- Commercial market conditions; and
- Depositor and investor behaviour.

Sources of risk

Capital
The eligibility of instruments and financial resources as regulatory capital is laid down by applicable regulation. Capital is categorised by applicable regulation under two tiers (Tier 1 and Tier 2) according to the ability to absorb losses on either a going or gone concern basis, degree of permanency and the ranking of absorbing losses.

There are three broad categories of capital across these two tiers:

- Core Tier 1 (CET1) capital - CET1 capital must be perpetual and capable of unrestricted and immediate use to cover risks or losses as soon as these occur. This includes ordinary shares issued and retained earnings.
- Additional Tier 1 (AT1) capital - This is the second type of loss absorbing capital and must be capable of absorbing losses on a going concern basis. The instruments are either written down or converted into CET1 capital when a pre-specified CET1 ratio is reached.
- Tier 2 capital - Tier 2 capital is supplementary capital and provides loss absorption on a gone concern basis. Tier 2 capital absorbs losses after Tier 1. It typically consists of subordinated debt securities with a minimum maturity of five years.

Minimum requirement for own funds and eligible liabilities (MREL) - In addition to capital, other specific loss absorbing instruments, including senior notes issued by the Bank, may be used to cover certain gone concern capital requirements which, in the EU, is referred to as MREL. Gone concern refers to the situation in which resources must be available to enable an orderly resolution, in the event that the Bank of England (BoE) deems that the Bank has failed or is likely to fail.

Liquidity
Liquidity risk is managed as part of the UK Domestic Liquidity Sub Group (UK DoLSub), which is regulated by the PRA and comprises NWH's four licensed deposit taking UK banks: National Westminster Bank Plc, The Royal Bank of Scotland plc, Coutts & Company, and Ulster Bank Limited.

NWH maintains a prudent approach to the definition of liquidity resources. NWH manages its liquidity to ensure it is always available when and where required, taking into account regulatory, legal and other constraints.

Liquidity resources are divided into primary and secondary liquidity as follows:

- Primary liquid assets include cash and balances at central banks, Treasury bills and other high quality government and US agency bonds.
- Secondary liquid assets are eligible as collateral for local central bank liquidity facilities. These assets include own-issued securitisations or whole loans that are retained on balance sheet and pre-positioned with a central bank so that they may be converted into additional sources of liquidity at very short notice.

Funding
The Bank is funded principally by its client deposits. Through NWB, the Bank retains access to a diversified set of funding sources, including Tier 2 capital and subordinated debt. The Bank also retains access to central bank funding facilities, should it become necessary.

Managing capital requirements
In line with paragraph 135 of IAS 1 'Presentation of Financial Statements', the Bank manages capital having regard to regulatory requirements. Regulatory capital is monitored and reported on an individual basis by the Bank.

Risk management

Capital
Capital management is the process by which the Bank ensures that it has sufficient capital and other loss absorbing instruments to operate effectively including meeting minimum regulatory requirements, operating within Board approved risk appetite, maintaining credit ratings and supporting strategic goals. Capital management is critical in supporting the Bank's business.

Capital planning is integrated into the Bank's wider annual budgeting process and is assessed and updated at least monthly.

Other elements of capital management, including risk appetite and stress testing, are set out on page 7 and 10 respectively.

Liquidity
Liquidity risk takes into account regulatory, legal and other constraints to ensure sufficient liquidity is available where required to cover liquidity stresses.

The size of the liquidity portfolio held in the UK DoLSub is determined by referencing NWH's liquidity risk appetite. NWH retains a prudent approach to setting the composition of the liquidity portfolio, which is subject to internal policies and limits over quality of counterparty, maturity mix and currency mix.

NWB manages the majority of the UK DoLSub's liquidity portfolio under the responsibility of the RBS Group Treasurer.

Funding
The Bank manages funding risk through a comprehensive framework which measures and monitors the funding risk on the balance sheet.

Client deposits provide more funding than client loans utilise.

Capital, liquidity and funding risk continued

Minimum Capital Requirements

Capital adequacy ratios

The Bank is subject to minimum capital requirements relative to RWAs. The table below summarises the minimum ratios of capital to RWAs that the Bank is expected to have to meet.

Type	CET1	Total Tier 1	Total capital
Minimum capital requirements	4.5%	6.0%	8.0%
Capital conservation buffer	2.5%	2.5%	2.5%
UK countercyclical capital buffer [(1)]	0.9%	0.9%	0.9%
Total [(2)]	7.9%	9.4%	11.4%

Notes:
(1) The countercyclical capital buffer (CCyB) applied to UK designated assets is set by the Financial Policy Committee (FPC). Firm specific CCyB is based on a weighted average at CCyB rates applicable to countries in which the Bank has exposures. As at the reporting date the UK CCyB was 1.0%.
(2) The minimum requirements do not include any capital that the Bank may be required to hold as a result of the Pillar 2 assessment.

Leverage ratio

Amendments to the Capital Requirements Regulation (CRR) introduced by CRR2 will result in a binding 3% Tier 1 minimum capital leverage ratio from 28 June 2021. The Bank is already above this minimum.

Liquidity and funding ratios

The Bank is a member of the UK DoLSub, which is collectively subject to the minimum Liquidity Coverage Ratio requirement of 100%.

Capital, liquidity and funding risk continued

Risk measurement

Capital

	Bank	
	Unaudited(1)	Unaudited(1)
	Dec 2019	Dec 2018
Composition of regulatory capital	£m	£m
Shareholders' equity	1,375	1,357
Other equity instruments	(200)	(200)
	1,175	1,157
Regulatory adjustments and deductions		
Goodwill and other intangible assets	(38)	(30)
Other regulatory adjustments	(20)	(123)
	(58)	(153)
Common equity Tier 1 capital	1,117	1,004
Additional Tier 1 capital		
Qualifying instruments and related share premium	202	202
Tier 1 capital	1,319	1,206
Qualifying Tier 2 capital		
Paid up capital instruments and subordinated loans	266	266
Tier 2 capital	266	266
Total regulatory capital	1,585	1,472
Risk weighted assets by risk		
Credit risk	8,262	7,510
Counterparty risk	35	42
Market risk	9	6
Operational risk	1,004	861
Total risk weighted assets	9,310	8,419
Key capital ratios (2)		
CET1	12.0%	11.9%
Tier 1	14.2%	14.3%
Total capital	17.0%	17.5%

Notes:

(1) The capital metrics included in the above table have not been audited for the financial years ended 31 December 2019 and 31 December 2018.

(2) Key capital ratios represent capital as a proportion of risk weighted assets.

Capital, liquidity and funding risk continued

Liquidity and Funding Risk

Key liquidity and related metrics monitored in relation to the UK DoLSub includes:

- Liquidity coverage ratio;
- Stressed outflow coverage;
- Net stable funding ratio; and
- Loan to Deposit ratio.

These metrics are compiled in line with regulatory guidance or industry standards, with own interpretation applied where appropriate. Monitoring of these measures allows for ongoing assessment of the position of the overall UK DoLSub liquidity portfolio, and ensures regulatory targets are, at minimum, met or exceeded. The Bank's Liquidity metrics are monitored at the NWH Asset and Liabilities Committee.

Contractual maturity (audited)

The contractual maturity of assets and liabilities, shown in the following tables, highlight the maturity transformation which underpins the role of banks to lend longer-term but funded predominantly by short-term liabilities such as client deposits. In practice, the behavioural profile of many assets and liabilities differs from the contractual maturity.

	Group					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2019	£m	£m	£m	£m	£m	£m
Assets by contractual maturity						
Cash and balances at central banks	3	-	-	-	-	-
Loans to banks - amortised cost	104	39	-	-	-	-
Loans to customers - amortised cost	3,001	2,510	4,107	2,348	2,618	1,762
Amounts due from holding companies and fellow subsidiaries(1)	9,136	2,579	3,443	3,199	591	-
Total assets	12,244	5,128	7,550	5,547	3,209	1,762
Liabilities by contractual maturity						
Bank deposits	12	-	-	-	-	-
Customer deposits	26,041	352	-	-	-	-
Amounts due to holding companies and fellow subsidiaries(1)	290	740	2,095	2,024	493	-
Other financial liabilities	-	-	-	50	260	-
Subordinated liabilities	-	-	-	-	265	-
Total liabilities	26,343	1,092	2,095	2,074	1,018	-
Maturity gap	(14,099)	4,036	5,455	3,473	2,191	1,762
Cumulative maturity gap	(14,099)	(10,063)	(4,608)	(1,135)	1,056	2,818
Guarantees and commitments - notional amounts						
Guarantees(2)	73	-	-	-	-	-
Commitments(3)	2,843	-	-	-	-	-
	2,916	-	-	-	-	-

For notes related to this table, refer to page 15.

CAPITAL AND RISK MANAGEMENT

Capital, liquidity and funding risk continued

Contractual maturity (audited) continued

	Group					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2018	£m	£m	£m	£m	£m	£m
Assets by contractual maturity						
Cash and balances at central banks	2	-	-	-	-	-
Loans to banks - amortised cost	88	33	-	-	-	-
Loans to customers - amortised cost	2,650	2,315	3,759	2,083	2,434	1,725
Amounts due from holding companies and fellow subsidiaries(1)	10,436	2,824	3,709	3,483	54	-
Total assets	13,176	5,172	7,468	5,566	2,488	1,725
Liabilities by contractual maturity						
Bank deposits	5	-	-	-	-	-
Customer deposits	26,102	426	4	-	-	-
Amounts due to holding companies and fellow subsidiaries(1)	1,480	960	1,452	1,785	408	5
Subordinated liabilities	-	-	-	-	315	-
Total liabilities	27,587	1,386	1,456	1,785	723	5
Maturity gap	(14,411)	3,786	6,012	3,781	1,765	1,720
Cumulative maturity gap	(14,411)	(10,625)	(4,613)	(832)	933	2,653
Guarantees and commitments - notional amounts						
Guarantees(2)	75	-	-	-	-	-
Commitments(3)	2,986	-	-	-	-	-
	3,061	-	-	-	-	-

Notes:

(1) £1.9 billion of short dated intercompany assets and liabilities, which meet the IAS 32 criteria, have been netted in 2019. The 2018 balances of £1.8 billion have been presented gross.

(2) The Group is only called upon to satisfy a guarantee when the guaranteed party fails to meet its obligations. The Group expects most guarantees it provides to expire unused.

(3) The Group has given commitments to provide funds to clients under undrawn formal facilities, credit lines and other commitments to lend subject to certain conditions being met by the counterparty. The Group does not expect all facilities to be drawn, and some may lapse before drawdown.

	Bank					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2019	£m	£m	£m	£m	£m	£m
Assets by contractual maturity						
Cash and balances at central banks	3	-	-	-	-	-
Loans to banks - amortised cost	84	40	-	-	-	-
Loans to customers - amortised cost	2,878	2,419	3,948	2,228	2,495	1,690
Amounts due from holding companies and fellow subsidiaries(1)	9,694	2,579	3,443	3,199	591	-
Total assets	12,659	5,038	7,391	5,427	3,086	1,690
Liabilities by contractual maturity						
Bank deposits	12	-	-	-	-	-
Customer deposits	26,041	352	-	-	-	-
Amounts due to holding companies and fellow subsidiaries(1)	407	705	2,079	1,975	469	-
Other financial liabilities	-	-	-	50	260	-
Subordinated liabilities	-	-	-	-	265	-
Total liabilities	26,460	1,057	2,079	2,025	994	-
Maturity gap	(13,801)	3,981	5,312	3,402	2,092	1,690
Cumulative maturity gap	(13,801)	(9,820)	(4,508)	(1,106)	986	2,676
Guarantees and commitments - notional amounts						
Guarantees(2)	73	-	-	-	-	-
Commitments(3)	2,843	-	-	-	-	-
	2,916	-	-	-	-	-

For notes related to this table, refer to page 16.

Capital, liquidity and funding risk continued

Contractual maturity (audited) continued

	Bank					
	0-3 months	3-12 months	1-3 years	3-5 years	5-10 years	10-20 years
2018	£m	£m	£m	£m	£m	£m
Assets by contractual maturity						
Cash and balances at central banks	2	-	-	-	-	-
Loans to banks - amortised cost	67	33	-	-	-	-
Loans to customers - amortised cost	2,430	2,105	3,557	1,937	2,249	1,602
Amounts due from holding companies and fellow subsidiaries(1)	11,322	2,824	3,709	3,483	54	-
Total assets	13,821	4,962	7,266	5,420	2,303	1,602
Liabilities by contractual maturity						
Bank deposits	5	-	-	-	-	-
Customer deposits	26,102	426	4	-	-	-
Amounts due to holding companies and fellow subsidiaries(1)	1,898	706	1,345	1,766	359	5
Subordinated liabilities	-	-	-	-	315	-
Total liabilities	28,005	1,132	1,349	1,766	674	5
Maturity gap	(14,184)	3,830	5,917	3,654	1,629	1,597
Cumulative maturity gap	(14,184)	(10,354)	(4,437)	(783)	846	2,443
Guarantees and commitments - notional amounts						
Guarantees(2)	75	-	-	-	-	-
Commitments(3)	2,986	-	-	-	-	-
	3,061	-	-	-	-	-

Notes:

(1) £1.9 billion of short dated intercompany assets and liabilities, which meet the IAS 32 criteria, have been netted in 2019. The 2018 balances of £1.8 billion have been presented gross.

(2) The Bank is only called upon to satisfy a guarantee when the guaranteed party fails to meet its obligations. The Bank expects most guarantees it provides to expire unused.

(3) The Bank has given commitments to provide funds to clients under undrawn formal facilities, credit lines and other commitments to lend subject to certain conditions being met by the counterparty. The Bank does not expect all facilities to be drawn, and some may lapse before drawdown.

The tables above analyse the contractual cash flows receivable and payable up to a period of 20 years. 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 Bank. 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. Balances for derivatives are not included in the tables.

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 at 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.

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.

Credit risk

Definition (audited)
Credit risk is the risk that clients fail to meet their contractual obligation to settle outstanding amounts.

Sources of risk (audited)
The principal sources of credit risk are lending and related undrawn commitments. Derivatives and securities financing are also a source of credit risk, primarily related to Treasury activities for the Group. The Group is also exposed to settlement risk through foreign exchange and payments activities.

Risk governance (audited)
The Group's governance activities include:
- Defining credit risk appetite for the management of concentration risk and credit policy to establish the key causes of risk in the process of providing credit and the controls that must be in place to mitigate them.
- Approving and monitoring credit limits.
- Oversight of the first line of defence to ensure that credit risk remains within the appetite set by the Board and that controls are being operated adequately and efficiently.

Risk appetite
The Group's approach to Commercial credit is governed by a comprehensive credit risk appetite framework. The framework is monitored and actions are taken to adapt lending criteria as appropriate. Credit risk appetite aligns to the strategic risk appetite set by the Board of RBS Group (RBS Group Board). The framework has been designed to reflect factors that influence the ability to operate within risk appetite.

Tools such as stress testing and economic capital are used to measure credit risk volatility and develop links between the framework and risk appetite limits. The framework is supported by a suite of transaction acceptance standards that set out the risk parameters within which businesses should operate.

The Retail credit risk appetite framework sets limits that measure and control the quality of both existing and new business for each relevant business segment. The actual performance of each portfolio is tracked relative to these limits and management action is taken where necessary. The limits apply to a range of credit risk-related measures including expected loss at portfolio level and the loan-to-value (LTV) ratio of the Retail mortgage portfolios.

For the Commercial credit risk appetite framework, the four formal frameworks used – and their basis for classification – are detailed in the following table.

Framework	Basis for classification	
	Measure	Other
Single name concentration	Exposure	Risk - based on loss given default for a given probability of default (PD)
Sector	Exposure	Risk - based on economic capital and other qualitative factors
Country	Exposure	Risk - based on sovereign default risk, political stability and macro economic factors
Product and asset class	Exposure	Risk - based on heightened risk characteristics

Risk controls
Credit policy standards are in place for both the Commercial and Retail portfolios. They are expressed as a set of mandatory controls.

Risk identification and measurement

Credit stewardship (audited)
Risks are identified through relationship management and/or credit stewardship of portfolios or clients. Credit risk stewardship takes place throughout the client relationship, beginning with the initial approval. It includes the application of credit assessment standards, credit risk mitigation and collateral, ensuring that credit documentation is complete and appropriate, carrying out regular portfolio or client reviews and problem debt identification and management.

A key aspect of credit risk stewardship is ensuring that, when signs of client stress are identified, appropriate debt management actions are applied.

Risk models
Credit risk models is the collective term used to describe all models, frameworks and methodologies used to calculate PD, exposure at default (EAD), loss given default (LGD), maturity and the production of credit grades.

Credit risk models are designed to provide:
- An assessment of customer and transaction characteristics.
- A meaningful differentiation of credit risk.
- Accurate internal default, loss and exposure at default estimates that are used in the capital calculation or wider risk management purposes.

Credit risk continued

Asset quality
All credit grades map to an asset quality scale, used for financial reporting. For Commercial clients, a master grading scale is used for internal management reporting across portfolios. Measures of risk exposure may be aggregated and reported at differing levels of detail depending on stakeholder or business requirements. Performing loans are defined as AQ1-AQ9 (where the PD is less than 100%) and non-performing loans as AQ10 or Stage 3 under IFRS 9 (where the PD is 100%).

Counterparty credit risk
The Bank mitigates counterparty credit risk through collateralisation and netting agreements, which allow amounts owed by the Bank to a counterparty to be netted against amounts the counterparty owes to the Bank.

Risk mitigation
Risk mitigation techniques, as set out in the appropriate credit policies, are used in the management of credit portfolios across the Group. These techniques mitigate credit concentrations in relation to an individual client, a borrower group or a collection of related borrowers. Where possible, client credit balances are netted against obligations. Mitigation tools can include structuring a security interest in a physical or financial asset, the use of credit derivatives including credit default swaps, credit-linked debt instruments and securitisation structures, and the use of guarantees and similar instruments (for example, credit insurance) from related and third parties. Property is used to mitigate credit risk across a number of portfolios, in particular residential mortgage lending and commercial real estate (CRE).

Residential mortgages
The Group takes collateral in the form of residential property to mitigate the credit risk arising from mortgages. The Group values residential property during the loan underwriting process by appraising properties individually.

The current indexed value of the property is a component of the ECL provisioning calculation.

CRE valuations
The Group has a panel of chartered surveying firms that cover the spectrum of geography and property sectors in which the Group takes collateral. Suitable valuers for particular assets are contracted through a single service agreement to ensure consistency of quality and advice. Valuations are commissioned when an asset is taken as security; a material increase in a facility is requested; or a default event is anticipated or has occurred. In the UK, an independent third-party market indexation is applied to update external valuations once they are more than a year old and every three years a formal independent valuation is commissioned. The current indexed value of the property is a component of the ECL provisioning calculation.

Risk assessment and monitoring
Practices for credit stewardship – including credit assessment, approval and monitoring as well as the identification and management of problem debts – differ between the Retail and Commercial portfolios.

Commercial portfolios are applied to non-personal trading entities, and Personal portfolios are applied to all personal individuals, as well as some non-personal vehicles which have been set up specifically to house a private client's wealth.

For Commercial the output of credit risk models is used in the credit approval process – as well as for ongoing assessment, monitoring and reporting – to inform risk appetite decisions.

Where the calculation method is on an individual counterparty or account level the models used will be PD, loss given default (LGD), or exposure at default (EAD). The economic capital model is used for credit appetite setting.

Retail
Retail clients are managed through the Group's Retail Credit Policy Framework.

To ensure that these lending decisions are made consistently, the Bank analyses internal credit information as well as external data from credit reference agencies (including historical debt servicing behaviour of clients with respect to both the Group and other lenders). The Bank then sets its lending rules, accordingly, developing different rules for different products.

Underwriting standards and portfolio performance are monitored on an ongoing basis to ensure they remain adequate in the current market environment and are not weakened materially to sustain growth.

Commercial
Commercial clients are managed through the Group's Commercial Credit Policy Framework.

Commercial clients are grouped by industry sectors and geography as well as by product/asset class and are managed on an individual basis. Consideration is given to identifying groups of individual clients with sufficient inter-connectedness to merit assessment as a single risk.

A credit assessment is carried out before credit facilities are made available to clients. The assessment process is dependent on the complexity of the transaction. Credit approvals are subject to environmental, social and ethical risk policies which restrict exposure to certain highly carbon intensive industries as well as those with potentially heightened reputational impacts.

Transaction Acceptance Standards provide detailed transactional lending and risk acceptance metrics and structuring guidance. As such these standards provide a mechanism to manage risk appetite at the client/transaction level and are supplementary to the established credit risk appetite.

Credit grades (PD and LGD) are reviewed and, if appropriate, re-approved annually. The review process assesses borrower performance, including reconfirmation or adjustment of risk parameter estimates; the adequacy of security; compliance with terms and conditions; and refinancing risk.

Problem Debt Management

Retail
Early problem identification
Pre-emptive triggers are in place to help identify clients that may be at risk of being in financial difficulty. Pro-active contact is then made with the client to establish if they require help with managing their finances.

Retail clients experiencing financial difficulty are managed by the Risk Management team. If the Risk Management team is unable to provide appropriate support after discussing suitable options with the client, management of that client moves to the Recoveries team.

Policies are in place to ensure any client identified as being potentially vulnerable, at any point in the problem management process, receives appropriate support for their circumstances.

Credit risk continued

Collections
When a client exceeds an agreed limit or misses a regular monthly payment the client is contacted by the Bank and requested to remedy the position. If the situation is not regularised then, where the client review indicates that it is appropriate, the Collections team will become more fully involved and the client will be supported by skilled debt management staff who endeavour to provide clients with bespoke solutions. Solutions include short-term account restructuring, refinance loans, management of expired facilities in line with published policy to release secured assets and forbearance which can include interest suspension and 'breathing space'. In the event that an affordable/sustainable agreement with a client cannot be reached, the debt will transition to the Recoveries team. For provisioning purposes, under IFRS 9, exposure to clients managed by the Recoveries team is categorised as Stage 2 and subject to a lifetime loss assessment, unless it is 90 days past due, in which case it is categorised as Stage 3.

Recoveries
The Recoveries team will issue a notice of intention to default to the client and, if appropriate, a formal demand, while also registering the account with credit reference agencies where appropriate. Following this, the client's debt may then be placed with a third-party debt collection agency, or alternatively a solicitor, in order to agree an affordable repayment plan with the client. An option that may also be considered, is the sale of unsecured debt. Exposures subject to formal debt recovery are defaulted and categorised as Stage 3 impaired.

Commercial
Early problem identification
Each segment and sector have defined early warning indicators to identify clients experiencing financial difficulty, and to increase monitoring if needed. Early warning indicators may be internal, such as a client's bank account activity, or external, such as a publicly-listed client's share price. If early warning indicators show a client is experiencing potential or actual difficulty, or if relationship managers or credit officers identify other signs of financial difficulty, they may decide to classify the client within the Risk of Credit Loss framework.

Risk of Credit Loss framework
The Risk of Credit loss framework is used where the credit profile of a Commercial client has deteriorated. Experienced credit risk officers apply expert judgement to classify cases into categories that reflect progressively deteriorating credit risk. There are two classifications in the framework that apply to non-defaulted clients – Heightened Monitoring and Risk of Credit Loss. For the purposes of provisioning, all exposures subject to the framework are categorised as Stage 2 and subject to a lifetime loss assessment. The framework also applies to those clients that have met the Bank's default criteria (AQ10 exposures). Defaulted exposures are categorised as Stage 3 impaired for provisioning purposes.

Clients classified in the Heightened Monitoring category are those who are still performing but have certain characteristics – such as trading issues, covenant breaches, material PD downgrades and past due facilities – that may affect the ability to meet repayment obligations. Heightened Monitoring clients require pre-emptive actions to return or maintain their facilities within risk appetite prior to maturity.

Risk of Credit Loss clients are performing clients that have met the criteria for Heightened Monitoring and also pose a risk of credit loss to the Bank in the next 12 months should mitigating action not be taken or not be successful.

Once classified as either Heightened Monitoring or Risk of Credit Loss, a number of mandatory actions are taken – including a review of the client's credit grade, facility and security documentation and the valuation of security. Depending on the severity of the financial difficulty and the size of the exposure, the client relationship strategy is reassessed by credit officers, by specialist credit risk or relationship management units in the relevant business, or by Restructuring.

Forbearance (audited)
Forbearance takes place when a concession is made on the contractual terms of a loan/debt in response to a client's financial difficulties.

The aim of forbearance is to support and restore the client to financial health while minimising risk. To ensure that forbearance is appropriate for the needs of the client, minimum standards are applied when assessing, recording, monitoring and reporting forbearance.

A loan/debt may be forborne more than once, generally where a temporary concession has been granted and circumstances warrant another temporary or permanent revision of the loan's terms.

In the Retail portfolio, loans are considered forborne until they meet the exit criteria set out by the European Banking Authority. These include being classified as performing for two years since the last forbearance event, making regular repayments and the loan/debt being less than 30 days past due. Exit criteria are not currently applied for Commercial portfolios.

Types of forbearance
Retail
In the Retail portfolio, forbearance may involve payment concessions and loan rescheduling (including extensions in contractual maturity), capitalisation of arrears and, in the Republic of Ireland only, temporary interest-only conversions. Forbearance is granted principally to clients with mortgages and less frequently to clients with unsecured loans. This includes instances where forbearance may be provided to clients with highly flexible mortgages.

Commercial
In the Commercial portfolio, forbearance may involve covenant waivers, amendments to margins, payment concessions and loan rescheduling (including extensions in contractual maturity), capitalisation of arrears, and debt forgiveness or debt-for-equity swaps.

Monitoring of forbearance
Retail
For Retail portfolios, forborne loans are separated and regularly monitored and reported while the forbearance strategy is implemented until they exit forbearance.

Commercial
In the Commercial portfolio, client PDs and facility LGDs are re-assessed prior to finalising any forbearance arrangement. The ultimate outcome of a forbearance strategy is highly dependent on the cooperation of the borrower and a viable business or repayment outcome. Where forbearance is no longer appropriate, the Bank will consider other options such as the enforcement of security, insolvency proceedings or both, although these are options of last resort.

Provisioning for forbearance
Retail
The methodology used for provisioning in respect of Retail forborne loans will differ depending on whether the loans are performing or non-performing and which business is managing them due to local market conditions.

Credit risk continued

The loan would remain in forbearance for the defined probation period and be subject to performance criteria. These include making regular repayments and being less than 30 days past due.

Additionally, for some forbearance types a loan may be transferred to the performing book if a client makes payments that reduce loan arrears below 90 days.

For ECL provisioning, all forborne but performing exposures are categorised as Stage 2 and are subject to a lifetime loss provisioning assessment.

For non-performing forborne loans, the Stage 3 loss assessment process is the same as for non-forborne loans.

Commercial
Provisions for forborne loans are assessed in accordance with normal provisioning policies. The client's financial position and prospects – as well as the likely effect of the forbearance, including any concessions granted, and revised PD or LGD gradings – are considered in order to establish whether an impairment provision is required.

Commercial loans granted forbearance are individually assessed in most cases. Performing loans subject to forbearance treatment are categorised as Stage 2 and subject to a lifetime loss assessment. Forbearance may result in the value of the outstanding debt exceeding the present value of the estimated future cash flows. This difference will lead to a client being classified as non-performing.

In the case of non-performing forborne loans, an individual loan impairment provision assessment generally takes place prior to forbearance being granted. The amount of the loan impairment provision may change once the terms of the forbearance are known, resulting in an additional provision charge or a release of the provision in the period the forbearance is granted.

The transfer of Commercial loans from impaired to performing status follows assessment by relationship managers and credit. When no further losses are anticipated and the client is expected to meet the loan's revised terms, any provision is written-off or released and the balance of the loan returned to performing status. This is not dependent on a specified time period and follows the credit risk manager's assessment.

Impairment, provisioning and write-offs (audited)
In the overall assessment of credit risk, impairment, provisioning and write-offs are used as key indicators of credit quality.

The RBS Group's IFRS 9 provisioning models, which used existing Basel models as a starting point, incorporate term extension and forward-looking information.

Five key areas may materially influence the measurement of credit impairment under IFRS 9. Two of these relate to model build and three relate to their application:

Model build:
- The determination of economic indicators that have most influence on credit loss for each portfolio and the severity of impact (this leverages existing stress testing mechanisms).
- The build of term structures to extend the determination of the risk of loss beyond 12 months that will influence the impact of lifetime loss for assets in Stage 2.

Model application:
- The assessment of the significant increase in credit risk and the formation of a framework capable of consistent application.
- The determination of asset lifetimes that reflect behavioural characteristics while also representing management actions and processes (using historical data and experience).
- The determination of a base case (or central) economic scenario which has the most material impact (of all forward-looking scenarios) on the measurement of loss (the Group uses consensus forecasts to remove management bias).

Credit risk modelling (audited)
IFRS 9 ECLs are calculated using a combination of PD, LGD and EAD. In addition, lifetime PDs (as at reporting date and at date of initial recognition) are used in the assessment of the significant increase in credit risk criteria.

IFRS 9 ECL model design principles
To meet IFRS 9 requirements, PD, LGD and EAD used in ECL calculations must be:
- Unbiased – material regulatory conservatism has been removed to produce unbiased model estimates.
- Point -in-time – recognise current economic conditions.
- Forward-looking- incorporated into PD estimates and, where appropriate, EAD and LGD estimates.
- For the life of the loan – all PD, LGD and EAD models produce term structures to allow a lifetime calculation for assets in Stage 2 and Stage 3.

IFRS 9 requires that at each reporting date, an entity shall assess whether the credit risk on an account has increased significantly since initial recognition. Part of this assessment requires a comparison to be made between the current lifetime PD (i.e. the probability of default over the remaining lifetime at the reporting date) with the equivalent lifetime PD as determined at the date of initial recognition.

For assets originated before IFRS 9 was introduced, comparable lifetime origination PDs did not exist. These have been retrospectively created using the relevant model inputs applicable at initial recognition.

The Bank bases its calculations on the most appropriate NWB risk models; in particular NWB Premier for Retail and NWB Wholesale for Commercial.

The output of credit risk models is used in the credit approval process – as well as for ongoing assessment, monitoring and reporting – to inform risk appetite decisions. These models are divided into different categories. Where the calculation method is on an individual counterparty or account level, the models used will be;
- PD, based on the prevailing economic conditions,
- LGD, current assessment of the amount that will be recovered in the event of a default, taking into account future conditions, and
- EAD, expected balance sheet exposure at default including the effects of amortisation, exposure is capped at the contractual limit.

Lifetime PDs are used in the assessment of a significant increase in credit risk, which also considers quantitative and qualitative measures aligned to the RBS Group's current risk management framework.

PD estimates (audited)
Retail models
NWB PD models use the Exogenous, Maturity and Vintage (EMV) approach to model default rates. The EMV approach separates portfolio default risk trends into client and vintage effects (quality of new business over time).

Credit risk continued

PD estimates (audited)

Retail models (continued)

The EMV methodology has been widely adopted across the industry because it enables forward-looking economic information to be incorporated into PD estimates.

Commercial models

Commercial PD models use the existing Credit Cycles Indices (CCI) based point-in-time/through-the-cycle framework to convert one-year regulatory PDs into point-in-time estimates that reflect economic conditions observed at the reporting date across a comprehensive set of region/industry segments.

One year point-in-time PDs are subsequently extended to life-time PDs using a conditional transition matrix approach. The conditional transition matrix approach allows for the incorporation of forward-looking economic information into the life-time PDs.

LGD estimates (audited)

The general approach for the IFRS 9 LGD models is to leverage the corresponding Basel LGD models with bespoke adjustments to ensure estimates are unbiased and where relevant forward-looking.

Retail

Forward-looking information has only been incorporated for the secured portfolios, where changes in property prices can be readily accommodated. Analysis has shown minimal impact of economic conditions on LGDs for the other Retail portfolios.

Commercial

Forward-looking economic information is incorporated into LGD estimates using the existing CCI framework. For low default portfolios, including sovereigns and banks, loss data is too scarce to substantiate estimates that vary with economic conditions. Consequently, for these portfolios, LGD estimates are assumed to be constant throughout the projection horizon.

EAD estimates (audited)

Retail

The IFRS 9 Retail modelling approach for EAD is dependent on product type.

Amortising products use an amortising schedule, where a formula is used to calculate the expected balance based on remaining terms and interest rates.

There is no EAD model for Retail loans. Instead, debt flow (i.e. combined PD x EAD) is directly modelled.

Analysis has indicated that there is minimal impact on EAD arising from changes in the economy for all Retail portfolios except mortgages. Therefore, forward-looking information is only incorporated in the mortgage EAD model (through forecast changes in interest rates).

Commercial

For Commercial, EAD values are projected using product specific credit conversion factors (CCF), closely following the product segmentation and approach of the respective Basel model. However, the CCFs are estimated over multi-year time horizons to produce unbiased model estimates.

No explicit forward-looking information is incorporated, on the

basis that analysis has shown that temporal variations in CCFs are largely attributable to changes in exposure management practices rather than economic conditions.

Significant increase in credit risk (SICR) (audited)

RBS Group has adopted a framework to identify deterioration based primarily on movements in PD supported by additional backstops. The principles applied are consistent across the RBS Group and align to credit risk management practices. Exposures within commercial that are considered significantly credit deteriorated since initial recognition are classified in Stage 2 and assessed for lifetime ECL measurement (exposures not considered deteriorated carry a 12 month ECL).

The framework comprises:

Commercial:

- IFRS 9 lifetime PD assessment (the primary driver) – on modelled portfolios the assessment is based on the relative deterioration in forward-looking lifetime PD and is assessed monthly. To assess whether credit deterioration has occurred, the residual lifetime PD at balance sheet date (which PD is established at date of initial recognition (DOIR)) is compared to the current PD. If the current lifetime PD exceeds the residual origination PD by more than a threshold amount deterioration is assumed to have occurred and the exposure transferred to Stage 2 for a lifetime loss assessment. For Commercial, a doubling of PD would indicate a significant increase in credit risk subject to a minimum PD uplift of 0.1%.

For retail, SICR criteria is described on pages 19 & 20.

Asset lifetimes (audited)

The choice of initial recognition and asset duration is another critical judgement in determining the quantum of lifetime losses that apply.

- The date of initial recognition reflects the date that a transaction (or account) was first recognised on the balance sheet; the PD recorded at that time provides the baseline used for subsequent determination of significant increase in credit risk.
- For asset duration, the approach applied (in line with IFRS 9 requirements) is:
  - Term lending – the contractual maturity date, reduced for behavioural trends where appropriate (such as, expected prepayment and amortisation).
  - Revolving facilities – for Retail portfolios (except credit cards), asset duration is based on behavioural life and this is normally greater than contractual life (which would typically be overnight).
  - For Commercial portfolios, asset duration is based on annual counterparty review schedules and will be set to the next review date.

Multiple economic scenarios (MES) (audited)

The MES approach involves the selection of the central (or base) scenario that is most critical to the ECL calculation, independent of the method used to generate a range of alternative outcomes and their probabilities. Different approaches to model MES around the central scenario have all been found of low significance for the overall ECL impact.

The base scenario plays a greater part in the calculation of ECL than the approach to MES.

The response of portfolio loss rates to changes in economic conditions is typically non-linear and asymmetric. Therefore, in order to appropriately take account of the uncertainty in economic forecasts a range of economic scenarios are considered when calculating ECL.

Credit risk continued

Retail – the approach to MES is based on using a set of discrete scenarios. In addition to the central base case a further four bespoke scenarios are taken into account – a base case upside and downside – and an additional upside and downside. The overall MES ECL is calculated as a probability weighted average across all five scenarios.

Commercial – the approach to MES is a Monte Carlo method that involves simulating a large number of alternative scenarios around the central scenario (adjusted for mean reversion) and averaging the losses and PD values for each individual scenario into unbiased expectations of losses and PD.

The simulation of alternative scenarios does not occur on the level of the individual economic loss drivers but operates on the aggregate CCI that underpin the Commercial credit models.

The Monte Carlo MES approach increases Commercial ECL for Stage 1 and Stage 2 by approximately 7% above the single, central scenario outcomes. No additional MES overlay was applied for Commercial.

For both Retail and Commercial, the impact from MES is factored into account level PDs through scalars. These MES-adjusted PDs are used to assess whether a significant increase in credit risk has occurred.

As shown in the table below larger commercial clients are assigned credit grades, based on various credit grading models that reflect the key drivers of default for the client type. All credit grades map to both RBS level asset quality scale used for external financial reporting by the Group, and a master grading scale for commercial exposures used for internal management reporting across portfolios.

Asset Quality Grade	Probability of default range
AQ1	0% - 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%
AQ10	100%

Credit risk continued

Portfolio summary - sector analysis (audited)

The table below summarises financial assets gross of ECL, related ECL provisions, impairment and past due by sector and asset quality.

	Group			Bank		
2019	Retail £m	Commercial £m	Total £m	Retail £m	Commercial £m	Total £m
Loans and commitments by asset quality						
- AQ 1 - 4	6,406	960	7,366	6,025	941	6,966
- AQ 5 - 8	4,805	2,608	7,413	4,601	2,607	7,208
- AQ 9	63	2	65	58	2	60
- AQ 10	165	15	180	129	15	144
Loans by stage						
- Stage 1	11,007	3,285	14,292	10,429	3,265	13,694
- Stage 2	267	285	552	255	285	540
- Stage 3	165	15	180	129	15	144
Loans - past due analysis						
Total	11,439	3,585	15,024	10,813	3,565	14,378
- Not past due	11,182	3,566	14,748	10,600	3,546	14,146
- Past due 1-29 days	55	2	57	51	2	53
- Past due 30-89 days	66	5	71	59	5	64
- Past due 90-180 days	61	-	61	50	-	50
- Past due > 180 days	75	12	87	53	12	65
Stage 2						
- Not past due	175	278	453	171	278	449
- Past due 1-29 days	52	2	54	48	2	50
- Past due 30-89 days	40	5	45	36	5	41
- ECL measurement (years)	2	5	-	2	5	4
Weighted average 12 month PDs (unaudited)						
IFRS 9 (%)	0.6	0.7	0.7	0.6	0.7	0.7
Basel (%)	1.0	1.2	1.1	1.0	1.2	1.1
ECL provision by stage						
- Stage 1	3	4	7	3	4	7
- Stage 2	2	4	6	2	4	6
- Stage 3	20	6	26	15	6	21
ECL provisions coverage (%)						
- Stage 1 (%)	0.0	0.1	0.0	0.0	0.1	0.1
- Stage 2 (%)	0.8	1.4	1.1	0.8	1.4	1.1
- Stage 3 (%)	12.1	40.0	14.4	11.6	40.0	14.6
ECL loss rate (basis point)[1]	NA	NA	NA	NA	NA	NA
Amounts written off	-	1	1	-	1	1

Note:
(1) No ECL loss for the current or prior year, hence ECL loss rate is not applicable.

Amounts due from holding companies and fellow subsidiaries (Inter-Group) are all considered as Stage 1.

	Group					
		Stage 2				
2019	Total credit exposure £m	Past Due 1-30 Days £m	Past Due > 30 Days £m	Total £m	Stage 3 £m	ECL provisions £m
Retail	11,439	52	40	92	165	25
Commercial	3,442	2	5	7	15	14
of which Property	1,973	-	-	-	10	5
Total financial assets excluding balances at central banks	14,881	54	45	99	180	39
Balances at and due from banks	143	-	-	-	-	-
Total financial assets	15,024	54	45	99	180	39
Total contingent liabilities and commitments	2,916	-	-	-	-	-
Total exposure	17,940	54	45	99	180	39

Credit risk continued

	Bank					
		Stage 2				
	Total credit exposure	Past Due 1-30 Days	Past Due > 30 Days	Total	Stage 3	ECL provisions
2019	£m	£m	£m	£m	£m	£m
Retail	10,813	48	36	84	129	20
Commercial	3,441	2	5	7	15	14
of which Property	1,973	-	-	-	10	5
Total financial assets excluding balances at central banks	14,254	50	41	91	144	34
Balances at and due from banks	124	-	-	-	-	-
Total financial assets	14,378	50	41	91	144	34
Total contingent liabilities and commitments	2,916	-	-	-	-	-
Total exposure	17,294	50	41	91	144	34

	Group			Bank		
	Retail	Commercial	Total	Retail	Commercial	Total
2018*	£m	£m	£m	£m	£m	£m
Loans and commitments by asset quality						
- AQ 1 - 4	4,201	710	4,911	3,658	705	4,363
- AQ 5 - 8	6,167	2,516	8,683	5,778	2,495	8,273
- AQ 9	-	-	-	-	-	-
- AQ 10	176	18	194	123	18	141
Loans by stage						
- Stage 1	10,180	2,909	13,089	9,284	2,883	12,167
- Stage 2	189	317	506	152	317	469
- Stage 3	175	18	193	123	18	141
Loans - past due analysis						
Total	10,544	3,244	13,788	9,559	3,218	12,777
- Not past due	10,293	3,088	13,381	9,381	3,062	12,443
- Past due 1-29 days	64	14	78	54	14	68
- Past due 30-89 days	29	125	154	17	125	142
- Past due 90-180 days	54	5	59	45	5	50
- Past due > 180 days	104	12	116	62	12	74
Stage 2						
- Not past due	115	177	292	98	177	275
- Past due 1-29 days	51	15	66	40	15	55
- Past due 30-89 days	23	125	148	14	125	139
IFRS 9 (%)	0.7	0.5	0.5	0.7	0.5	0.5
Basel (%)	1.4	1.7	1.5	1.4	1.7	1.5
ECL provision by stage (total)						
- Stage 1	5	8	13	5	8	13
- Stage 2	2	8	10	2	8	10
- Stage 3	23	2	25	17	2	19
ECL provision coverage (%)						
- Stage 1 (%)	0.1	0.3	0.1	0.1	0.3	0.1
- Stage 2 (%)	1.1	2.5	2.0	1.3	2.5	2.1
- Stage 3 (%)	13.1	11.1	13.0	13.8	11.1	13.5
ECL loss rate (basis point)(1)	NA	NA	NA	NA	NA	NA
Amounts written off (total)	5	2	7	5	2	7

Note:
(1) No ECL loss for the current or prior year, hence ECL loss rate is not applicable.

*2018 data has been restated for a change to presentation of unrecognised interest. Refer to accounting policy 1, Other amendments to IFRS, for further details.

Credit risk continued

	Group					
		Stage 2				
2018*	Total credit exposure £m	Past Due 1-30 Days £m	Past Due > 30 Days £m	Total £m	Stage 3 £m	ECL provisions £m
Retail	10,544	51	23	74	175	30
Commercial	3,121	15	125	140	18	18
of which Property	2,144	9	119	128	6	10
Total financial assets excluding balances at central banks	13,665	66	148	214	193	48
Balances at and due from banks	123	-	-	-	-	-
Total financial assets	13,788	66	148	214	193	48
Total contingent liabilities and commitments	3,061	-	-	-	-	-
Total exposure	16,849	66	148	214	193	48

*2018 data has been restated for a change to presentation of unrecognised interest. Refer to accounting policy 1, Other amendments to IFRS, for further details.

	Bank					
		Stage 2				
2018*	Total credit exposure £m	Past Due 1-30 Days £m	Past Due > 30 Days £m	Total £m	Stage 3 £m	ECL provisions £m
Retail	9,559	40	14	54	123	24
Commercial	3,116	15	125	140	18	18
of which Property	2,102	9	119	128	6	10
Total financial assets excluding balances at central banks	12,675	55	139	194	141	42
Balances at and due from banks	102	-	-	-	-	-
Total financial assets	12,777	55	139	194	141	42
Total contingent liabilities and commitments	3,061	-	-	-	-	-
Total exposure	15,838	55	139	194	141	42

*2018 data has been restated for a change to presentation of unrecognised interest. Refer to accounting policy 1, Other amendments to IFRS, for further details.

Credit risk continued

Retail portfolio (audited)

Mortgages represent the largest product in the loan book. The table below further details the spread and risk of these exposures.

At 31 December 2019 LTV ratios are split by stage under IFRS 9.

	Group		Bank	
	2019	2018*	2019	2018*
	£m	£m	£m	£m
Gross new mortgage lending	2,027	1,742	2,027	1,739
Owner occupied exposure	1,810	1,591	1,810	1,588
Weighted average LTV	65%	62%	65%	62%
Buy-to-let	217	151	217	151
Weighted average LTV	59%	55%	59%	55%
Interest only - variable	665	656	665	653
Interest only - fixed	951	733	951	733
Mixed	-	-	-	-
Retail lending				
Mortgages	9,377	8,512	8,754	7,535
Owner occupied	8,196	7,444	7,637	6,566
Buy-to-let	1,181	1,068	1,117	969
Interest only - variable	3,464	3,649	3,212	3,238
Interest only - fixed	4,356	3,437	4,157	3,116
Mixed	-	-	-	-
ECL provisions	13	11	11	9
Other lending	2,062	2,032	2,059	2,024
ECL provisions	12	19	9	17
Total Retail lending	11,439	10,544	10,813	9,559
Mortgage LTV ratios				
- Total portfolio	57%	56%	57%	56%
- Stage 1/performing	57%	55%	57%	56%
- Stage 2/performing	61%	58%	61%	63%
- Stage 3/non-performing	70%	58%	61%	56%
- Buy-to-let	54%	53%	55%	54%
- Stage 1	54%	53%	55%	53%
- Stage 2	57%	53%	60%	55%
- Stage 3	57%	67%	57%	69%

*2018 data has been restated for a change to presentation of unrecognised interest. Refer to accounting policy 1, Other amendments to IFRS, for further details.

The Bank holds collateral in respect of net exposures. For individual loans and advances to banks and customers, the collateral includes mortgages over property and charges over business assets.

Non-traded market risk

Definition (audited)
Non-traded market risk is the risk to the value of assets or liabilities outside the trading book, or the risk to income, that arises from changes in market prices such as interest rates, foreign exchange rates and equity prices, or from changes in managed rates.

Sources of risk (audited)
The Bank's non-traded market risk largely comprises interest rate risk and foreign exchange risk.

Interest rate risk
Non-traded interest rate risk (NTIRR) arises from the provision to clients of a range of banking products with differing interest rate characteristics. When aggregated, these products form portfolios of assets and liabilities with varying degrees of sensitivity to changes in market interest rates. Mismatches can give rise to volatility in net interest income as interest rates vary.

Foreign exchange risk
Non-traded foreign exchange risk arises from client transactions and profits and losses that are in a currency other than the functional currency of the transacting operation.

Risk governance
Responsibility for identifying, measuring, monitoring and controlling market risk arising from non-trading activities lies with the relevant business. Market risk policy statements set out the governance and risk management framework.

Risk appetite
The Bank's qualitative appetite is set out in the non-traded market risk appetite statement. Its quantitative appetite is expressed in terms of exposure limits. These limits are approved and monitored by the Asset and Liability Committee.

Risk controls
For information on risk controls, refer to page 10.

Risk monitoring and mitigation

Interest rate risk
NTIRR factors are grouped into the following categories:
- Gap risk – arises from the timing of rate changes in non-trading book instruments. The extent of gap risk depends on whether changes to the term structure of interest rates occur consistently across the yield curve (parallel risk) or differentially by period (non-parallel risk).
- Basis risk – captures the impact of relative changes in interest rates for financial instruments that have similar tenors but are priced using different interest rate indices, or on the same interest rate indices but with different tenors.
- Option risk – arises from option derivative positions or from optional elements embedded in assets, liabilities and/or off-balance sheet items, where the Bank or its client can alter the level and timing of their cash flows.

Due to the long-term nature of many Retail and Commercial portfolios, and their varied interest rate repricing characteristics and maturities, net interest income is likely to vary from period to period, even if interest rates remain the same. New business originated in any period will alter the Bank's interest rate sensitivity if the resulting portfolio differs from portfolios originated in prior periods, depending on the extent to which exposure has been hedged. To manage exposures within appetite, the Bank aggregates its interest rate positions and hedges these.

The market risk exposures arising as a result of the Bank's retail and commercial banking activities are measured using a combination of value-based metrics (VaR and sensitivities) and earnings-based metrics.

VaR is a statistical estimate of the potential change in the market portfolio (and, thus the impact on the income statement) over a specified time horizon at a given level of confidence.

Foreign exchange risk
The Bank has no foreign subsidiaries and manages its exposures to overseas suppliers within specified limits.

Risk identification and measurement

Sensitivity of net interest earnings
Earnings sensitivity to rate movements is derived from a central forecast over a 12 month period. A simplified scenario is shown below based on the period end balances assuming that non interest rate variables remain constant. Market implied forward rates are used to generate a base case income forecast which is then subjected to interest rate shock. The variance between the central forecast and the shock gives an indication of underlying sensitivity to interest rate movements.

The sensitivity of net interest earnings table shows the expected impact, over 12 months, to an immediate upward or downward change of 25 and 100 basis points to all interest rates. Yield curves are expected to move in parallel though interest rates are assumed to floor at zero per cent or, for euro rates, at the current negative rate.

The main driver of earnings sensitivity relates to interest rate pass-through assumptions on client products. The scenario also captures the impact of the reinvestment of maturing structural hedges at higher or lower rates than the base-case earnings sensitivity and mismatches in the repricing dates of loans and deposits.

However, reported sensitivities should not be considered a guide to future performance. They do not capture potential management action in response to sudden changes in the interest rate environment. Actions that could reduce NII sensitivity and mitigate adverse impacts are changes in pricing strategies on client loans and deposits as well as hedging. Management action may also be targeted at stabilising total income taking into account non-interest income in addition to NII.

Non-traded market risk continued

The table below sets out the expected impact on net interest earnings of a movement in yield curves:

			Group		
	Euro	Sterling	US Dollar	Other	Total
2019	£m	£m	£m	£m	£m
+25bps shift in yield curves	1	11	1	-	13
-25bps shift in yield curves	-	(5)	(2)	-	(7)
+100bps shift in yield curves	5	46	5	1	57
-100bps shift in yield curves	-	(55)	(8)	(1)	(64)
2018					
+25bps shift in yield curves	-	11	-	-	11
-25bps shift in yield curves	-	(7)	-	-	(7)
+100bps shift in yield curves	1	44	3	1	49
-100bps shift in yield curves	-	(76)	(6)	(1)	(83)

Compliance & Conduct risk

Definition and sources of risk
Compliance risk is the risk that the behaviour of the Bank towards clients fails to comply with laws, regulations, rules, standards and codes of conduct. Such a failure may lead to breaches of regulatory requirements, organisational standards, product suitability or client expectations and could result in legal or regulatory sanctions, material financial loss or reputational damage.

Conduct risk is the risk that the conduct of the Bank and its subsidiaries and its colleagues towards clients – or in the markets in which it operates – leads to unfair or inappropriate client outcomes and results in reputational damage, financial loss or both.

Sources of risk
Compliance and conduct risks exist across all stages of the Bank's relationships with its clients and arise from a variety of activities including product design, marketing and sales, complaint handling and colleague training.

Key developments in 2019
- Policies were simplified and enhanced to reflect regulatory changes and technical training delivered across the lines of defence.
- Ongoing investment in regulatory technology.
- Planning for LIBOR transition continued including an extended SONIA pilot and further industry engagement.
- Preparations continued for a number of Brexit outcomes.
- Enhanced operational capabilities to cope with unprecedented volumes of PPI mis-selling claims.

Risk governance
The Bank defines appropriate standards of compliance and conduct and ensures adherence to those standards through its risk management framework.

Risk appetite
Risk appetite statements articulate the levels of risk that the Bank works within when pursuing its strategic objectives and business plans.

Risk controls
The Bank operates a range of controls to ensure its business is conducted in accordance with legal and regulatory requirements, as well as delivering good client outcomes. A suite of policies addressing compliance and conduct risks set appropriate standards across the Bank. Examples of these include the Complaints Management Policy, Client Assets & Money Policy, and Product Lifecycle Policy as well as policies relating to clients in vulnerable situations, cross-border activities and market abuse. Continuous monitoring and targeted assurance is undertaken, as appropriate.

Risk monitoring and measurement
Compliance and conduct risks are measured and managed through continuous assessment and reporting to the Bank's senior risk committees and at Board level.

The compliance and conduct risk framework facilitate the consistent monitoring and measurement of compliance with laws and regulations and the delivery of consistently good client outcomes.

The first line of defence is responsible for effective risk identification, reporting and monitoring, with oversight, challenge and review by the second line. Compliance and conduct risk management is also integrated into the Bank's planning cycle.

Risk mitigation
Activity to mitigate the most material compliance and conduct risks is carried out across the Bank with specific focus on client-facing activities. Examples of mitigation include consideration of client needs in business and product planning, targeted training, complaints management, as well as independent assurance activity. Internal policies help support a strong client focus across the Bank.

Financial crime

Definition
Financial crime risk is the risk presented by criminal activity in the form of money laundering, terrorist financing, bribery and corruption, sanctions and tax evasion. It does not include fraud risk management.

Sources of risk
Financial crime risk may occur if the Bank's colleagues, clients or third parties undertake or facilitate financial crime, or if the Bank's products or services are used to facilitate such crime. Financial crime risk is an inherent risk across all of the Bank's lines of business.

Financial crime continued

Key developments in 2019

- Enhanced financial crime risk assessment processes were implemented to enable improved identification and mitigation of financial crime risks.
- Improvements were made to transaction monitoring alert processes, including the use of risk-based artificial intelligence to facilitate focus on activity of higher concern.
- Financial crime policies were refreshed and updated to reflect changes to the regulatory environment and industry best practice.

Risk governance

The Financial Crime Risk Executive Committee, which is chaired by the RBS Group Chief Financial Crime Risk Officer, is the principal financial crime risk management forum. The committee reviews and, where appropriate, escalates material financial crime risks and issues across RBS Group to the Executive Risk Committee and the Board Risk Committee.

Risk appetite

The Bank has no appetite to operate in an environment where systems and controls do not enable the Bank to identify, assess, monitor, manage and mitigate financial crime risk. The Bank systems and controls must be comprehensive and proportionate to the nature, scale and complexity of its businesses. The Bank has no tolerance to systematically or repeatedly breach relevant financial crime regulations and laws.

Risk controls

The Bank operates a framework of preventative and detective controls designed to ensure the Bank mitigates the risk that it could facilitate financial crime. These controls are supported by a suite of policies, procedures and detailed instructions to ensure they operate effectively.

Risk monitoring and measurement

Financial crime risks are identified and reported through continuous risk management and regular monthly reporting to the Bank's senior risk committees and the Board. Quantitative and qualitative data is reviewed and assessed to measure whether financial crime risk is within the Bank's risk appetite.

Risk mitigation

Through the financial crime framework, the Bank employs relevant policies, systems, processes and controls to mitigate financial crime risk. This would include the use of dedicated screening and monitoring controls to identify people, organisations, transactions and behaviours which might require further investigation or other actions. The Bank ensures that centralised expertise is available to detect and disrupt threats to the Bank and its clients. Intelligence is shared with law enforcement, regulators and government bodies to strengthen national and international defences against those who would misuse the financial system for criminal motives.

Climate risk

Definition

Climate risk is the risk arising from the effects of, and exposure to, climate change. It includes those risks likely to affect clients as well as the Bank's ability to achieve its strategic ambitions together with the impact of the global transition to a low-carbon economy.

Sources of risk

Physical risk describes the more immediate and tangible effects of global warming, including rising sea levels and the increased occurrence of extreme weather events such as extended droughts, flooding, fire and storms. These can result in changes to business models, the impairment of asset values or adversely affect the creditworthiness of clients. Large scale extreme weather events have the potential to affect operational, credit, market and sovereign risk.

Transition risk explores the longer-term impact of the move to a low carbon economy, which may affect the Bank, its clients and the wider market.

Key developments in 2019

- Climate risk was reclassified as a Top Risk and is now reported quarterly to the Board Risk Committee.
- Geographic information system and flood risk data has been applied at property level across RBS Group's retail mortgage portfolio in Great Britain. Projected flood risk to 2040 has been calculated at postcode level.
- Where data is available, an Energy Performance Certificate (EPC) rating has been applied to retail mortgage property in England and Wales.
- RBS Group submitted a detailed plan to the Prudential Regulation Authority detailing how it intends to address expectations on how the financial risks from climate change will be governed, managed, assessed and reported.
- A transitional Executive Steering Group was created to support the delivery of RBS Group's climate change response plan.
- A climate risk governance map was created. Responsibility for identifying and managing financial risks from climate change was allocated to the RBS Group Chief Risk Officer under the Senior Managers Regime.
- RBS Group is one of five UK banks represented on the Climate Financial Risk Forum, established by the PRA and FCA to shape the financial service industry's response to the challenges posed by climate risk.

Risk governance

The RBS Group's Board is responsible for addressing and overseeing the financial risks from climate change within the RBS Group's overall business strategy and risk appetite and ensuring adequate resources, skills and expertise are devoted.

The climate change response plan represents an iterative approach to building climate risk into existing corporate strategy, risk management, governance, disclosures and capital planning cycles from 2020 onwards. In support, an Executive Steering Group is responsible for overseeing delivery of the climate change response plan against regulatory expectations. Its remit is to provide executive-level support, advice and resource direction on climate change strategy, including risk management and climate-related business opportunities.

RBS CRO and the chair of RBS Group Board Risk Committee receive monthly updates on RBS Group's response to climate risk through internal Top & Emerging Risk reporting.

The RBS Climate Change Working Group, established in 2018, meets on a quarterly basis. Reporting to the RBS CRO, its remit is to coordinate RBS Group activity in response to climate-related regulation, helping to address risks through robust metrics and analysis as well as identify the potential opportunities climate change may bring.

The Bank reviews Climate risk regularly and considers the impact it might have on its portfolio.

Climate risk continued

Risk appetite
As climate risk policies and processes evolve in response to a maturing regulatory framework, RBS Group has continued to explore how climate change can be embedded into existing risk frameworks. To date, this work has focused largely on credit, market and operational risk frameworks.

Risk controls
For information on risk controls, refer to page 10.

Risk monitoring and measurement
RBS Group's response to climate-related risk has been developed around four central themes: governance, scenario analysis and stress testing, risk frameworks and disclosure.

RBS Group is a member of the United Nations Environment Programme – Finance Initiative, which aims to promote sustainable finance around the globe. As part of this, RBS Group is participating in three climate thematic modules exploring how climate change will affect real estate, as well as agriculture and land use.

Within the Bank, a programme of work is underway to define robust metrics for the measurement of climate-related risk, both physical and transitional, with the aim of supporting future Bank of England mandated stress testing requirements in 2021.

Risk mitigation
RBS Group treats the mitigation of climate change and the effective management of climate risk as strategic priorities.

RBS Group is increasingly embedding climate risk, both physical and transitional, into how it manages risk daily. In addition to integrating climate risk in its business as usual operating model, RBS Group continues to expand its capabilities in response to future climate risk stress testing requirements. The Bank of England has confirmed that the 2021 Biennial Exploratory Scenario will stress test the UK financial system's resilience to the physical and transitional risks of climate change.

Operational risk

Definition
Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or external events. It arises from day-to-day operations and is relevant to every aspect of the business.

Sources of risk
Operational risk may arise from a failure to manage operations, systems, transactions and assets appropriately. This can take the form of human error, an inability to deliver change adequately or on time, the non-availability of technology services, or the loss of client data. Fraud and theft – as well as the increasing threat of cyber attacks – are sources of operational risk, as is the impact of natural and man-made disasters. Operational risk can also arise from a failure to account for changes in law or regulations or to take appropriate measures to protect assets.

As cyber attacks evolve and become more sophisticated, the Bank will be required to invest additional resources to upgrade the security of its systems. The Bank has information security controls in place, which are subject to review on a continuing basis, but there can be no assurance that such measures will prevent all cyber attacks in the future.

Key developments in 2019
- There was an improvement in the operational risk profile, indicated by an improved control environment, with residual elements under close management.
- A focus remained on maintaining operational resilience and ensuring preparedness for external threats and challenges such as cyber attacks and Brexit.
- The threat landscape continued to evolve during 2019 and NWB Group invested in control enhancements to keep pace. This included new anti-malware controls and improved security testing to quickly detect and remediate vulnerabilities.
- During 2019, progress was made in embedding an innovation framework to help deliver innovative solutions to customers safely and at pace.
- Following the introduction of ring-fencing and Operational Continuity in Resolution requirements, NWB Group introduced a consistent approach to identify and capture the risk associated with service provision of service between its legal entities.
- There was an increased focus on ensuring the security and business strategies were aligned. Security is considered at the outset of new business projects to ensure they are delivered in a safe and secure manner. The number of critical customer-impacting incidents that NWB Group experiences continued to reduce year-on-year.
- Internal training programmes ensure all employees are aware of the threats facing NWB Group and remain vigilant to unauthorised attempts to access systems and data.

Risk appetite
Operational risk appetite supports effective management of material operational risks. It expresses the level and types of operational risk the Bank is willing to accept to achieve its strategic objectives and business plans.

The bank-wide operational risk appetite statement encompasses the full range of operational risks faced by the Bank. Should any risk appetite limit be breached, this would impact on our ability to achieve business plans and threaten stakeholder confidence.

Risk monitoring and measurement
Risk and control assessments are used across all business areas and support functions to identify and assess material operational and conduct risks and key controls. All risks and controls are mapped to the Bank Risk Directory. Risk assessments are refreshed at least annually to ensure they remain relevant and capture any emerging risks, with associated trigger processes to ensure risks are reassessed at key periods of change.

Scenario analysis is used to assess how extreme but plausible operational risks will affect the Bank. It provides a forward-looking basis for evaluating and managing operational risk exposures.

Operational resilience
The Bank manages and monitors operational resilience through its risk and control assessments methodology. As challenges to operational resilience become more demanding, given a hostile cyber environment and a greater focus on serving clients through digital platforms, the Bank is working with supervisory authorities in the UK to ensure the provision of its products and services can be maintained regardless of the cause of disruption.

Operational risk continued

This is underpinned by setting, monitoring and testing tolerances for key business services, which define the amount of disruption that could be tolerated.

Risk mitigation

Risks are mitigated by applying key preventative and detective controls, an integral step in the risk assessment methodology which determines residual risk exposure. Control owners are accountable for the design, execution, performance and maintenance of key controls. Key controls are regularly assessed for adequacy and tested for effectiveness. The results are monitored and, where a material change in performance is identified, the associated risk is re-evaluated.

Reputational risk

A reputational risk policy is in place to support the management of issues that could pose a threat to the Bank's public image. A number of measures including some also used in the management of operational, conduct and financial risks are used to assess risk levels against risk appetite. Where a material reputational risk is presented, this is escalated to the RBS Group Reputational Risk Committee. For further information on reputational risk, refer to page 189 of the RBS Group Annual Report & Accounts.

Model risk

A variety of models are used as part of risk management processes and activities. To mitigate the risk that models are specified, implemented or used incorrectly, independent validation and regular reviews are carried out. Oversight is provided by an RBS Group model risk governance committee in accordance with relevant policies and procedures. For further information on model risk, refer to page 189 of the RBS Group Annual Report & Accounts.

REPORT OF THE DIRECTORS

The directors present their report together with the audited accounts for the year ended 31 December 2019. It should be read in conjunction with the Strategic report.

Directors and secretary

The names of the current members of the Board of Directors are shown on page 6.

From 1 January 2019 to date, changes that have taken place are shown under 'Appointments and Resignations' on page 6.

Share capital

Analysis of share capital and paid-in equity can be found in notes 17 and 18 respectively to the financial statements.

In the previous year, the Group raised an additional Tier 1 equity note of £35 million, and a Tier 2 loan of £45 million from NWB; further details of which are provided in notes 16 and 18. These changes were made to optimise the capital structure at that time. Further issuances will occur from time to time to improve capital efficiency.

Dividends

An interim dividend of £140 million was approved on 6 June 2019 and a further interim dividend of £75 million was approved on 4 December 2019 (2018 - £90 million). These were paid in the year.

The Bank also declared coupon payments of £13 million during the year (2018 - £10 million) on Additional Tier 1 notes.

The Bank received a dividend of £35 million from Coutts Finance Co in 2019 (2018 - £46 million) and £24 million from AMH (2018 - £29 million).

The directors do not recommend the payment of a final dividend (2018 - nil).

Going concern

The Group business activities and financial position, together with the factors likely to affect its future development, performance and position are set out in the Strategic report on pages 2 to 31.

Having reviewed the content of these and the Bank forecasts, projections and other relevant evidence, the directors have a reasonable expectation that the Bank will continue in operational existence for the foreseeable future. Accordingly, the financial statements of the Bank have been prepared on a going concern basis.

Governance

Our Board

The Board has seven directors comprising the Independent Non-Executive Chair, two Executive Directors, one Non-Independent Non-Executive Director and three Independent Non-Executive Directors. Director biographies can be found at www.coutts.com.

The Board is collectively responsible for the long-term success of the Bank, and delivery of sustainable value to its shareholders. It monitors and maintains the consistency of the Bank's activities within the strategic direction of RBS Group. It reviews and approves risk appetite for strategic and material risks in accordance with RBS Group Risk Appetite Framework and it monitors performance against risk appetite for the Bank. It approves the Bank's key financial objectives and keeps the capital and liquidity positions of the Bank under review. The Board is also responsible for culture, which underpins all the Bank's activities and its long-term sustainability.

In order to extend its effective oversight and leadership, the Board has an Audit Committee, Risk Committee, Nominations Committee and Performance and Remuneration Committee.

There is regular reporting to the Board on risk culture which allows the Board to have appropriate oversight of risk culture matters that are relevant.

Audit Committee

The Committee is responsible for discharging the Board's responsibilities for monitoring the quality of the financial statements. It reviews the accounting policies, financial reporting and relevant compliance practices of the Bank. It also reviews the Bank's systems and standards of internal controls, and monitors the Bank's processes for internal audit and external audit.

Risk Committee

The Committee provides oversight and advice to the Board on current and potential risk exposures, and on future risk strategy. It reviews compliance with approved risk appetite and oversees the operation within the Bank of RBS Group's Risk Policy Framework.

Performance and Remuneration Committee

The Committee is responsible for overseeing the implementation within the Bank of RBS Group's remuneration policy, and of performance and remuneration arrangements.

Nominations Committee

The Committee is responsible for assisting the Board in the formal selection and appointment of directors. It reviews the structure, size and composition of the Board, and the membership and chairmanship of Board committees.

Executive Committee

The Board is supported by the Executive Committee comprising the executive directors and other senior executives. It supports the Chief Executive Officer (CEO) in managing the Bank's businesses and reviewing relevant items before consideration by the Board. It is responsible for developing and delivering the Bank's strategy and culture and it monitors and manages financial performance, capital allocation, risk strategy and policy, risk management, operational issues and client issues for the Bank.

Directors' indemnities

In terms of Section 236 of the Companies Act 2006, all directors listed on page 6 have been granted Qualifying Third Party Indemnity Provisions by RBS Group.

The Wates Corporate Governance Principles

The Companies (Miscellaneous Reporting) Regulations 2018 introduced new statutory reporting requirements for financial years beginning on or after 1 January 2019. As a result of these new requirements, the directors of the Bank are required to provide a statement in the Report of the directors stating which corporate governance code the Bank followed during the year, how it applied the code and any part of the code it did not follow.

For the financial year ended 31 December 2019 the Bank has chosen to report against the Wates Corporate Governance Principles for Large Private Companies, published by the Financial Reporting Council (FRC) in December 2018 and available on the FRC website (the 'Wates Principles'). The disclosures below explain how the Bank has applied the Wates Principles in the context of its corporate governance arrangements.

REPORT OF THE DIRECTORS

1. Purpose and Leadership

The Bank's purpose of being an indispensable partner to its clients sits within the purpose of RBS Group. RBS Group's purpose is established by the RBS Group Board and cascaded to subsidiaries. Further information on RBS Group's purpose can be found in the 2019 Annual Report and Accounts of RBS Group plc.

Strategy for the RBS Group is likewise approved by the RBS Group Board and cascaded to subsidiaries. The Board of the Bank approves and monitors the strategic direction of the Bank within the parameters set by the RBS Group.

The Bank's strategy remains based on a clear vision: to be the Best Private Bank in the UK, measured through three lenses: client satisfaction, colleague engagement and financial returns. The Board oversees the execution of strategy and holds management to account for its delivery. This is done through a mix of reporting, Board and other meetings and an annual Board strategy day.

Building a healthy culture that embodies Our Values is also a core priority for RBS Group. Our Values, which guide the way RBS Group identifies the right people to serve customers well, and how to manage, engage and reward colleagues, are at the heart of Our Code (the RBS Group-wide Code of Conduct).

There is regular reporting to the Board on culture which allows the Board to have appropriate oversight of culture matters. This includes 6-monthly reviews of 'Our View' colleague survey and culture measurement reports, as well as of the Bank's risk culture. In 2019, the Bank made further progress in these areas, with colleague survey results placing it ahead of the Global Financial Services Norm (GFS) in 12 out of 14 categories. The Board also considers the overall alignment of purpose and strategy with culture and values.

2. Board Composition

Details on the Board and its Committees are presented in the section on Governance above (see page 32).

The Board's Nominations Committee regularly reviews the structure, size and composition of the Board, and ensures there is an appropriate mix of skills, knowledge, experience and diversity, as well as independence. The Nominations Committee further supports the Board in succession planning. Board diversity is supported by a Boardroom Inclusion Policy, which includes gender and ethnicity diversity targets. The policy sets out the aspiration to meet the targets set by the Hampton-Alexander Report on "FTSE100 Women Leaders" (33% female balance) and the Parker Report "Beyond 1 by '21" (at least one director from an ethnic minority background to be included on the list of candidates by 2020/21). Whilst the Board meets the gender target, it remains focused on developing its diversity, particularly with respect to its ethnic diversity.

The size of the Board is considered appropriate, taking into account the size and scale of the Bank's business.
The independent non-executive directors combine broad business and commercial experience with independent and objective judgement and provide independent challenge to the executive directors and the leadership team. The balance between independent non-executive and executive directors enables the Board to provide clear and effective leadership across the Bank's business activities. The role of the Chair is to lead the Board and ensure its overall effectiveness, and is distinct and separate from that of the CEO, who manages the business day-to-day.

A review of the effectiveness of the Board is conducted at least annually. Non-executive directors participate in scheduled Board training sessions and other external sessions, as required. An active Board 'teach-in' training programme was run in 2019, with over a dozen sessions held. The topics covered include artificial intelligence and data, cyber risks and competition and company law responsibilities. Directors also request individual in-depth briefings from time to time on areas of particular interest, and undertake visits to regional offices. An induction programme is provided for all new directors, which is tailored to their specific experience and knowledge.

3. Director Responsibilities

All directors receive guidance on their statutory duties under the Companies Act 2006 and are supported in the discharge of their duties by the Company Secretary.

RBS Group has a Corporate Governance Framework, including a Corporate Governance Policy, which sets out the key aspects of the governance framework as they relate to its key subsidiaries. The Corporate Governance Policy provides high-level guidance to the Board on how the Bank should be managed in line with RBS Group policy and best practice.
The Board and its Committees have Terms of Reference which clearly map out their respective authority, responsibilities and accountabilities. Each director has a role profile which clearly articulates their responsibilities and accountabilities, and any additional regulatory responsibilities are set out in their Statement of Responsibilities, as provided for under the UK's Senior Managers Regime. The Board holds regular quarterly meetings, an annual strategy day, and other meetings as required.

Directors' conflicts of interest are managed in accordance with conflicts of interest guidance. The company maintains a register of directors' interests and appointments and this is presented at each quarterly Board meeting for review.

The Chair, CEO and Company Secretary are responsible for the quality and integrity of information provided to directors. The Board receives regular information on key aspects of the business, including monthly reports from the CEO, in addition to reporting provided to the quarterly Board meetings.

Extensive internal processes are in place to ensure that the quality and integrity of information provided to the Board is reliable and able to support effective decision making. This is supported by assurance undertaken by second and third lines of defence teams, who respectively provide quarterly Risk and Internal Audit opinions to the quarterly Board Risk and Audit Committees.

4. Opportunity and Risk

The role of the Board is to promote the long-term, sustainable success of the Bank, which already has a heritage of over 300 years. Opportunities are primarily identified through regular Board reviews of the different parts of the Bank's business and an annual Board strategy session, drawing on client and external market insights, and are framed within the overall strategy of the RBS Group.

The Board reviews and approves risk appetite for strategic and material risks in accordance with the RBS Group risk appetite framework; monitors performance against risk appetite for the Bank; and considers any material risks and approves, as appropriate, recommended actions escalated by the Bank's Board Risk Committee.

The Bank's risk strategy is informed and shaped by an understanding of the risk landscape including a range of significant risks and uncertainties in the external economic, political and regulatory environments.

The Bank complies with RBS Group's risk appetite framework, which is approved annually by the RBSG plc Board, in line with RBS Group's risk appetite statements, frameworks and policies. RBS Group risk appetite is set in line with overall strategy.

REPORT OF THE DIRECTORS

RBS Group operates an integrated risk management framework, which is centred around the embedding of a strong risk culture. The framework ensures the tools and capability are in place to facilitate sound risk management and decision-making across the organisation.

During 2019, a number of enhancements to the risk management framework were developed. The increasing significance of climate risk was considered as part of these developments and will be fully integrated as part of the implementation of the enhanced framework in 2020.

The Bank also complies with the RBS Group Policy Framework, the purpose of which is to ensure that RBS Group establishes and maintains RBS Group-wide policies that adequately address the material inherent risks it faces in its business activities.

Further information on the Bank's risk management framework including risk culture, risk governance, risk appetite, risk controls and limits, and risk identification and measurement can be found in the Capital and risk management section of this report (pages 7 to 31).

5. Remuneration

The RBS Group Remuneration Policy provides a consistent policy across all companies in RBS Group and ensures compliance with regulatory requirements. The remuneration policy is aligned with the business strategy, objectives, values and long-term interests of the Bank. The policy supports a culture where individuals are rewarded for delivering sustained performance in line with risk appetite and for demonstrating the right conduct and behaviours.

The Bank has a Performance & Remuneration Committee (RemCo) with non-executive directors as members. In addition to reviewing remuneration for executives of the Bank, the RemCo considers reports on the wider workforce including annual pay outcomes and diversity information. The RemCo helps to ensure that the remuneration policies, procedures and practices being applied are appropriate at the Bank level.

Executive remuneration structures incentivise individuals to deliver sustainable performance based on strategic objectives for the RBS Group and the Bank. Performance is assessed against a balanced scorecard of financial and non-financial measures and variable pay is subject to deferral as well as malus and clawback provisions to ensure rewards are justified in the long-term.

The RBS Group is committed to providing a fair wage for the role performed. The Bank is a fully accredited Living Wage Employer with rates of pay that continue to exceed the Living Wage Foundation Benchmarks.

6. Stakeholder Relationships and Engagement

The Bank is committed to engaging with its stakeholders and to bringing their voice into key decisions, as well as managing the wider social, environmental and economic impacts of its operations, as a cornerstone of building a sustainable business.

The Board recognises the importance of engaging with stakeholders and discussions at Board meetings are focused around the impact that the Bank's activities may have on key stakeholder groups. For further details on the Board's engagement with colleagues, customers, suppliers and others, and how these stakeholder interests have been taken into account, see pages 3 to 5 of the Strategic report, which includes a section 172(1) statement

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 to, or additional disclosure or amendment in the financial statements.

Political donations

During 2019, no political donations were made in the UK or EU, nor any political expenditure incurred in the UK or EU.

Directors' disclosure to auditor

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

- so far as the director is aware, there is no relevant audit information of which the Group and the Bank's auditor is unaware; and
- 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 Group and the Bank's auditor is 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.

Auditor

Ernst & Young LLP has expressed its willingness to continue in office as auditor.

A resolution to re-appoint Ernst & Young LLP as the Group's auditor will be proposed at the forthcoming Annual General Meeting.

By order of the Board:

The Rt Hon Lord Waldegrave of North Hill
Chair

Date: 12 March 2020

Coutts & Company is registered in England and Wales No. 00036695

STATEMENT OF DIRECTORS' RESPONSIBILITIES

This statement should be read in conjunction with the responsibilities of the auditor set out in their report on page 36.

The directors are responsible for the preparation of the Annual Report and Accounts. The directors are required by Article 4 of the IAS Regulation (European Commission Regulation No 1606/2002) to prepare Group accounts, and as permitted by the Companies Act 2006 have elected to prepare company accounts for each financial year in accordance with International Financial Reporting Standards as adopted by the European Union. They are responsible for preparing accounts that present fairly the financial position, financial performance and cash flows of the Group and the Bank. In preparing those accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts; and
- make an assessment of the Group and the Bank's ability to continue as a going concern.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and the Bank and to enable them to ensure that the Annual Report and Accounts complies with the Companies Act 2006. They are also responsible for safeguarding the assets of the Group and the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with International Financial Reporting Standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and the Bank; and
- the Strategic report (incorporating the Business review) and Report of the directors includes a fair review of the development and performance of the business and the position of the Group and the Bank.

By order of the Board:

The Rt Hon Lord Waldegrave of North Hill
Chair

Date: 12 March 2020

Board of Directors

Chair, Non-Executive Director
The Rt Hon Lord Waldegrave of North Hill

Executive Directors
Peter Gordon Flavel
Andrew Richard Kyle

Non-Executive Directors
Francesca Barnes
Mark Joseph Lund
Linda Hamilton Urquhart OBE
Matthew Edward James Waymark

INDEPENDENT AUDITOR'S REPORT TO THE MEMBER OF COUTTS & COMPANY

Opinion

We have audited the financial statements (see table below) of Coutts & Company (the 'Bank') and its subsidiaries (together, the 'Group') for the year ended 31 December 2019. 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 2019 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the Bank 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 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements of Coutts & Company which comprise:

Group	Bank
• Consolidated balance sheet as at 31 December 2019; • Consolidated statement of comprehensive income for the year then ended; • Consolidated statement of changes in equity for the year then ended; • Consolidated cash flow statement for the year then ended; • Related notes 1 to 25 to the financial statements; • Accounting Policies on pages 46 to 50 • Capital and risk management section identified as 'audited'	• Balance sheet as at 31 December 2019; • Statement of changes in equity for the year then ended; • Cash flow statement for the year then ended; • Related notes 1 to 25 to the financial statements; • Accounting Policies on pages 46 to 50; and • Capital and risk management section identified as 'audited'

The financial reporting framework that has been applied in their preparation is applicable law and IFRSs as adopted by the European Union and, as regards the Bank financial statements, as applied in accordance with the provisions of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report below. We are independent of the Group and Bank in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

In relation to the ISAs (UK) which require us to report to you, we have nothing to report in respect of the following matters:
- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Group's or the Bank's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

Overview of our audit approach

Key Audit Matters	• Provisions for conduct, litigation and regulatory matters. • Impairment of loans. • Legal entity recharges.
Audit scope	• We performed an audit of the complete financial information of the Group.
Materiality	• Overall Group materiality has been set at £24 million which represents 8% of profit before tax.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in our opinion thereon, and we do not provide a separate opinion on these matters.

Risk	Our response to the risk
Provisions for conduct, litigation and regulatory matters	
The continued litigious environment and the heightened regulatory scrutiny gives rise to a high level of judgement in determining appropriate provisions and disclosures. At the year-end, the Group has reported £50.0 million (2018: £46 million) of provisions for liabilities and charges for conduct and litigation claims as detailed in Note 15 of the financial statements on page 65. Management judgement is needed to determine whether an obligation exists and the extent to which a provision should be recorded at 31 December 2019 in accordance with the accounting criteria set under IAS 37. This is therefore subject to the risk of management override. The most significant areas of judgement, therefore, include the determination of the following: • It is probable that an economic outflow such as a payment will occur; • The amount of the payment (or other economic outflow) can be estimated reliably including the appropriateness of the assumptions and judgements to determine this amount, and • The disclosures are adequate and in accordance with accounting standards.	We tested the design and operating effectiveness of the Group's key controls over the identification, estimation, monitoring and disclosure of provisions considering the potential for management override of controls. We examined the relevant regulatory correspondence and the list of litigations and enquired of management to identify potentially material conduct or legal matters. We also reviewed any whistle blowing cases noted in the period. For cases where a provision was not recognised, we considered whether the outcome was probable and reliably estimable in accordance with the accounting criteria. For material provision raised, we understood, assessed and challenged the provisioning methodology. We tested the underlying data and assumptions used in the determination of the provision recorded including the associated legal costs, and assessed the estimated timing of any potential settlement. We also considered recent legal developments and concluded on the reasonableness of the assumptions used by management. We also developed our own reasonable alternative estimate using external publicly available information and compared this range to management's provision. We received confirmation from the Group's external counsel of the existence of the obligations. We tested the disclosure provided to determine whether it complied with accounting standards. Given the inherent estimation uncertainty and the judgmental nature of these provisions, we evaluated the appropriateness of the disclosure made in the financial statements.

Key observations communicated to the Audit Committee

We highlighted to the Audit Committee a judgemental difference in one of the provisions however this was not considered material. Overall, we are satisfied that provisions for conduct, litigation and regulatory matters are within a reasonable range and recognised in accordance with IFRS. We are satisfied that the overall disclosure is appropriate. We did not identify any material unrecorded provisions.

Relevant references in the Annual Report and Accounts

Accounting policies
Note 15 of the financial statements

Key observations communicated to the Audit Committee

Risk	Our response to the risk
Impairment of loans	
At 31 December 2019 the Group reported total gross loans of £15.02bn (2018: £13.79bn) and £39m (2018: £48million) of expected credit loss provisions. Key judgements and estimates in respect of the timing and measurement of expected credit losses (ECL) include: • Allocation of assets to stage 1, 2, or 3 using criteria in accordance with the accounting standard; • Accounting interpretations and modelling assumptions used to build and select the most appropriate models that calculate the ECL; • Completeness and accuracy of data used to calculate the ECL; • Inputs and assumptions used to estimate the impact of multiple economic scenarios; • Measurements of individually assessed provisions including the assessment of multiple scenarios; and • Accuracy and adequacy of the financial statement disclosures.	We tested the design and operating effectiveness of key controls across the processes relevant to the ECL. This included the allocation of assets into stages, model governance and selection, data accuracy and completeness, credit monitoring, multiple economic scenarios, individual provisions and production of journal entries and disclosures. We observed the key executive finance and risk committees where the inputs, assumptions, models and adjustments to the ECL were discussed and approved. We performed an overall assessment of the ECL provision levels by stage to determine if they were reasonable considering the Group's portfolio, risk profile, credit risk management practices and the macroeconomic environment. As part of the review of a sample of performing loans, we challenged the criteria used to allocate an asset to stage 1, 2 or 3 in accordance with IFRS 9. Separately, we tested management's staging criteria's of all assets in stage 1, 2 and 3 to verify that they were allocated to the appropriate stage. With the support of our internal modelling specialists, we tested the assumptions, inputs and formulas used in a sample of ECL models. This included assessing the appropriateness of model design and formulas used, considering alternative modelling techniques and recalculating the Probability of Default, Loss Given Default and Exposure at Default for a sample of models. We also assessed and challenged the appropriateness of the models selected by management and evaluated the justification for their use. To verify data quality, we tested the data used in the ECL calculation by reconciling to source systems. With the support of our internal economic specialists, we assessed the base case and alternative economic scenarios, including challenging probability weights and comparing to other scenarios from a variety of external sources, as well as EY internally developed forecasts. We assessed whether forecasted macroeconomic variables were appropriate, such as GDP, unemployment, interest rates and House Price Index. We recalculated a sample of individually assessed provisions. The sample was based on a number of factors that also included collateral held. We assessed the adequacy and appropriateness of disclosures for compliance with the accounting standards.

We are satisfied that credit impairment provisions were reasonable and in compliance with IFRS 9. We highlighted the following matters to the Audit Committee:

- In a few instances our testing on the staging criteria identified differences in respect of the Bank's staging allocation however none of these differences were considered material and we concluded that the overall stage allocation at 31 December 2019 were reasonable;
- Our testing of models, model assumptions and individually assessed impairments did not highlight material differences; and
- Considerable improvements were made to the control environment throughout the year, which previously identified control deficiencies remediated by year-end.

Relevant references in the Annual Report and Accounts

Credit risk section of the Capital and risk management section
Accounting policies
Note 8 on the financial statements

Risk	Our response to the risk
Legal entity recharges	
The majority of RBS group-wide costs are paid centrally by the ultimate holding company, and recharged to other RBS Group companies, including the Bank. RBS Group recharges currently constitute the majority of the Bank's total cost base. These costs are recharged in line with Inter-group Agreements ("IGA") and transfer pricing policy. Coutts & Co is heavily dependent on the accuracy of the RBS Group processes to appropriately present and disclose transactions with the rest of the RBS Group, including elimination of intercompany accounts, transfers of business and legal entity. Accounting and reporting risk arising includes: • recharged costs may not be calculated in accordance with the revised RBS Group IGA and transfer pricing methodology; • risk of errors in the computation of recharges; and • Reconciliation of recharges and intercompany transactions.	We tested the design and operating effectiveness of the Group's key controls, including the review of the service catalogue, the allocation metrics and net recharge balance by management as well as the application controls to calculate the allocation of costs and the mark-ups applied, over the completeness and accuracy of cost recharges. This included understanding RBS Group's recharging processes and controls, including how management ensures the assessment is complete. The transfer pricing methodology was reviewed by our tax specialists. We reconciled amounts recharged to intercompany balances. We also tested a sample of cost recharged and agreed them to supporting documentation.

Key observations communicated to the Audit Committee

We are satisfied that the cost recharged in the year were reasonable. We highlighted to the Audit Committee control deficiencies identified within the RBS Group's recharging process and we performed additional testing in response to those deficiencies.

Relevant references in the Annual Report and Accounts

Accounting policies
Note 3 of the financial statements

An overview of the scope of our audit

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for the Group. This enables us to form an opinion on the financial statements. We take into account size, risk profile, the organisation of the Group and effectiveness of controls, including controls and changes in the business environment when assessing the level of work to be performed. All audit work performed for the purposes of the audit was undertaken by the Group audit team.

Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality

The magnitude of omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality to be £24 million (2018 materiality: £26 million), which is 8% of profit before tax of the Group. This measure is consistent with the basis from the prior year and is consistent with the wider industry and is the standard for regulated entities and we believe it reflects the most useful measure for users of the financial statements.

Performance materiality

The application of materiality at the individual account or balance level is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and corrected misstatements exceed materiality.

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality was 75% of our planning materiality, namely £18 million (2018: £19 million). We have set performance materiality at this percentage (which is at the highest end of the range of our audit methodology) based on various considerations including the past history of misstatements, our ability to assess the likelihood of misstatements, the effectiveness of the control environment and other factors affecting the entity and its financial reporting.

Reporting threshold

An amount below which identified misstatements are considered to be clearly trivial.

We agreed with the Audit Committee that we would report to them all corrected and uncorrected audit misstatements in excess of £1.2 million (2018: £1.3 million), which is set at 5% of planning materiality, as well as misstatements below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative and qualitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Other information

The other information comprises the information included in the Annual Report and Financial Statements, including the Strategic Report (set out on pages 1 to 5), Directors' report (set out on pages 32 to 34), and Board of Directors and Company Secretary (set out on page 6) other than the financial statements and our auditor's report thereon. The directors are responsible for the other information.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the Directors' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the Group and the Bank and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the directors' report.

We have nothing to report in respect of the following matters in relation to which 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 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.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement (set out on page 35), the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for the implementation of such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Group and Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or the Bank or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBER OF COUTTS & COMPANY

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

The objectives of our audit, in respect to fraud, are: to identify and assess the risks of material misstatement of the financial statements due to fraud; to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud, through designing and implementing appropriate responses; and to respond appropriately to fraud or suspected fraud identified during the audit. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management.

Our approach was as follows:

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Group and have a direct impact on the preparation of the financial statements. We determined that the most significant are:
    - The regulations, licence conditions and supervisory requirements of the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA)
    - Companies Act 2006
    - Financial Reporting Council (FRC) and the UK Corporate Governance Code
    - Tax Legislation (governed by HM Revenue and Customs)
- We understood how the Group is complying with those frameworks by reviewing of the Group's documented policies and procedures, holding discussions with the Audit Committee and Company Secretary, external counsel, amongst others. We inquired as to any known instances of non-compliance or suspected non-compliance with laws and regulations.
- We assessed the susceptibility of the Group's financial statements to material misstatement, including how fraud might occur by holding discussions with senior management, including the Chief Executive Officer, Financial Director, Chief Operating Officer, Head of Legal, Head of Lending and Capital Management, Head of Risk, Audit Committee Chair and non-executive directors.
- As part of our audit procedures, we were aware of the risk of fraud, especially in the areas of estimation and those we assessed as having the risk of management override.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved inquiring of key management, reviewing the key policies and reports on the aforementioned regulatory frameworks as well as reviewing the correspondence exchanged with the Regulators.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at https://www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Other matters we are required to address

- Following the recommendation of the RBS Group Audit Committee we were appointed by the Group at its annual general meeting on 4 May 2016 to audit the financial statements of the Group for the period ending 31 December 2016 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments is 4 years, covering periods from our appointment through 31 December 2019.
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Bank and we remain independent of the Group and the Bank in conducting the audit.
- The audit opinion is consistent with the additional report to the Audit Committee.

Use of our report

This report is made solely to the Group's member, 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 Group's member 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 Group and the Group's member as a body, for our audit work, for this report, or for the opinions we have formed.

Michael-John Albert (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London
Date: 13 March 2020

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2019

	Note	2019 £m	2018* £m
Interest receivable		607	544
Interest payable		(157)	(101)
Net interest income	1	450	443
Fees and commissions receivable		230	226
Fees and commissions payable		(14)	(18)
Other operating income		24	30
Non-interest income	2	240	238
Total income		690	681
Staff costs		(142)	(138)
Premises and equipment		(13)	(13)
Depreciation & amortisation		(12)	(10)
Other administrative expenses		(230)	(206)
Operating expenses	3	(397)	(367)
Profit before impairment releases		293	314
Impairment releases	8	7	7
Operating profit before tax		300	321
Tax charge	6	(80)	(86)
Profit and total comprehensive income for the year		220	235
Attributable to:			
Ordinary shareholders		220	235
		220	235

*Restated for IAS 12 ‘Income taxes’ refer to accounting policy 1 for further details.

The accompanying notes, on pages 51 to 72, and the accounting policies, on pages 46 to 50, form an integral part of these financial statements.

BALANCE SHEETS AS AT 31 DECEMBER 2019

		Group		Bank	
		2019	2018	2019	2018
	Note	£m	£m	£m	£m
Assets					
Cash and balances at central banks	7	3	2	3	2
Loans to banks - amortised cost	7	143	121	124	100
Loans to customers - amortised cost	7	14,792	13,566	14,172	12,587
Amount due from holding companies and fellow subsidiaries	7	18,690	20,238	19,249	21,124
Derivatives	7, 9	22	20	22	20
Investment in Group undertakings	7, 10	-	-	110	110
Property, plant and equipment	7, 11	294	246	294	246
Other assets	7, 13	93	87	76	70
Total assets		34,037	34,280	34,050	34,259
Liabilities					
Bank deposits	7	12	5	12	5
Customer deposits	7	26,390	26,527	26,390	26,527
Amount due to holding companies and fellow subsidiaries	7	5,463	5,944	5,463	5,944
Derivatives	7, 9	20	20	20	20
Other financial liabilities	7, 14	310	-	310	-
Other liabilities	7, 15	224	107	215	91
Subordinated liabilities	7, 16	265	315	265	315
Total liabilities		32,684	32,918	32,675	32,902
Owner's equity		1,353	1,362	1,375	1,357
Total equity		1,353	1,362	1,375	1,357
Total liabilities and equity		34,037	34,280	34,050	34,259

Owner's equity of the Bank as at 31 December 2019 includes the profit for the year then ended of £247 million (2018 - £271 million).

The accompanying notes, on pages 51 to 72, and the accounting policies, on pages 46 to 50, form an integral part of these financial statements.

The accounts were approved by the Board of Directors on 12 March 2020 and signed on its behalf by:

Andrew Richard Kyle
Executive Director

The Rt Hon Lord Waldegrave of North Hill
Chair

STATEMENTS OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2019

		Group		Bank	
		2019	2018*	2019	2018*
	Note	£m	£m	£m	£m
Called-up share capital at 1 January and 31 December	17	41	41	41	41
Paid-in equity at 1 January		200	165	200	165
Additional Tier 1 capital notes issued		-	35	-	35
At 31 December	18	200	200	200	200
Retained earnings at 1 January		782	667	734	585
Implementation of IFRS 16 on 1 January 2019	19	(1)	-	(1)	-
Implementation of IFRS 9 on 1 January 2018		-	(20)	-	(22)
Profit and total comprehensive income for the year		220	235	247	271
Paid-in equity coupon payments		(13)	(10)	(13)	(10)
Dividends paid		(215)	(90)	(215)	(90)
At 31 December		773	782	752	734
Capital contribution at 1 January		339	275	382	275
Addition during the year	17	-	64	-	107
At 31 December		339	339	382	382
Owner's equity at 31 December		1,353	1,362	1,375	1,357

*Restated for IAS 12 ‘Income taxes’ refer to accounting policy 1 for further details.

The accompanying notes, on pages 51 to 72, and the accounting policies, on pages 46 to 50, form an integral part of these financial statements.

CASH FLOW STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2019

		Group		Bank	
		2019	2018	2019	2018
	Note	£m	£m	£m	£m
Cash flows from operating activities					
Operating profit before tax		300	321	319	344
Adjustments for:					
Depreciation, amortisation and impairment		12	10	12	10
Impairment (release)/charge		(7)	(7)	(7)	(8)
Other non-cash items		8	(60)	11	1
Equity dividends received		-	-	(59)	(75)
Increase in loans to banks and customers		(1,248)	(1,011)	(1,609)	(1,530)
Decrease/ (increase) in amounts due from holding companies and fellow subsidiaries		40	(1,931)	376	(1,472)
Increase in derivative assets and liabilities		(2)	-	(2)	-
Decrease/ (increase) in other assets		1	17	(1)	28
(Decrease)/ increase in deposits by banks and customers		(130)	1,950	(130)	1,950
(Decrease)/ increase/ in amounts due to holding companies and fellow subsidiaries		(481)	804	(481)	804
(Decrease)/ increase/ in other liabilities		(9)	3	-	(9)
Changes in operating assets and liabilities		(1,829)	(168)	(1,847)	(229)
Income taxes paid		(6)	(80)	(1)	(68)
Net cash flows from operating activities[(1)]		(1,522)	16	(1,572)	(25)
Cash flows from investing activities					
Purchase of property, plant and equipment	11	(6)	(7)	(6)	(7)
Acquisition of cash and cash equivalents	10	-	68	-	-
Disposal of property, plant & equipment	11	1	2	1	2
Purchase of intangible assets	12	(12)	(13)	(12)	(13)
Equity dividends received		-	-	59	75
Net cash flows from investing activities		(17)	50	42	57
Cash flows from financing activities					
Additional Tier 1 capital notes issued		-	35	-	35
Issue of subordinated liabilities		-	95	-	95
Paid-in equity coupon payments		(13)	(10)	(13)	(10)
Issue of debt securities	14	260	-	260	-
Equity dividends paid		(215)	(90)	(215)	(90)
Net cash flows from financing activities		32	30	32	30
Effects of exchange rate changes on cash & cash equivalents		(82)	109	(82)	109
Net increase/ (decrease) in cash and cash equivalents		(1,589)	205	(1,580)	171
Cash and cash equivalents 1 January	22	10,821	10,616	10,783	10,612
Cash and cash equivalents 31 December		9,232	10,821	9,203	10,783

The accompanying notes, on pages 51 to 72, and the accounting policies, on pages 46 to 50, form an integral part of these financial statements..

Note:

(1) Includes interest received for Group of £603 million (2018 - £532 million) and interest paid of £159 million (2018 - £94 million), and for Bank interest received of £593 million (2018 - £503 million) and interest paid of £159 million (2018 - £94 million).

ACCOUNTING POLICIES

1. Presentation of accounts

The accounts, set out on pages 42 to 72, including these accounting policies on pages 46 to 50 and the audited sections of the Capital and risk management on pages 7 to 31, are prepared on a going concern basis (see the Report of the directors, page 32) and in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IASB), and interpretations as issued by the IFRS Interpretations Committee of the IASB and adopted by the European Union (EU) (together IFRS). The significant accounting policies and relevant judgements are set out below.

The Bank, a private unlimited company, is incorporated in the UK and registered in England and Wales. The Group and Bank accounts are presented in accordance with the Companies Act 2006.

The functional currency of the accounts is pounds sterling.

With the exception of investment property and certain financial instruments as described in accounting policies 9, 13, 15 and 16, the accounts are prepared on an historical cost basis.

Adoption of new and revised standards

Refer to accounting policy 10 and note 19 for details of the adoption of IFRS 16.

Other amendments to IFRS

IAS 12 'Income taxes' was revised with effect from 1 January 2019. The income statement now includes any tax relief on the servicing cost of instruments classified as equity. Relief of £3 million was recognised in the statement of changes in equity for the year ended 31 December 2018; this and prior years have been restated.

IAS 19 'Employee Benefits' was amended by the IASB in February 2018 to clarify the need to update assumptions whenever there is a plan amendment, curtailment or settlement. This amendment has not affected the accounts.

Presentation of interest in suspense recoveries: In March 2019 the IFRS Interpretations Committee (IFRIC) issued an agenda decision on the presentation of unrecognised interest when a credit-impaired financial asset (commonly referred to as a 'Stage 3' financial asset) is subsequently paid in full or is no longer credit-impaired. This concluded that the difference arising from the additional interest recovered must be recognised as a reversal of impairment rather than within interest revenue. This affects both recognition and the reversal of the expected credit loss (ECL) allowance.

RBS Group changed its accounting policy in line with the IFRIC decision. Hence, the gross carrying amount of the financial assets within the scope of the provisions of the decision, as well as the associated ECL allowance on the balance sheet, have been adjusted by £6 million and the comparative period restated by £6 million with no effect on equity. The coverage ratio for the current and comparative periods have been adjusted and restated accordingly.

In addition, until 1 January 2019, interest in suspense recoveries were presented as a component of interest receivable within Net interest income. From 1 January 2019 interest in suspense recoveries are presented within Impairment losses and amounted to £1 million for the year ended 31 December 2019. Comparatives have not been restated on the grounds of materiality.

2. Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and entities that are controlled by the Group (its subsidiaries). Control is assessed by reference to our ability to enforce our will on the other entity, typically through voting rights.

On acquisition of a subsidiary from outside of RBS Group, its identifiable assets, liabilities and contingent liabilities are included in the consolidated accounts at their fair value. A subsidiary is included in the consolidated financial statements from the date it is controlled by the Group until the date the Group ceases to control it through a sale or a significant change in circumstances.

On the acquisition of a business from an RBS Group company, the assets, liabilities and IFRS reserves are recognised at their inherited values taken from the consolidated accounts of RBS Group and include the accounting history since initial recognition. The acquirer recognises in the capital contribution reserve any difference between the consideration and the net items recognised at inherited values.

All intergroup balances, transactions, income and expenses are eliminated on consolidation. The consolidated accounts are prepared under uniform accounting policies.

3. Income recognition

Interest income or expense, on financial instruments that are measured at amortised cost, is determined using the effective interest rate method. Negative effective interest accruing to financial assets is presented in interest payable.

Net interest income in the income statement only relates to financial instruments measured at amortised cost. Other interest relating to financial instruments measured at fair value is recognised as part of movement in fair value.

Commitment and utilisation fees are determined as a percentage of the outstanding facility. The fees are deferred and included in the effective interest rate on the advance.

Fees in respect of services are recognised on the satisfaction of the performance obligation. 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.

4. Colleague benefits

Short-term colleague benefits, such as salaries, paid absences, and other benefits are accounted for on an accruals basis over the period in which the colleagues provide the related services. Colleagues may receive variable compensation satisfied by cash, by debt instruments issued by RBS Group or RBS Group shares.

Variable compensation that is settled in cash or debt instruments is charged to statement of comprehensive income over the period from the start of the year to which the variable compensation relates to the expected settlement date taking account of forfeiture and claw back criteria.

NWB provides post-retirement benefits in the form of pensions and healthcare plans to eligible colleagues on behalf of the Group.

There is no contractual agreement or policy on the way that the cost of NWB defined benefit pension schemes and healthcare plans are allocated to the Group. It therefore accounts for the charges it incurs as payments to a defined contribution scheme.

Contributions to defined contribution pension schemes are recognised in profit or loss when payable.

5. Intangible assets and goodwill
Intangible assets acquired by the Group, excluding goodwill, are stated at cost less accumulated amortisation and impairment losses. Amortisation is charged to statement of comprehensive income over the assets' estimated economic lives.

Computer software	3 to 12 years
Other acquired intangibles	5 to 10 years

Intangible assets include goodwill arising on the acquisition of subsidiaries. Goodwill on the acquisition of a subsidiary from a third party is the excess of the fair value of the consideration transferred, the fair value of any existing interest in the subsidiary and the amount of any non-controlling interest measured either at fair value or at its share of the subsidiary's net assets over the net fair value of the subsidiary's identifiable assets, liabilities and contingent liabilities.

Where a subsidiary acquires a business from an RBS Group company, goodwill is acquired at the value inherited from RBS Group's accounts.

Direct costs relating to the development of internal-use computer software are capitalised once technical feasibility and economic viability have been established. These costs include payroll, the costs of materials and services, and directly attributable overheads.

Capitalisation of costs ceases when the software is capable of operating as intended. During and after development, accumulated costs are reviewed for impairment against the benefits that the software is expected to generate.

Costs incurred prior to the establishment of technical feasibility and economic viability are expensed as incurred as are all training costs and general overheads.

The costs of licences to use computer software that are expected to generate economic benefits beyond one year are also capitalised.

6. Property, plant and equipment
Items of property, plant and equipment (except investment property) are stated at cost less accumulated depreciation and impairment losses. Where an item of property, plant and equipment comprises major components having different useful lives, these 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. Freehold land is not depreciated.

The estimated useful lives of the Group's property, plant and equipment are:

Freehold buildings	50 years
Long leasehold property (leases with more than 50 years to run)	50 years
Short leaseholds	unexpired period of lease
Property adaptation costs	10 to 15 years
Computer equipment	up to 5 years
Other equipment	4 to 15 years
Right of use	unexpired period of lease

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

7. Impairment of intangible assets and property, plant and equipment
At each reporting date, the Group assesses whether there is any indication that its intangible assets, right of use assets or property, plant and equipment are impaired. If any such indication exists, the Group estimates the recoverable amount of the asset and the impairment loss. Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired.

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.

A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

For the purposes of impairment testing, goodwill acquired in a business combination is allocated to each of the Group's cash-generating units or groups of cash-generating units expected to benefit from the combination.

The recoverable amount of an asset or cash-generating unit 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 taken into account in estimating future cash flows.

An impairment loss is recognised if the recoverable amount of an intangible or tangible asset is less than its carrying value. The carrying value of the asset is reduced by the amount of the loss and a charge recognised in the profit or loss.

A reversal of an impairment loss on an intangible assets (excluding goodwill) or property, plant and equipment can be recognised as it arises provided the increased carrying value is not greater than it would have been had no impairment loss been recognised. Impairment losses on goodwill are not reversed.

8. Investment properties
Investment property comprises leasehold properties that are held to earn rentals or for capital appreciation or both. Investment property is not depreciated but is stated at fair value. Fair value is based on the current prices for similar properties in the same location and condition. Further details are included in note 11.

Any gain or loss arising from a change in fair value is recognised in statement of comprehensive income. Rental income from investment property is recognised on a straight-line basis over the term of the lease in other operating income. 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 Group and the Bank. Transactions in foreign currencies are recorded in the functional currency at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the relevant functional currency at the foreign exchange rates ruling at the balance sheet date. Foreign exchange differences arising on the settlement of foreign currency transactions and from the translation of monetary assets and liabilities are reported in income from trading activities.

Non-monetary items denominated in foreign currencies are translated into the relevant functional currency at the foreign exchange rates ruling at the dates the values are determined. Translation differences arising on non-monetary items are recognised in profit or loss.

10. Leases
The Group has adopted IFRS 16 'Leases' with effect from 1 January 2019, replacing IAS 17 'Leases'. The Group has applied IFRS 16 on a modified retrospective basis without restating prior years. The effect is set out in note 19. Comparatives are still based on IAS17 and related accounting policy can be found in Annual Report and Accounts 2018.

As lessor
Rental income from operating leases is recognised in other operating income on a straight-line basis over the lease term unless another systematic basis better represents the time pattern of the asset's use. Operating lease assets are included within Property, plant and equipment and depreciated over their useful lives (see accounting policy 6). Operating lease rentals receivable, for the investment property, are included in other operating income.

As lessee
On entering a new lease contract, the Group recognises a right of use asset and a lease liability to pay future rentals. The liability is measured at the present value of future lease payments discounted at the applicable incremental borrowing rate. The right of use asset is depreciated over the shorter of the term of the lease and the useful economic life, subject to review for impairment.

Short term and low value leased assets are expensed on a systematic basis.

11. Provisions
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.

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. Tax
Income tax expense or income, comprising current tax and deferred tax, is recorded in the consolidated statement of comprehensive income 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 profit or loss, other comprehensive income or 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 their recovery is probable. Deferred tax is not recognised on temporary differences that arise from initial recognition of an asset or a liability in a transaction (other than a business combination) that at the time of the transaction affects neither accounting nor taxable profit or loss.

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.

Deferred tax assets and liabilities are offset where the Group has a legally enforceable right to offset and where they relate to income taxes levied by the same taxation authority either on an individual Group company or on Group companies in the same tax group that intend, in future periods, to settle current tax liabilities and assets on a net basis or on a gross basis simultaneously.

Accounting for taxes is judgmental and carries a degree of uncertainty because tax law is subject to interpretation, which might be questioned by the relevant tax authority. The Group recognises the most likely current and deferred tax liability or asset, assessed for uncertainty using consistent judgments and estimates. Current and deferred tax assets are only recognised where their recovery is deemed probable, current and deferred tax liabilities are recognised at the amount that represents the best estimate of the probable outcome having regard to their acceptance by the tax authorities.

13. Financial instruments
Financial instruments are classified either by product, by business model or by reference to the IFRS default classification.

Classification by product relies on specific designation criteria which are applicable to certain classes of financial assets or circumstances where accounting mismatches would otherwise arise. Classification by business model reflects how the Group manages its financial assets to generate cash flows. A business model assessment determines if cash flows result from holding financial assets to collect the contractual cash flows; from selling those financial assets; or both.

The product classifications apply to financial assets that are either designated as at fair value through profit or loss (DFV), or to equity investments designated as at fair value through other comprehensive income (FVOCI). In all other instances, fair value through profit or loss (MFVTPL) is the default classification and measurement category for financial assets.

Regular way purchases of financial assets classified as amortised cost are recognised on the settlement date; all other regular way transactions in financial assets are recognised on the trade date.

All financial instruments are measured at fair value on initial recognition.

All liabilities not subsequently measured at fair value are measured at amortised cost.

Business models assessment of assets is made at portfolio level, being the level at which they are managed to achieve a predefined business objective. This is expected to result in the most consistent classification of assets because it aligns with the stated objectives of the portfolio, its risk management, manager's remuneration and the ability to monitor sales of assets from a portfolio.

Most financial assets are within "held to collect" business models, and have contractual cash flows that comprise solely payments of principal and interest and are measured at amortised cost. Certain financial assets managed under a business model of both "held to collect and sell" and have contractual cash flows comprising solely of payments of principal and interest, and are measured at fair value through other comprehensive income ('FVOCI').

The contractual terms of a facility; any leverage features; prepayment and extension terms; and triggers that might reset the effective rate of interest; are considered in determining whether cash flows comprise solely payments of principal and interest.

14. Impairment: expected credit losses

At each balance sheet date each financial asset or portfolio of loans measured at amortised cost or at fair value through other comprehensive income, issued financial guarantee and loan commitment is assessed for impairment. Loss allowances are forward looking based on 12 month expected credit losses where there has not been a significant increase in credit risk rating, otherwise allowances are based on lifetime expected losses.

Expected credit losses are a probability-weighted estimate of credit losses. The probability is determined by the risk of default which is applied to the cash flow estimates. In the absence of a change in credit rating, allowances are recognised when there is reduction in the net present value of expected cash flows. On a significant increase in credit risk, allowances are recognised without a change in the expected cash flows, although typically expected cash flows do also change; and expected credit losses are rebased from 12 month to lifetime expectations.

Judgement is exercised as follows:

- Models – in certain low default portfolios, Basel parameter estimates are also applied for IFRS 9.
- Non-modelled portfolios, use a standardised capital requirement under Basel II. Under IFRS 9, they have bespoke treatments for the identification of significant increase in credit risk. Benchmark PDs, EADs and LGDs are reviewed annually for appropriateness. The ECL calculation is based on expected future cash flows, which is typically applied at a portfolio level.
- Multiple economic scenarios (MES) – the central, or base, scenario is most critical to the ECL calculation, independent of the method used to generate a range of alternative outcomes and their probabilities.
- Significant increase in credit risk - IFRS 9 requires that at each reporting date, an entity shall assess whether the credit risk on an account has increased significantly since initial recognition. Part of this assessment requires a comparison to be made between the current lifetime PD (i.e. the current probability of default over the remaining lifetime) with the equivalent lifetime PD as determined at the date of initial recognition.

On restructuring a financial asset without causing derecognition of the original asset the revised cash flows are used in re-estimating the credit loss. Where restructuring causes derecognition of the original financial asset, the fair value of the replacement asset is used as the closing cash flow of the original asset.

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

The costs of loss allowances on assets held at amortised cost are presented as impairments in the income statement. Allowances in respect of financial guarantees and loan commitments are presented in impairments in the income statement. Contingent liabilities are presented gross of allowances except where the asset has been wholly or partially written off.

15. Financial guarantee contracts

Under a financial guarantee contract, the Group, in return for a fee, undertakes to meet a client's obligations under the terms of a debt instrument if the client fails to do so. A financial guarantee is recognised as a liability; initially at fair value and, if not designated at fair value through profit or loss, subsequently at the higher of its initial value less cumulative amortisation and any provision under the contract measured in accordance with accounting policy 14. Amortisation is calculated so as to recognise fees receivable in profit or loss over the period of the guarantee.

16. Derecognition

A financial asset is derecognised when the contractual right to receive cash flows from the asset has expired or when it has been transferred and the transfer qualifies for derecognition. Conversely, an asset is not derecognised by a contract under which the Group retains substantially all the risks and rewards of ownership. If substantially all the risks and rewards have been neither retained nor transferred, the Group does not derecognise an asset over which it has retained control but limits its recognition to the extent of its continuing involvement.

A financial liability is removed from the balance sheet when the obligation is discharged, or is cancelled, or expires. Cancellation includes the issuance of a substitute instrument on substantially different term.

17. Capital Instruments

The Bank classifies a financial instrument that it issues as a liability if there is a contractual obligation to deliver cash or another financial asset, or to exchange financial assets or financial liabilities on potentially unfavourable terms and as equity if it evidences a residual interest in the assets of the Bank after the deduction of liabilities.

18. Derivatives

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. A derivative embedded in a contract is accounted for as a standalone 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.

The Bank's client derivatives are hedged directly with NWB with no material fair value impact to the profit or loss.

19. Cash and cash equivalents

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

20. Investment in Group undertakings
The Bank's investments in its subsidiaries are stated at cost less any impairment.

Critical accounting policies and key sources of estimation uncertainty
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 of interpretation, 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 the light of the requirements and guidance in IFRS dealing with similar and related issues and the IASB's 'Conceptual Framework for Financial Reporting'. 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.

Critical accounting policy	Note
Loan impairment provisions	8
Provisions for liabilities and charges	15

Accounting developments
International Financial Reporting Standards
A number of IFRSs and amendments to IFRS were in issue at 31 December 2019 that would affect the Group from 1 January 2020 or later.

Effective 1 January 2020
The amendments to IAS 1 'Presentation of Financial Statements' and IAS 8 'Accounting Policy, Changes in Accounting Estimates and Errors' on the definition of material were issued in October 2018 and are effective for annual periods beginning on or after 1 January 2020 with earlier application permitted. The amendments are aimed at improving the understanding of the existing requirements rather than to significantly impact current materiality judgements. They provide a new definition of material which shall be used to assess whether information, either individually or in combination with other information, is material in the context of the financial statements.

The amendments to IFRS 3 'Business Combinations' which clarify the definition of a Business were issued in October 2018, are effective for annual reporting periods beginning on or after 1 January 2020 and apply prospectively with earlier application permitted. They clarify the minimum requirements for a business; remove the assessment of whether market participants are capable of replacing any missing elements; add guidance to help entities assess whether an acquired process is substantive; narrow the definitions of a business and of outputs; and introduce an optional fair value concentration test.

Effective in 2022 - IFRS 17 'Insurance contracts' was issued in May 2017 to replace IFRS 4 and to establish a comprehensive standard for inceptors of insurance policies. The effective date is 1 January 2021, subject to IASB's approval of a deferral until 1 January 2022.

The Group is assessing the effect of adopting these standards on its financial statements.

NOTES TO THE ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2019

1. Net interest income

	2019 £m	2018 £m
Loans to customers - amortised cost	413	384
Loans to banks - amortised cost	194	160
Interest receivable	607	544
Bank deposits	(65)	(50)
Customer deposits	(91)	(51)
Lease liabilities	(1)	-
Interest payable	(157)	(101)
Net interest income	450	443

2. Non-interest income

	2019 £m	2018 £m
Fees and commission receivable		
Investment management income	148	160
Payment Services fee	31	31
Other income	31	15
Card fee	12	12
Brokerage fee	5	5
Credit Facilities fee	2	2
Trade Finance	1	1
	230	226
Fees and commission payable		
Clearing and settlement	(12)	(10)
Other	(2)	(8)
	(14)	(18)
Other operating income		
Dealing profits	27	25
Rental income	4	3
Changes in the fair value of investment properties	(5)	-
Other income	(2)	2
	24	30
Non-interest income	240	238

3. Operating expenses

	2019 £m	2018 £m
Wages, salaries and other staff costs	103	106
Bonus tax	15	15
Social security costs	13	13
Pension costs	11	4
Staff costs	142	138
Premises and equipment	13	13
Depreciation & amortisation (see note 11 and 12)	12	10
Other operating charges[1]	174	157
Other expenses[2]	56	49
Other administrative expenses	230	206
Operating expenses	397	367

Notes:
(1) Other operating charges consist of recharges from RBS Group companies.
(2) Other expenses consists of other miscellaneous costs included in which are litigation and conduct costs. Further details of conduct and litigation are provided in note 15.

The average number of persons seconded by the Group during the year was made up as follows:

	2019 Number	2018 Number
Managers	590	595
Clerical and other staff	979	965
	1,569	1,560

4. Auditor's remuneration

All audit-related and other services are approved by the RBS Group Audit Committee and are subject to strict controls to ensure the external auditor's independence is unaffected by the provision of other services. The RBS Group Audit Committee recognises that for certain assignments the auditors are best placed to perform the work economically; for other work the Group selects the supplier best placed to meet its requirements. The Group's auditors are permitted to tender for such work in competition with other firms where the work is permissible under audit independence rules. The Group's Audit Committee reviews the amount of audit and non audit services provided by the Group's auditor.

Amounts paid to the Group's auditors for statutory audit and other services are set out below:

	2019 £m	2018 £m
Fees payable for the audit of the Group's annual accounts	0.4	0.3
Non audit work:	-	-
- Other services pursuant to legislation	0.2	0.2
Total audit and audit-related assurance services fees	0.6	0.5

In addition, the auditor received remuneration for RBS reporting audit work; this fee was borne by RBS Group.

5. Emoluments of directors

	2019 £m	2018 £m
Chairman and non-executive directors - emoluments	0.3	0.3
Executive directors - emoluments	1.5	1.3
	1.8	1.6

Number of directors to whom retirement benefits are accruing in respect of qualifying service:		
- money purchase schemes	2	1
- defined benefit schemes	-	-

5. Emoluments of directors continued

The total emoluments of the highest paid director were £1.1 million (2018 - £1 million). This includes long term benefits consisting of Long Term Incentive Plans and deferred pay awards. The accrued pension attributable to that director was £0.1 million (2018 - £0.1 million). The executive directors may also participate in the RBS executive share option and share save schemes.

6. Tax

	2019 £m	2018* £m
Current tax		
Charge for the year	82	86
Over provision in respect of prior years	(3)	(7)
	79	79
Deferred tax		
Origination and reversal of timing differences	1	1
Under provision in respect of prior years	-	6
	1	7
Tax charge for the year	80	86

The actual tax charge differs from the expected tax charge computed by applying the UK corporation tax rate of 19% (2018 - 19%) as follows:

	2019 £m	2018* £m
Expected tax charge(1)	57	61
Factors affecting the charge for the year:		
Items not allowed for tax	5	4
Tax credit paid in equity	(3)	(3)
Banking surcharge	24	25
Adjustments in respect of prior years	(3)	(1)
Actual tax charge	80	86

*Restated for IAS 12 'Income taxes' refer to accounting policy 1 for further details.

Note:
(1) In recent years the UK Government has steadily reduced the rate of UK corporation tax, with the latest rates substantively enacted at the balance sheet date standing at 19% from 1 April 2017 and 17% from 1 April 2020. Under the Finance (No 2) Act 2015, tax losses carried forward at 31 December 2015 are given credit in future periods at the main rate of UK corporation tax rate, excluding the Banking Surcharge rate (8%) introduced by the Act. The closing deferred tax assets and liabilities have been calculated taking into account that existing temporary differences may unwind in periods subject to the reduced rates.

Deferred tax

	Group		Bank	
	2019 £m	2018 £m	2019 £m	2018 £m
Deferred tax asset	8	9	9	10

Net deferred tax asset comprised:

	Group			Bank		
	Other timing differences £m	IFRS Transition £m	Total £m	Other timing differences £m	IFRS Transition £m	Total £m
At 1 January 2018	10	-	10	10	-	10
IFRS9 transitional adjustments	-	6	6	-	7	7
Charge to income statement	(6)	(1)	(7)	(6)	(1)	(7)
At 1 January 2019	4	5	9	4	6	10
Charge to income statement	(1)	-	(1)	(1)	-	(1)
At 31 December 2019	3	5	8	3	6	9

6. Tax continued

The provision for UK deferred taxation has been calculated at 25% (2018 - 27%), inclusive of the 8% Banking Surcharge. A deferred tax asset of £8 million has been recognised for the Group at 31 December 2019 (2018 - £9 million). This asset has been recognised in the financial statements following the deferral of bonuses under the medium-term incentive plan, the provision for litigation and sundry losses, the impairment and redress provision, the movement in investment property fair value and accelerated capital allowances. Based on recent and forecasted trading, the tax due on future profits in the current and next financial year will exceed the value of the deferred tax asset.

The directors are of the opinion that, in view of the type and use of properties involved, the likelihood of any material tax liabilities arising on the disposal of the Group's non-investment properties at current market value is so remote that no useful purpose would be served in attempting to quantify it. The Group's principal property is occupied for the purposes of the Group's trade and consequently any gains arising on disposal are expected to be rolled-over pursuant to Taxation of Chargeable Gains Act 1992, Section 152.

7. Financial instruments

Financial instruments - classification

The following tables analyse the Company's financial assets and financial liabilities in accordance with the categories of financial instruments in IFRS 9. Assets and liabilities outside the scope of IFRS 9 are shown within other assets and liabilities.

	Group			
Assets	Mandatory fair value through profit or loss £m	Amortised cost £m	Other assets £m	Total £m
Cash and balances at central bank	-	3	-	3
Loans to banks - amortised cost	-	143	-	143
Loans to customers - amortised cost	-	14,792	-	14,792
Amount due from holding companies and fellow subsidiaries(1)	-	18,690	-	18,690
Derivatives	22	-	-	22
Property, plant and equipment	-	-	294	294
Other assets	-	34	59	93
31 December 2019	22	33,662	353	34,037
Cash and balances at central bank	-	2	-	2
Loans to banks - amortised cost	-	121	-	121
Loans to customers - amortised cost	-	13,566	-	13,566
Amount due from holding companies and fellow subsidiaries(1)	-	20,238	-	20,238
Derivatives	20	-	-	20
Property, plant and equipment	-	-	246	246
Other assets	-	33	54	87
31 December 2018	20	33,960	300	34,280

Note:
(1) £1.9 billion of short dated intercompany assets and liabilities, which meet the IAS 32 criteria, have been netted in 2019. The 2018 balances of £1.8 billion have been presented gross.

7. Financial instruments continued

Financial instruments – classification continued

Liabilities	Group Mandatory fair value through profit or loss £m	Amortised cost £m	Non-financial liabilities £m	Total £m
Bank deposits	-	12	-	12
Customer deposits	-	26,390	-	26,390
Amount due to holding companies and fellow subsidiaries(1)	-	5,463	-	5,463
Derivatives	20	-	-	20
Other financial liabilities	-	310	-	310
Other liabilities	-	3	221	224
Subordinated liabilities	-	265	-	265
31 December 2019	20	32,443	221	32,684
Bank deposits	-	5	-	5
Customer deposits	-	26,527	-	26,527
Amount due to holding companies and fellow subsidiaries(1)	-	5,944	-	5,944
Derivatives	20	-	-	20
Other liabilities	-	12	95	107
Subordinated liabilities	-	315	-	315
31 December 2018	20	32,803	95	32,918

Note:
(1) £1.9 billion of short dated intercompany assets and liabilities, which meet the IAS 32 criteria, have been netted in 2019. The 2018 balances of £1.8 billion have been presented gross.

Assets	Bank Mandatory fair value through profit or loss £m	Amortised cost £m	Other assets £m	Total £m
Cash and balances at central bank	-	3	-	3
Loans to banks - amortised cost	-	124	-	124
Loans to customers - amortised cost	-	14,172	-	14,172
Amount due from holding companies and fellow subsidiaries(1)	-	19,249	-	19,249
Derivatives	22	-	-	22
Investment in Group undertakings	-	-	110	110
Property, plant and equipment	-	-	294	294
Other assets	-	28	48	76
31 December 2019	22	33,576	452	34,050
Cash and balances at central bank	-	2	-	2
Loans to banks - amortised cost	-	100	-	100
Loans to customers - amortised cost	-	12,587	-	12,587
Amount due from holding companies and fellow subsidiaries(1)	-	21,124	-	21,124
Derivatives	20	-	-	20
Investment in Group undertakings	-	-	110	110
Property, plant and equipment	-	-	246	246
Other assets	-	27	43	70
31 December 2018	20	33,840	399	34,259

Note:
(1) £1.9 billion of short dated intercompany assets and liabilities, which meet the IAS 32 criteria, have been netted in 2019. The 2018 balances of £1.8 billion have been presented gross.

7. Financial instruments continued

Financial instruments - classification continued

	Bank			
Liabilities	Mandatory fair value through profit or loss £m	Amortised cost £m	Non-financial liabilities £m	Total £m
Bank deposits	-	12	-	12
Customer deposits	-	26,390	-	26,390
Amount due to holding companies and fellow subsidiaries[1]	-	5,463	-	5,463
Derivatives	20	-	-	20
Other financial liabilities	-	310	-	310
Other liabilities	-	5	210	215
Subordinated liabilities	-	265	-	265
31 December 2019	20	32,445	210	32,675
Bank deposits	-	5	-	5
Customer deposits	-	26,527	-	26,527
Amount due to holding companies and fellow subsidiaries[1]	-	5,944	-	5,944
Derivatives	20	-	-	20
Other liabilities	-	5	86	91
Subordinated liabilities	-	315	-	315
31 December 2018	20	32,796	86	32,902

Note:
(1) £1.9 billion of short dated intercompany assets and liabilities, which meet the IAS 32 criteria, have been netted in 2019. The 2018 balances of £1.8 billion have been presented gross.

Financial instruments - valuations

The following table shows the financial instruments carried at fair value:

	Group and Bank					
	2019			2018		
	Level 1 £m	Level 2[1] £m	Level 3[2] £m	Level 1 £m	Level 2[1] £m	Level 3[2] £m
Assets						
Derivatives	-	22	-	-	20	-
	-	22	-	-	20	-
Liabilities						
Derivatives	-	20	-	-	20	-
	-	20	-	-	20	-

Notes:
(1) Valued using techniques based significantly on observable market data. Instruments in this category are valued using quoted prices for similar instruments.
(2) 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.

In accordance with accounting policies 13 and 18, financial instruments at fair value through profit or loss and financial assets classified as fair value through other comprehensive income are recognised in the financial statements at fair value. All derivatives are measured at fair value.

7. Financial instruments continued

Financial instruments – valuations continued

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

	Group					
				Fair value hierarchy level		
2019	Items where fair value approximates carrying value £m	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets						
Cash and balances at central bank	3	-	-	-	-	-
Loans to banks	143	-	-	-	-	-
Loans to customers	1,223	13,569	13,474	-	-	13,474
Amount due from holding companies and fellow subsidiaries	8,292	10,398	10,347	26	-	10,321
Other assets	34	-	-	-	-	-
Financial liabilities						
Bank deposits	12	-	-	-	-	-
Customer deposits	26,390	-	-	-	-	-
Amount due to holding companies and fellow subsidiaries	108	5,355	5,332	-	-	5,332
Other financial liabilities	310	-	-	-	-	-
Subordinated liabilities	-	265	256	-	-	256

	Group					
				Fair value hierarchy level		
2018	Items where fair value approximates carrying value £m	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets						
Cash and balances at central bank	2	-	-	-	-	-
Loans to banks	121	-	-	-	-	-
Loans to customers	1,216	12,350	12,142	-	-	12,142
Amount due from holding companies and fellow subsidiaries	10,817	9,421	9,336	-	-	9,336
Other assets	33	-	-	-	-	-
Financial liabilities						
Bank deposits	5	-	-	-	-	-
Customer deposits	26,527	-	-	-	-	-
Amount due to holding companies and fellow subsidiaries	1,887	4,057	4,005	-	-	4,005
Subordinated liabilities	95	220	219	-	-	219

7. Financial instruments continued

Financial instruments - valuations continued

	Bank					
				Fair value hierarchy level		
2019	Items where fair value approximates carrying value £m	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets						
Cash and balances at central bank	3	-	-	-	-	-
Loans to banks	124	-	-	-	-	-
Loans to customers	1,202	12,970	12,889	-	-	12,889
Amount due from holding companies and fellow subsidiaries	8,670	10,579	10,532	26	-	10,506
Other assets	28	-	-	-	-	-
Financial liabilities						
Bank deposits	12	-	-	-	-	-
Customer deposits	26,390	-	-	-	-	-
Amount due to holding companies and fellow subsidiaries	108	5,355	5,332	-	-	5,332
Other financial liabilities	310	-	-	-	-	-
Subordinated liabilities	-	265	256	-	-	256

	Bank					
				Fair value hierarchy level		
2018	Items where fair value approximates carrying value £m	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets						
Cash and balances at central bank	2	-	-	-	-	-
Loans to banks	100	-	-	-	-	-
Loans to customers	1,167	11,420	11,237	-	-	11,237
Amount due from holding companies and fellow subsidiaries	11,284	9,840	9,756			9,756
Other assets	27	-	-	-	-	-
Financial liabilities						
Bank deposits	5	-	-	-	-	-
Customer deposits	26,527	-	-	-	-	-
Amount due to holding companies and fellow subsidiaries	1,887	4,057	4,009			4,009
Subordinated liabilities	95	220	219	-	-	219

7. Financial instruments continued

Financial instruments - valuations continued

The fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Quoted market values are used where available, otherwise, fair values have been established based on discounted expected future cash flows and other valuation techniques. These techniques involve uncertainties and require assumptions and judgements covering prepayments, credit risk and discount rates. Furthermore there is a wide range of potential valuation techniques. 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.

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

Short-term financial instruments
For certain short-term financial instruments: 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 client demand deposits, carrying value is a reasonable approximation of fair value.

Loans to banks and customers – amortised cost
In estimating the fair value of loans to banks and customers measured at amortised cost, loans are segregated into appropriate portfolios reflecting the characteristics of the constituent loans. Two principal methods are used to estimate fair value:

(a) Contractual cash flows are discounted using a market discount rate that incorporates the current spread for the borrower or where this is not observable, the spread for borrowers of a similar credit standing.
(b) Expected cash flows (unadjusted for credit losses) are discounted at the current offer rate for the same or similar products.

Bank and customer deposits
Fair values of deposits are estimated using discounted cash flow valuation techniques.

Debt securities in issue and subordinated liabilities
Fair values are determined by using internal valuation models or using quoted prices for similar liabilities.

Financial instruments - maturity analysis

Remaining maturity

The following table shows the residual maturity of financial instruments, based on contractual date of maturity:

	Group					
	2019			2018		
	Less than 12 months £m	More than 12 months £m	Total £m	Less than 12 months £m	More than 12 months £m	Total £m
Assets						
Cash and balances at central bank	3	-	3	2	-	2
Loans to banks - amortised cost	143	-	143	121	-	121
Loans to customers - amortised cost	4,921	9,871	14,792	4,667	8,899	13,566
Amount due from holding companies and fellow subsidiaries	11,702	6,988	18,690	13,320	6,918	20,238
Derivatives	1	21	22	1	19	20
Other assets	34	-	34	33	-	33
Liabilities						
Bank deposits	12	-	12	5	-	5
Customer deposits	26,390	-	26,390	26,523	4	26,527
Amount due to holding companies and fellow subsidiaries	1,061	4,402	5,463	2,563	3,381	5,944
Derivatives	1	19	20	1	19	20
Other financial liabilities	-	310	310	-	-	-
Subordinated liabilities	-	265	265	-	315	315
Lease liabilities	1	56	57	-	-	-

7. Financial instruments continued

Financial instruments - maturity analysis continued

	Bank					
	2019			2018		
	Less than 12 months £m	More than 12 months £m	Total £m	Less than 12 months £m	More than 12 months £m	Total £m
Assets						
Cash and balances at central bank	3	-	3	2	-	2
Loans to banks - amortised cost	124	-	124	100	-	100
Loans to customers - amortised cost	4,721	9,451	14,172	4,258	8,329	12,587
Amount due from holding companies and fellow subsidiaries	12,177	7,072	19,249	14,037	7,087	21,124
Derivatives	1	21	22	1	19	20
Other assets	28	-	28	27	-	27
Liabilities						
Bank deposits	12	-	12	5	-	5
Customer deposits	26,390	-	26,390	26,523	4	26,527
Amount due to holding companies and fellow subsidiaries	1,061	4,402	5,463	2,563	3,381	5,944
Derivatives	1	19	20	1	19	20
Other financial liabilities	-	310	310	-	-	-
Subordinated liabilities	-	265	265	-	315	315
Lease liabilities	1	56	57	-	-	-

8. Loan impairment provisions

	2019 £m	2018* £m
Loans - amortised cost		
Stage 1	14,292	13,089
Stage 2	552	506
Stage 3	180	193
Total	15,024	13,788
ECL provisions		
Stage 1	7	13
Stage 2	6	10
Stage 3	26	25
Total	39	48
ECL provision coverage		
Stage 1 (%)	0.0	0.1
Stage 2 (%)	1.1	2.0
Stage 3 (%)	14.4	13.0
Total (%)	0.3	0.4
Total ECL release	7	7
ECL loss rate (basis point)(1)	NA	NA
Amounts written off	1	7

Note:
(1) No ECL loss for the current or prior year, hence ECL loss rate is not applicable.

* 2018 data has been restated for a change to presentation of unrecognised interest. Refer to accounting policy 1, Other amendments to IFRS, for further details.

Amounts due from holding companies and fellow subsidiaries (Inter-Group) are all considered as Stage 1.

8. Loan impairment provisions continued

Critical accounting policy: loan impairment provisions
The loan impairment provisions have been established in accordance with IFRS 9. Accounting policy 14 sets out how the expected loss approach is applied. Key judgements in respect of the measurement of ECL include the selection of the most appropriate RBS Group credit models and modelling assumptions used to calculate the Group's ECL. At 31 December 2019, customer loan impairment provisions amounted to £39 million (2018 - £48 million). A loan is impaired when there is objective evidence that the cash flows will not occur in the manner expected when the loan was advanced. Such evidence includes changes in the credit rating of a borrower, the failure to make payments in accordance with the loan agreement; significant reduction in the value of any security; breach of limits or covenants; and observable data about relevant macroeconomic measures.

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.

Further details relating to the credit risk framework can be found on page 17 to 26.

Key economic loss drivers
The table below shows the base case economics used at 31 December 2019.

	2019					2018				
	Upside 2	Upside 1	Base case	Downside 1	Downside 1	Upside 2	Upside 1	Base case	Downside 1	Downside 1
UK	%	%	%	%	%	%	%	%	%	%
GDP - change	2.4	2.2	1.6	1.3	0.9	2.6	2.3	1.7	1.5	1.1
Unemployment	3.6	3.9	4.4	4.7	5.2	3.3	3.8	5.0	5.6	6.9
House Price Inflation - change	4.1	3.3	1.6	0.8	(1.0)	4.3	3.3	1.7	1.1	(0.5)
Bank of England base rate	1.0	0.7	0.3	-	-	1.7	1.3	1.1	0.5	-
World GDP - change	3.8	3.3	2.8	2.5	2.1	3.6	3.2	2.7	2.5	2.3
Probability weight	12.7	14.8	30.0	29.7	12.7	12.8	17.0	30.0	25.6	14.6

Sensitivity of impairments to assumptions
Key assumptions relating to impairment levels are economic conditions, the interest rate environment, the ease and timing of enforcing loan agreements in varying legal jurisdictions and the level of client co-operation. In addition, for secured lending, key assumptions relate to the valuation of the security and collateral held, as well as the timing and cost of asset disposals based on underlying market depth and liquidity.

Due to the low level of default and high level of collateral, loan impairments are not very sensitive to these economic scenarios.

9. Derivatives

	Group and Bank					
	2019			2018		
	Notional amounts £m	Assets £m	Liabilities £m	Notional amounts £m	Assets £m	Liabilities £m
Exchange rate contracts:						
Spot, forwards and futures	108	1	1	69	1	1
Currency swaps	18	-	-	20	-	-
Interest rate contracts:						
Interest rate swaps	1,071	21	19	1,070	19	19
	1,197	22	20	1,159	20	20

10. Investments in Group undertakings

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

	Bank	
	2019	2018
	£m	£m
At 1 January	110	3
Acquisitions	-	107
At 31 December	110	110

The acquisition in 2018 relates to 100% of the share capital of RBS Asset Management Holdings acquired through a capital contribution from NWB.

The subsidiary undertakings of the Bank are shown below. Their capital consists of ordinary shares which are unlisted.

All of the subsidiary undertakings are owned directly or indirectly through intermediate holding companies and are all wholly owned. They are included in the Group's consolidated financial statements and have an accounting reference date of 31 December.

	Proportion of ownership (%)	Nature of business	Country of incorporation
Coutts Finance Co.[(1)]	100%	Provision of residential mortgages	Great Britain
RBS Asset Management (Dublin) Limited[(3)]	100%	Provision of management services	Ireland
RBS Collective Investment Funds Limited[(2)]	100%	Provision of management services	Great Britain
RBS Asset Management Holdings[(1)]	100%	Holding company	Great Britain
RBS Asset Management (ACD) Limited[(1)]	100%	Provision of management services	Great Britain
RBSG Collective Investments Holdings Limited[(2)]	100%	Holding company	Great Britain
RBSG Collective Investments Nominees Limited[(2)]	100%	Nominee	Great Britain
Strand Nominees Limited[(1)]	100%	Nominee	Great Britain

No impairment was recognised in 2019 or 2018.

Notes:
(1) Registered office is 440 Strand, London.
(2) Registered office is 24/25 St Andrews Sq, Edinburgh.
(3) Registered office is One Dockland Central, Dublin.

11. Property, plant and equipment

	Group and Bank						
2019	Investment properties £m	Land £m	Building £m	Short Leasehold £m	Computer and other equipment £m	Right of use property* £m	Total £m
Cost or valuation:							
At 1 January	55	47	153	3	16	-	274
Implementation of IFRS 16 on 1 January 2019	-	-	-	-	-	60	60
Additions	-	-	2	-	3	1	6
Disposals	-	-	-	(2)	(1)	-	(3)
Fair value adjustment	(5)	-	-	-	-	-	(5)
At 31 December	50	47	155	1	18	61	332
Accumulated depreciation and amortisation:							
At 1 January	-	-	14	3	11	-	28
Implementation of IFRS 16 on 1 January 2019	-	-	-	-	-	4	4
Charge for the year	-	-	6	-	1	1	8
Disposals	-	-	-	(2)	-	-	(2)
At 31 December	-	-	20	1	12	5	38
Net book value at 31 December	50	47	135	-	6	56	294

*For further details on the adoption of IFRS 16 see note 19.

11. Property, plant and equipment continued

	Group and Bank					
2018	Investment properties £m	Land £m	Building £m	Short Leasehold £m	Computer and other equipment £m	Total £m
Cost or valuation:						
At 1 January	55	47	150	3	14	269
Additions	-	-	3	-	4	7
Disposals	-	-	-	-	(2)	(2)
At 31 December	55	47	153	3	16	274
Accumulated depreciation and amortisation:						
At 1 January	-	-	7	3	10	20
Charge for the year	-	-	7	-	1	8
At 31 December	-	-	14	3	11	28
Net book value at 31 December	55	47	139	-	5	246

There was no loss on disposal of assets during the year (2018 - £nil).

Investment property valuations principally employ present value techniques that discount expected cash flows. Expected cash flows reflect rental income, occupancy and residual market values; valuations are sensitive to changes in these factors. The investment property fair value measurements are categorised as level 3.

Valuations were carried out by qualified surveyors who are members of the Royal Institution of Chartered Surveyors, or an equivalent overseas body.

Rental income from investment properties was £4 million (2018 - £3 million).

12. Intangible assets

	Group					
	2019			2018		
	Goodwill £m	Other(1) £m	Total £m	Goodwill £m	Other(1) £m	Total £m
Cost:						
At 1 January	9	33	42	-	20	20
Additions	-	12	12	9	13	22
At 31 December	9	45	54	9	33	42
Accumulated amortisation:						
At 1 January	-	3	3	-	1	1
Charge for the year	-	4	4	-	2	2
At 31 December	-	7	7	-	3	3
Net book value at 31 December	9	38	47	9	30	39

Note:
(1) Principally internally generated software.

12. Intangible assets continued

	Bank	
	2019 £m	2018 £m
Cost:		
At 1 January	33	20
Additions	12	13
At 31 December	45	33
Amortisation:		
At 1 January	3	1
Charge for the year	4	2
At 31 December	7	3
Net book value at 31 December	38	30

13. Other assets

	Group		Bank	
	2019 £m	2018 £m	2019 £m	2018 £m
Due within 12 months:				
Prepayments	3	2	2	2
Current tax	-	-	-	2
Accrued income and other assets[1]	35	37	27	26
Due after 12 months:				
Deferred tax (refer note 6)	8	9	9	10
Intangible assets (refer note 12)	47	39	38	30
	93	87	76	70

Note:
(1) Balances primarily consist of accrued fee income.

14. Other financial liabilities

	Group and Bank	
	2019 £m	2018 £m
Debt securities in issue - amortised cost	310	-
	310	-

15. Other liabilities

	Group		Bank	
	2019 £m	2018 £m	2019 £m	2018 £m
Due within 12 months:				
Accruals	14	19	12	13
Deferred income	19	20	19	21
Other liabilities	3	12	5	5
Lease liabilities	57	-	57	-
Current tax	77	4	68	-
Due after 12 months:				
Provisions for liabilities and charges	54	52	54	52
	224	107	215	91

15. Other liabilities continued

The following amounts are included within provisions for liabilities and charges:

	Group and Bank		
	Provision for severance £m	Other £m	Total £m
At 1 January 2019	6	46	52
Charge to income statement	3	12	15
Releases to income statement	(2)	(2)	(4)
Provisions utilised	(3)	(6)	(9)
At 31 December 2019	4	50	54

Critical accounting policy: Provision for liabilities
Judgement is involved in determining whether an obligation exists, and in estimating the probability, timing and amount of any outflows. Where the Group can look to another party such as an insurer to pay some or all of the expenditure required to settle a provision, any reimbursement is recognised when, and only when, it is virtually certain that it will be received. The Group generally does not disclose information about the establishment or existence of a provision for a particular matter where disclosure of the information can be expected to prejudice seriously the Group's position in the matter.

Estimates - Provisions are liabilities of uncertain timing or amount and are recognised when there is a present obligation as a result of a past event, the outflow of economic benefit is probable and the outflow can be estimated reliably. Any difference between the final outcome and the amounts provided will affect the reported results in the period when the matter is resolved.

16. Subordinated liabilities

	Group and Bank				
	2019 Interest rate	2019 £m	2018 Interest rate	2018 £m	Maturity
Due to:					
National Westminster Bank Plc					
£221,000,000	2.90%	220	2.90%	220	2027
£45,000,000	Libor + 3.85%	45	Libor + 3.85%	45	2028
£50,000,000	-	-	Libor + 2.15%	50	2024
		265		315	

The loans are unsecured and subordinated to the claims of senior creditors. The loan capital is available to absorb losses but ranks ahead of other existing capital in the event of liquidation. The Bank has a contractual obligation to pay interest.

17. Share Capital and reserves

	Group and Bank			
	Allotted, called up and fully paid		Authorised	
	2019 £m	2018 £m	2019 £m	2018 £m
Equity shares:				
Ordinary shares of £1	41	41	50	50
Total share capital	41	41	50	50

Ordinary shares
During the year, the Bank paid ordinary dividends totalling £215 million (2018 - £90 million) to NWB.

Reserves

In 2018, the Group received a capital contribution from NWB for which no additional share capital was issued. Refer to note 10 for further details on the acquisition in 2018.

18. Paid-in equity

Paid-in equity comprises equity instruments issued by the Bank other than those legally constituted as shares

	Group and Bank	
	2019	2018
	£m	£m
Additional Tier 1 capital notes:		
£167 million 6.0% notes repayable from September 2022	165	165
£35 million Libor + 6.09% notes repayable from December 2023	35	35
	200	200

The coupons on this instrument are non-cumulative and payable at the Bank's discretion. In the event of winding up, any amounts outstanding on the loan will be subordinated. While taking the legal form of debt, these notes are classified as equity under IFRS.

Equity coupon payments

Equity coupon payments totalling £13 million were paid in the year (2018 - £10 million).

19. Leases

The Group has adopted IFRS 16 Leases retrospectively from 1 January 2019 but has not restated comparatives as permitted under the transition provisions of the standard. The impact on the Group's balance sheet and retained earnings is shown below:

The impact on the balance sheet at 1 January 2019 is as follows:

	Group
	2019
	£m
Retained earnings at 1 January 2019	782
Other assets - Net right of use assets	55
- Recognition of lease liabilities	(57)
- Provision for onerous leases	1
Other liabilities	(56)
Net impact on retained earnings	(1)
Retained earnings at 1 January 2019	781

On adoption of IFRS 16, the Group recognised right of use assets and lease liabilities in relation to leases which has been previously classified as operating leases under IAS 17 Leases subject to certain practical expedients as allowed by the standard.

The following practical expedients permitted by the standard were used:
- A single discount rate has been applied to a portfolio of leases with reasonably similar characteristics.
- Not applying IFRS 16 to operating leases with a remaining lease term of less than 12 months or low volume leases (non-property leases)
- Exclusion of initial direct costs from the measurement of the right of use asset at the date of initial application.
- Reliance on the assessment of whether the lease contract is overseas under IAS 37 Provisions, Contingent liabilities and Contingent assets at 31 December 2018 as an alternative to performing an impairment review of right of use assets created on 1 January 2019.
- The use of hindsight where contracts contain options to extend or terminate the lease in determining the lease term.

The lease liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of 1 January 2018. The weighted average lessee's incremental borrowing rate applied to the lease liabilities on 1 January 2019 was 2.2%.

	Group
	2019
	£m
Operating lease commitments as disclosed as at 31 December 2018	176
Adjustments as a result of a different treatment of extension and termination options	(2)
Discounted using the incremental borrowing rate	(117)
Lease liability recognised as at 1 January 2019 on adoption of IFRS 16	57

19. Leases continued

Lessees

	Group 2019 £m
Amounts recognised in consolidated income statement	
Interest payable	1
Depreciation	1

	Group and Bank 2019 £m
Amounts recognised on balance sheet	
Right of use assets included in property, plant and equipment(1)	56
Additions to right of use assets	1
Lease liabilities	(57)

The total cash outflow for leases is £1 million.

Note:
(1) Includes right of use asset for plant and equipment of £61 million and depreciation of £5 million.

	Group and Bank 2018 £m
Operating leases	
Minimum rentals payable under non-cancellable leases(1)	
- within 1 year	2
- after 1 year but within 5 years	7
- after 5 years	166
Total	175

Note:
(1) Predominantly property leases.

20. 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 2019. Although the Group and the Bank are exposed to credit risk in the event of non-performance of the obligations undertaken by clients, the amounts shown do not, and are not intended to, provide any indication of the Group and Bank's expectation of future losses.

	Group and Bank	
	2019 £m	2018 £m
Contingent liabilities:		
Guarantees and assets pledged as collateral security:		
- Guarantees and irrevocable letters of credit	73	75
	73	75
Commitments:		
Undrawn formal standby facilities, credit lines and other commitments to lend:		
- 1 year and over	436	704
- Less than 1 year	2,407	2,282
	2,843	2,986

20. Memorandum items continued

Banking commitments and contingent obligations, which have been entered into on behalf of clients and for which there are corresponding obligations from clients, are not included in assets and liabilities. The Group and Bank's maximum exposure to credit loss, in the event of its obligation crystallising and all counterclaims, collateral or security proving valueless, is represented by the contractual nominal amount of these instruments included in the table above. These commitments and contingent obligations are subject to the Group and Bank's normal credit approval processes.

Commitments

Commitments to lend – under a loan commitment the Bank agrees to make funds available to a client 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 and unutilised overdraft facilities.

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

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

Additional contingent liabilities arise in the normal course of the Bank's business, associated with ongoing legal, regulatory or tax situations at both individual client and Bank levels. These situations are monitored by management and where it is possible to quantify reliably, provisions are booked. However given uncertainties such as establishing detailed fact patterns, legal status and regulatory status, in certain cases this is not feasible until further investigation has been conducted. In relation to such matters, looking at the range of potential outcomes, it is not anticipated that any material loss will arise from these transactions.

Litigation

As a participant in the financial services industry, the Group operates in a highly regulated environment. At any moment in time it is likely that the Group will be involved in a number of investigations and disputes. Such matters are subject to many uncertainties and their outcome is often difficult to predict, particularly in the early stages. The directors of the Bank have reviewed these actual, threatened and known potential claims and proceedings and, after consulting with the relevant legal advisers are satisfied that the outcome of these claims and proceedings will not have a material adverse effect on the Group's consolidated net assets, results of operations or cash flows.

The Group records a provision for a liability in relation to such matters when it is probable that an outflow of economic benefits will be required to settle an obligation resulting from past events, and a reliable estimate can be made of the amount of the obligation.

In many proceedings and investigations, it is not possible to determine whether any loss is probable or to estimate reliably the amount of any loss, either as a direct consequence of the proceedings and investigations or as a result of adverse impacts or restrictions on the Group's reputation, business and operations.

Numerous legal and factual issues may need to be resolved, including through potentially lengthy discovery and document production exercises and determination of important factual matters, and by addressing novel or unsettled legal questions relevant to the proceedings in question, before a liability can reasonably be estimated for any claim. The Group cannot predict if, how, or when such claims will be resolved or what the eventual settlement, damages, fine, penalty or other relief, if any, may be, particularly for claims that are at an early stage in their development or where claimants seek substantial or indeterminate damages.

There are situations where the Group may pursue an approach that in some instances leads to a settlement agreement. This may occur in order to avoid the expense, management distraction or reputational implications of continuing to contest liability, or in order to take account of the risks inherent in defending claims or investigations even for those matters for which the Group believes it has credible defences and should prevail on the merits. The uncertainties inherent in all such matters affect the amount and timing of any potential outflows, both for matters in relation to which a provision has been established and for other contingent liabilities.

The future outflow of resources in respect of any matter may ultimately prove to be substantially greater than or less than the aggregate provision that the Group has recognised. Where (and as far as) liability cannot be reasonably estimated, no provision has been recognised.

Included in other provisions is £10 million charged in the year for conduct and litigation matters (2018 - £4 million). The Group generally does not disclose information about the establishment or existence of a provision for a particular matter where disclosure of the information can be expected to prejudice seriously the Group's position in the matter.

The Financial Services Compensation Scheme

The Financial Services Compensation Scheme (FSCS), the UK's statutory fund of last resort for clients of authorised financial services firms, pays compensation if a firm is unable to meet its obligations. The FSCS funds compensation for clients by raising management expenses levies and compensation levies on the industry. In relation to protected deposits, each deposit-taking institution contributes towards these levies in proportion to their share of total protected deposits on 31 December of the year preceding the scheme year (which runs from 1 April to 31 March), subject to annual maxima set by the FCA (Financial Conduct Authority). In addition, the FSCS has the power to raise levies on a firm that has ceased to participate in the scheme and is in the process of ceasing to be authorised for the costs that it would have been liable to pay had the FSCS made a levy in the financial year it ceased to be a participant in the scheme.

20. Memorandum items continued

Capital Support Deed

The Bank, together with other subsidiaries of NWH, is party to a Capital Support Deed ("CSD"). Under the terms of the CSD, the Bank may be legally required 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.

21. Analysis of changes in financing during the year

	Group					
	Share capital		Capital contribution reserve		Subordinated liabilities	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
At 1 January	241	206	339	275	315	220
Additional Tier 1 capital notes issued	-	35	-	-	-	-
Arising on business transfers during the year	-	-	-	64	-	-
Issue of subordinated liabilities	-	-	-	-	-	95
Transfer to debt securities in issue	-	-	-	-	(50)	-
At 31 December	241	241	339	339	265	315

	Bank					
	Share capital		Capital contribution reserve		Subordinated liabilities	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
At 1 January	241	206	382	275	315	220
Additional Tier 1 capital notes issued	-	35	-	-	-	-
Arising on business transfers during the year	-	-	-	107	-	-
Issue of subordinated liabilities	-	-	-	-	-	95
Transfer to debt securities in issue	-	-	-	-	(50)	-
At 31 December	241	241	382	382	265	315

22. Analysis of cash and cash equivalents

	Group		Bank	
	2019 £m	2018 £m	2019 £m	2018 £m
At 1 January				
- cash	2	3	2	3
- cash equivalents	10,819	10,613	10,781	10,609
	10,821	10,616	10,783	10,612
Net cash (outflow)/inflow	(1,671)	96	(1,662)	62
Effect of exchange rate changes on cash and cash equivalents	82	109	82	109
At 31 December	9,232	10,821	9,203	10,783
Comprising:				
Cash and balances at central bank	3	2	3	2
Net loans to banks	9,229	10,819	9,200	10,781
Cash and cash equivalents	9,232	10,821	9,203	10,783

23. Related parties

UK Government

The UK Government through HM Treasury is the ultimate controlling party of The Royal Bank of Scotland Group plc. Its shareholding is managed by UK Government Investments Limited, a company it wholly-owns and as a result, the UK Government and UK Government controlled bodies are related parties of the Bank.

Transactions between the Bank, the UK Government and UK Government controlled bodies, consisted of Corporation Tax and Value Added Tax.

The Group may participate in a number of schemes operated by the Bank of England in the normal course of business. Members of the Group that are UK authorised institutions are required to maintain non-interest bearing (cash ratio) deposits with the Bank of England amounting to 0.324% of their average eligible liabilities in excess of £600 million. They also have access to Bank of England reserve accounts: sterling current accounts that earn interest at the Bank of England Rate.

Group undertakings

The Group's ultimate holding company is The Royal Bank of Scotland Group plc, registered in Scotland, and its immediate parent company is National Westminster Bank Plc, registered in England and Wales. Both companies are incorporated in Great Britain.

As at 31 December 2019, The Royal Bank of Scotland Group plc heads the largest group in which the Group is consolidated, and National Westminster Bank Plc heads the smallest group in which the Group is consolidated. Copies of the consolidated financial statements of both companies may be obtained from The Company Secretary, The Royal Bank of Scotland Group plc, Gogarburn, PO Box 1000, Edinburgh EH12 1HQ.

(a) Directors and key management

For the purposes of IAS 24 'Related Party Disclosure', key management comprise directors of the Bank and members of the Executive Committee. The following amounts are attributable, in aggregate, to key management:

	2019 £m	2018 £m
Interest receivable	-	-

Key management have banking relationships with Group entities which are entered into in the normal course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with other persons of a similar standing or, where applicable, with other colleagues. These transactions did not involve more than the normal risk of repayment or present other unfavourable features.

(b) Compensation of directors and key management

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

	2019 £m	2018 £m
Short term benefits	4	4
Post-employment benefits	1	1
Long term benefits(1)	2	2
	7	7

Note:
(1) Long term benefits consist of Long Term Incentive Plans (LTIPs) and deferred pay awards.

23. Related parties continued

(c) Related party transactions

The table below discloses transactions between the Bank and Group and other RBS Group companies.

	Group	
	2019	2018
	£m	£m
Fees and commissions payable	18	23

	Bank	
	2019	2018
	£m	£m
Interest receivable	199	159
Interest payable	65	50
Fees and commissions receivable	27	13
Fees and commissions payable	18	22
Dividends receivable	59	75

At the balance sheet dates, the following balances were held with related parties:

	Group		Bank	
	2019	2018	2019	2018
	£m	£m	£m	£m
Assets				
Loans to customers:				
Parent companies(1)	18,690	20,238	18,676	20,204
Amount due from subsidiary company	-	-	573	920
Derivatives:				
Parent companies	2	3	2	3
Total assets	18,692	20,241	19,251	21,127
Liabilities				
Bank deposits:				
Parent companies(1)	5,463	5,944	5,463	5,944
Subordinated loans:				
Parent companies	265	315	265	315
Debt securities in issue:				
Parent companies	310	-	310	-
Derivatives:				
Parent companies	19	17	19	17
Total liabilities	6,057	6,276	6,057	6,276

Note:
(1) £1.9 billion of short dated intercompany assets and liabilities, which meet the IAS 32 criteria, have been netted in 2019. The 2018 balances of £1.8 billion have been presented gross.

Operating expenses includes management recharge of £174 million (2018 - £157 million) from other entities with the RBS Group. Included in the management recharge are payments of non cancellable operating leases and pension costs.

In December 2018, the Bank sold financial investments totalling £23 million to RBS HG (UK) Ltd. No gain or loss was recognised on the sale.

24. Transactions with directors

At 31 December 2019, amounts outstanding in relation to transactions, arrangements and agreements entered into by authorised institutions across the Group, are shown in the table below.

	2019		2018	
	Aggregate amount outstanding £m	Number of persons	Aggregate amount outstanding £m	Number of persons
Directors:				
Loans to customers	-	4	-	4
Customer deposits	4	5	1	5
Officers:				
Loans to customers	-	6	-	6
Customer deposits	1	7	-	7

Key management have banking relationships with Group entities which are entered into in the normal course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with other persons of a similar standing or, where applicable, with other colleagues. These transactions did not involve more than the normal risk of repayment or present other unfavourable features.

25. Post balance sheet events

There have been no other significant events between 31 December 2019 and the date of approval of these accounts which would require a change to or additional disclosure in the financial statements.

The directors considers the coronavirus outbreak, noted on page 3, to be a non-adjusting post balance sheet event.