The following are the "*Risk Factors*" referred to in the Bank's interim results for the six months ended 30 June 2017, being the risks and uncertainties which are considered by the Bank to be material to it. These are an extract from the Shareholder and Members' Scheme Circular dated 28 July 2017. The meanings of relevant defined terms are set out in the Annex to this document.

RISK FACTORS

Shareholders should carefully consider the factors and risks associated with the Restructuring and Recapitalisation, the Bank's business and strategy and the financial services industry in the United Kingdom in which the Bank operates, together with all the other information contained in this Circular and all information referred to in this Circular, including, in particular, the risks and uncertainties described below. Subordinated Noteholders wishing to understand the risks associated with the Consent Solicitation should refer to the Consent Solicitation Memorandum which describes those risks. Scheme Creditors wishing to understand the risks associated with the Creditors' Scheme should refer to the Creditors' Scheme Circular.

This section describes the risk factors which are considered by the Bank to be material to it and the decision of the Shareholders as to how to vote in relation to the Resolutions and the Members' Scheme and/or whether to make any investment in the A Shares pursuant to the Members' Equity Subscription. However, these risk factors should not be regarded as a complete and exhaustive statement or explanation of all potential risks and uncertainties which Shareholders may face when making a decision with respect to how to vote in relation to the Resolutions and the Members' Scheme and/or whether to make any investment in the A Shares pursuant to the Members' Equity Subscription and should be used as guidance only. There may be other risks and uncertainties which are currently not known to the Bank or which the Bank currently does not consider to be material. Should any of the risks described below, or any other risks or uncertainties occur, this could, individually or cumulatively, have a material adverse effect on the Bank's or, following completion of the Restructuring and Recapitalisation, Holdco's business, operating results, financial condition and/or prospects, including its ability to meet regulatory threshold conditions which, in turn, would be likely to cause the price of the Ordinary Shares or, following completion of the Restructuring and Recapitalisation, the A Shares to decline and, as a result, a Shareholder could lose some or all of the value of its investment. Shareholders should consider the Resolutions and the terms of the Members' Scheme carefully and whether or not to vote in favour of them in light of the information contained in this Circular, and their personal circumstances.

This section of the Circular is divided into three main sections: "Risks relating to the Restructuring and Recapitalisation"; "Risks relating to the Bank and its Business"; and "Risks relating to the A Shares and the B Shares".

Risks relating to the Restructuring and Recapitalisation

1. ***The implementation of the Restructuring and Recapitalisation faces a number of significant risks and relies on the Members' Scheme (including the Members' Equity Subscription) and the Creditors' Scheme (including the Scheme Creditors' Equity Subscription) and the Consent Solicitation being executed successfully and the Resolutions being passed. If the Restructuring and Recapitalisation does not succeed, the Bank believes the most likely outcome is that the Ordinary Shares and the Subordinated Notes will be subjected to a mandatory write-down, either as a preliminary step to, or in the course of the Bank's entry into, Special Resolution. In such a scenario, the Bank believes that Shareholders will receive no recovery in respect of the Ordinary Shares that they hold, and that Subordinated Noteholders will receive no recovery in respect of the Subordinated Notes that they hold.***

   The Bank's going concern status

   The auditor's reports contained in the Bank's financial statements for the three years ended 31 December 2014, 2015 and 2016 each contain an "emphasis of matter" in relation to the Bank's ability to continue as a "going concern", indicating that there are material uncertainties which may cast significant doubt on the Bank's ability to continue as a going concern. The going concern status of the Bank depends on the Bank successfully implementing the Plan and, where applicable, the May 2017 Outlook on the Plan, including the implementation of the Restructuring and Recapitalisation, which remains subject to the risks described in this Part 3, and may be subject to any enforcement action the Authorities may take in relation to any inability of the Bank to meet regulatory requirements relating to its credit risk modelling under the CRR, its ICG, its Combined Buffer, its PRA Buffer and its MREL. There is a risk that the Authorities may exercise their discretion and take enforcement action against the Bank at any time. In accordance with CRD IV, the Authorities must require the Bank to take the necessary measures at an early stage to address relevant problems where the Bank does not meet the requirements of CRD IV or the Authorities have evidence that the Bank is likely to breach the requirements of CRD IV within the following 12 months. If the Bank were to be unable to continue as a going concern, it is likely that the conditions for implementation of the Special Resolution Regime in respect of the Bank, which include, amongst other things, the condition that the Bank is "failing or likely to fail", would be met and that the Bank of England or HM Treasury would exercise their powers under the Banking Act to resolve the Bank. See the section entitled "*Resolution procedure under the Banking Act*" below for further information.

See paragraph 4 of Section A of Part 1 of this Circular for a description of the background to the Restructuring and Recapitalisation.

Overview of the principal risks to the implementation of the Restructuring and Recapitalisation

Implementation of the Restructuring and Recapitalisation in full relies on the Members' Scheme (including the Members' Equity Subscription), the Creditors' Scheme (including the Scheme Creditors' Equity Subscription) and the Consent Solicitation being executed successfully in accordance with their respective terms. Furthermore, the Restructuring and Recapitalisation is conditional on the passing of the Resolutions. The principal risks to the successful implementation of the Restructuring and Recapitalisation are the risks of:

(a) a failure of any Consenting Holder to fulfil its obligations under the Lock-Up Agreement to vote in favour of (where applicable): (i) the Resolutions; (ii) the Members' Scheme; (iii) the Creditors' Scheme; and (iv) the 2023 Noteholder Extraordinary Resolutions;

(b) the Lock-Up Agreement terminating in accordance with its terms or being terminated by one or more of the parties thereto pursuant to a Lock-Up Termination Event (as defined in Part 19 of this Circular) in each case prior to Completion. See paragraph 17.13 of Part 16 of this Circular for a description of the Lock-Up Agreement and the Lock-Up Termination Events;

(c) a failure of any Backstop Provider to fulfil its obligations under the Backstop Agreement to subscribe and pay for any Subscription Shares not subscribed and paid for pursuant to the Equity Subscriptions in the proportion of their Final Backstop Commitments;

(d) the Backstop Agreement terminating in accordance with its terms. See paragraph 17.19 of Part 16 of this Circular for a description of the Backstop Agreement;

(e) the Members' Scheme not being approved by a majority in number, representing not less than 75 per cent. in value, of those Shareholders present and voting, either in person or by proxy, at the Members' Scheme Court Meeting;

(f) the Creditors' Scheme not being approved by a majority in number, representing not less than 75 per cent. in value, of those Scheme Creditors present and voting, either in person or by proxy, at the Creditors' Scheme Court Meeting;

(g) the Members' Scheme not being sanctioned by the Court;

(h) the Creditors' Scheme not being sanctioned by the Court;

(i) the Resolutions (or any of them) not being passed by the Shareholders at the General Meeting;

(j) the 2023 Noteholder Extraordinary Resolutions not being passed by Eligible 2023 Noteholders at the 2023 Noteholder Meeting;

(k) not obtaining approval by either or both the PRA or FCA (if required) pursuant to Part XIII of FSMA for the Principal Investors (as applicable) and Holdco to become controllers of the Bank;

(l) a rejection by the PRA of a request for approval pursuant to Article 26(3) of the CRR for Holdco to classify the A Shares as CET1 instruments;

(m) a rejection by the PRA of a request for permission under article 77 of the CRR to permit the cancellation by Holdco of the Subordinated Notes held by Holdco following the Notes Exchange; and

(n) the Bank becoming involved in disputes and legal proceedings in respect of the Restructuring and Recapitalisation. Such disputes or proceedings could be brought or raised during the implementation of the Restructuring and Recapitalisation with the objective of preventing the implementation of all or part of the Restructuring and Recapitalisation and/or could be brought after the Restructuring and Recapitalisation has been implemented with the objective of seeking a declaration that all or part of the Restructuring and Recapitalisation was unlawful and invalid. Further information on the risk of litigation is contained in the risk factor entitled "*Litigation seeking to challenge the implementation of the Restructuring and Recapitalisation or certain aspects of it could materially impact or prevent the successful implementation of the Restructuring and Recapitalisation or result in all or part of the Restructuring and Recapitalisation being declared to be unlawful and invalid retrospectively*" below.

There is a risk that the requisite conditions of the Restructuring and Recapitalisation will not be satisfied in the expected time frame or at all. For instance, implementation of the Members' Scheme and the Creditors' Scheme are each conditional upon, amongst other things, sanction by the Court. It is possible that such sanction will be given only subject to conditions or could be refused. There is also a risk that the timetable for implementing the Restructuring and Recapitalisation may be delayed for a variety of reasons, including decisions of the Court, the need to give Shareholders and Subordinated Noteholders appropriate time to consider any significant new information that may be announced by the Bank after the date of this Circular (whether as a result of the publication of the Bank's interim results for the six months ended 30 June 2017, or unexpected intervening events or developments), regulatory or third party intervention.

Delay in completing the Restructuring and Recapitalisation for whatever reason: (i) will prolong the period of uncertainty for the Bank and may result in the accrual of additional costs (for example, there may be an increase in costs in relation to the preparation and issue of documentation, or other elements of the planning and implementation of the Restructuring and Recapitalisation) without any of the potential benefits of the Restructuring and Recapitalisation having been achieved; or (ii) may result in the failure of the Restructuring and Recapitalisation as a result of the Authorities taking enforcement action against the Bank as a result of its non-compliance with certain capital and regulatory requirements or the failure to satisfy a condition to the Restructuring and Recapitalisation or otherwise. Consequences of a failure of the Restructuring and Recapitalisation are detailed below.

Consequences of a failure of the Restructuring and Recapitalisation

Having concluded the FSP, the Bank does not currently believe that there is any realistic alternative to raising the required additional capital if the Restructuring and Recapitalisation is unsuccessful. The failure of the Restructuring and Recapitalisation would have a direct and material adverse effect on the Bank's ability to comply with its current and future regulatory capital requirements, loss-absorbing capacity and liquidity requirements.

If the Restructuring and Recapitalisation is not implemented, the Bank would expect to hold urgent discussions with the PRA and the Bank of England. It is not possible to be certain what the outcome of those discussions may be, nor the extent to which the Authorities would impose on the Bank requirements in respect of the Bank's non-compliance with requirements relating to its credit risk modelling under the CRR, its ICG, its Combined Buffer, its PRA Buffer and its MREL. It is not possible to be certain as to what actions the Bank of England and/or other Authorities would take in these circumstances, as they are afforded a wide degree of discretion.

The Authorities (between them) would have a wide range of measures available to them, including:

- agreeing a revised plan, or requiring the Bank to take other specified actions;
- varying or restricting the Bank's permissions or business;
- as a precursor to placing the Bank within the Special Resolution Regime, or as a standalone tool, using the mandatory write-down tool to write-down, cancel, or transfer some or all of the Bank's capital instruments, which could include the Ordinary Shares and the Subordinated Notes; and
- placing the Bank into the Special Resolution Regime under the Banking Act.

The Bank is aware that the Bank of England has already commenced preparatory steps in order to enable it to use the mandatory write-down tool, and if thought fit, subsequently or at the same time, to resolve the Bank pursuant to the Special Resolution Regime, shortly following a failure successfully to implement the Restructuring and Recapitalisation. If the Bank of England exercises its powers under the Banking Act or there is continuing press and/or market speculation regarding the occurrence of such an event, it is highly probable that the Bank would be materially adversely affected.

The Bank believes that, if the Restructuring and Recapitalisation is not successfully implemented, the most likely outcome is that the Ordinary Shares and the Subordinated Notes will be subjected to a mandatory write-down, either as a preliminary step to, or in the course of the Bank's entry into, Special Resolution. In such a scenario, the Bank believes that Shareholders will receive no recovery in respect of the Ordinary Shares that they hold, and that Subordinated Noteholders will receive no recovery in respect of the Subordinated Notes that they hold.

Additionally, absent the successful implementation of the Restructuring and Recapitalisation, in a Working Capital Stress Scenario, the Bank would not have enough CET1 capital to meet its minimum Pillar 1 regulatory capital requirements over the Working Capital Period (as defined in Part 19 of this Circular). Were these events to occur, the Bank believes the above described outcome and consequences would arise for Shareholders and Subordinated Noteholders. See paragraph 2.16 of Part 7 of this Circular for a description of the Working Capital Stress Scenario and the Bank's working capital position over the Working Capital Period.

For further information on the consequences for Shareholders and Subordinated Noteholders of a resolution of the Bank, see Section B of Part 1 of this Circular.

Resolution procedure under the Banking Act

The Banking Act empowers the Resolution Authorities, where certain conditions are met (the threshold condition being that the Bank is "failing or is likely to fail" – see paragraph 4 of Section B of Part 1 of this Circular, and paragraph 2.8 of Part 11 of this Circular) to impose the special resolution regime ("**Special Resolution Regime**") on the Bank. As described in further detail in Part 11 of this Circular, the Special Resolution Regime consists of both Stabilisation Powers and modified insolvency proceedings, which could be imposed on the Bank.

If the Bank becomes subject to the Special Resolution Regime, Shareholders are likely to experience a cancellation of their holdings and Subordinated Noteholders are likely to experience the entire loss of their investment. The Banking Act requires the Bank of England permanently to write-down, or convert into equity, Tier 1 capital instruments and Tier 2 capital instruments at the point of non-viability of the Bank and before, or together with, the exercise of any stabilisation option (except in the case where the bail-in tool is to be utilised for other liabilities, in which case such capital instrument would be written down or converted into equity pursuant to the exercise of the general bail-in tool, as described above, rather than the mandatory write-down tool and conversion power applicable only to capital instruments) (the "**mandatory write-down**"). For the purposes of the application of such mandatory write-down and conversion power, the point of non-viability is the point at which the PRA determines that the bank is "failing or likely to fail" and the Bank of England determines that the Bank meets the conditions for resolution (but no resolution action has yet been taken), or that the relevant entity will no longer be viable unless the relevant capital instruments are written down or converted, or the Bank requires extraordinary public support without which the Bank of England determines the Bank would no longer be viable. An exercise of the mandatory write-down would be effected by the Bank of England as resolution authority with no need for Court approval, and a bail-in order cannot be challenged in Court (although it may be capable of challenge by judicial review if certain conditions are met). The Bank anticipates that any claims that Shareholders or Subordinated Noteholders may have which survive an exercise of the mandatory write-down would receive no recovery from the applicable Special Resolution procedure.

Certain of the Bank's creditors are entitled to protection from the FSCS. However, FSCS protection does not extend to the Subordinated Notes or the Ordinary Shares. For more information see paragraph 2.16 of Part 11 of this Circular.

For further information on the consequences for Shareholders and Subordinated Noteholders of a resolution of the Bank, see Section B of Part 1 of this Circular.

2. ***Litigation seeking to challenge the implementation of the Restructuring and Recapitalisation or certain aspects of it could materially impact or prevent the successful implementation of the Restructuring and Recapitalisation or result in all or part of the Restructuring and Recapitalisation being declared to be unlawful and invalid retrospectively.***

Litigation seeking to challenge the implementation of the Restructuring and Recapitalisation

Previous liability management exercises and recapitalisations by other institutions in distress have demonstrated that there are people who may seek to bring claims or raise arguments in Court to stop or delay the Restructuring and Recapitalisation or challenge its legitimacy or fairness. There is, therefore, a risk that the Bank may become involved in disputes and legal proceedings in connection with the Restructuring and Recapitalisation and the likelihood of their occurrence or their outcome, cannot be predicted in advance with any certainty. It is possible that Shareholders, Noteholders or other parties may seek to bring claims or raise arguments in Court with the objective of preventing or delaying the implementation of all or part of the Restructuring and Recapitalisation.

In particular, it is possible that Shareholders, Subordinated Noteholders or other parties may advance arguments seeking to challenge aspects of the Restructuring and Recapitalisation. The making of any of these types of arguments or claims could delay the implementation of the Restructuring and Recapitalisation (whether or not such arguments or claims have merit) which could result in the failure of the Restructuring and Recapitalisation.

Claims determined after the implementation of the Restructuring and Recapitalisation

Claims challenging elements of the Restructuring and Recapitalisation, or certain aspects thereof, may be brought after the Restructuring and Recapitalisation has been implemented. Other claims brought before such implementation may not be determined until after such implementation.

The success of these claims could result in all or part of the Restructuring and Recapitalisation being declared to be unlawful and invalid retrospectively. The consequences of such a finding would largely depend on the scope of the claims and the legal basis of the finding. Such finding could result in the reversal or invalidity of the Restructuring and Recapitalisation (or a part thereof) and the Bank failing to achieve a critical component of its strategy, the Plan and the May 2017 Outlook on the Plan. It is not known, in such circumstances, what steps the Bank or the Authorities would take, but there is a risk that the Bank could be the subject of a Special Resolution procedure under the Banking Act. If such a resolution procedure were to occur, the Directors believe that Shareholders and Subordinated Noteholders would receive no recovery in respect of the Ordinary Shares and Subordinated Notes that they respectively hold.

Other potential consequences of proceedings

The Bank may incur significant expense in connection with any such proceedings (whether seeking to challenge the implementation of the Restructuring and Recapitalisation or determined after the implementation of the Restructuring and Recapitalisation) even if such proceedings are ultimately concluded in favour of the Bank. The costs of pursuing or defending one or more proceedings, and the outcome of any such proceedings, could also expose the Bank to substantial monetary damage, other penalties and injunctive relief and/or have a negative effect on the Bank's reputation, any of which could reduce the CET1 capital generated by the Restructuring and Recapitalisation and could have an adverse impact on the Bank's ability to deliver its strategy, the Plan and, where applicable, the May 2017 Outlook on the Plan and on its operations, financial condition and prospects. An adverse decision in any one matter could lead to further claims against the Bank.

Risks relating to the Bank and its Business

Following completion of the Restructuring and Recapitalisation, Holdco and the Holdco Group will be exposed to the impact of any material adverse change in the business, results of operations, financial condition, or prospects of the Bank whether as a result of any of the risks relating to the Bank described below or otherwise. Furthermore, the risks below may equally apply directly to Holdco following completion of the Restructuring and Recapitalisation.

3. ***A failure successfully to implement or a delay in implementing the Plan and, where applicable, the May 2017 Outlook on the Plan, may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital resources and its ability to comply with its regulatory capital requirements.***

The Bank required a £1.5 billion recapitalisation in December 2013 and a capital raise of £400 million in May 2014, enabling the commencement of a turnaround plan. Although the Bank believes it has made significant progress in implementing its turnaround plan, the Bank's capacity to build its capital and meet the current and longer-term regulatory capital requirements and MREL required of all UK banks has been constrained by: (i) the impact of interest rates that are and have been lower than previously forecast, reducing the Bank's ability to generate income; and (ii) higher than anticipated transformation and conduct redress and remediation costs. To address these issues, as part of the Bank's annual review process relating to the 2016 financial year, and concluding its annual planning process, the Bank finalised the Plan to help it implement its strategy.

The Plan anticipates various important management actions, including, as an alternative to a sale of the Bank, implementing a liability management exercise and equity capital raise to generate £700 million to £750 million of incremental CET1 capital for the Bank to raise sufficient CET1 capital to increase the CET1 component of the Bank's headroom above its minimum Pillar 1 regulatory capital requirements. The Plan was based on a number of key assumptions, forecasts and targets relating to a variety of factors within and outside of the control of the Bank and the Bank's prospects of implementing its strategy are sensitive to those factors. Accordingly, it became necessary to reassess the achievability of the Plan, and to adjust its implementation, to reflect the Bank's view of the impact on the Plan of trading through the first five months of 2017, the prevailing business environment, the differences between the capital raising contemplated in the Plan and the Restructuring and Recapitalisation the Bank is now seeking to implement and discussions that the Bank has had with its regulators since the Plan was adopted (the result being the May 2017 Outlook on the Plan). On 27 June 2017, the PRA confirmed its acceptance of the May 2017 Outlook on the Plan, including the terms of the Restructuring and Recapitalisation. The PRA may, however, withdraw its acceptance of the Plan and/or the May 2017 Outlook on the Plan at any time, whether or not the Restructuring and Recapitalisation is successful. The PRA has notified the Bank that it intends to monitor closely the Bank's performance against the Plan and consequently, where applicable, the May 2017 Outlook on the Plan. There is a risk that the Bank will not successfully deliver all or part of the May 2017 Outlook on the Plan when planned or as targeted. Failure to successfully implement, or a delay in implementing, the May 2017 Outlook on the Plan may adversely affect the Bank's business, operating results, financial condition, prospects, regulatory capital resources and its ability to comply with its regulatory capital requirements.

Through the Restructuring and Recapitalisation, the Bank is seeking to generate approximately £700 million of incremental CET1 capital (depending on the actual amount of Retail Cash Consideration paid out by the Bank pursuant to the Mandatory Cancellation and excluding costs and expenses incurred by the Bank). Against the assumed liability management exercise and equity capital raise provided for in the Plan, the outcome of this change will be a net reduction in the amount of CET1 capital generated (assuming that the Restructuring and Recapitalisation is successfully completed) as the Plan assumed that the Bank would implement a liability management exercise and equity capital raise which would generate between £700 million and £750 million of incremental CET1 capital for the Bank.

The Plan, which relates to the period 2017 – 2021, is in the very early stages of implementation. Its performance and effectiveness are not yet proven and, as components of the Plan are implemented and executed, the Plan may require amendments or adaptations to reflect any necessary or consequential changes to its targets and precise scope to reflect more appropriate structures for achieving the aims and targets of the Plan. Indeed, since the Plan was approved by the Bank on 13 February 2017, there have been a number of developments affecting the Plan's forecasts and outlook (see paragraph 8.2 of Part 7 of this Circular for a description of the May 2017 Outlook on the Plan). Whilst the May 2017 Outlook on the Plan reflects these recent developments, the modelled impacts of such events and developments on the Plan may prove to be incorrect or inaccurate, particularly given that the governance around such modelling (including the level of testing and sensitivity analysis performed in relation to the impact of the May 2017 Outlook on the Plan) has not been as extensive as the annual strategic planning process which the Bank followed in preparing and approving the Plan, which could necessitate or result in further adjustments being made to the Plan and, where applicable, the May 2017 Outlook on the Plan in the future and/or resulting in the Bank not achieving the Bank's plans, targets, estimates or expectations contained in the Plan and/or the May 2017 Outlook on the Plan including those described in paragraph 9 of Part 7 of this Circular. Whether or not the Restructuring and Recapitalisation is successful, there is a risk that delivery by the Bank of the Plan and, where applicable, the May 2017 Outlook on the Plan, may be insufficient to address the Bank's requirements or deliver the projected benefits either because of factors beyond its control or internal factors relating to the Bank. The successful execution of the Bank's strategy, the Plan and, where applicable, the May 2017 Outlook on the Plan requires the simultaneous execution of a number of business strategies including increasing mortgage sales, preserving the Bank's market share in retail and SME banking, implementing significant cost reduction initiatives, management of capital resources and loss-absorbing capacity and the other risks and uncertainties faced by the Bank. Historically, including since its 2013 recapitalisation, the Bank's track record of successfully executing change and cost reduction initiatives as contemplated by its business plans is inconsistent and implementation of said plans have not always delivered certain of the planned benefits. Based on historical performance, there remains a significant risk that the Bank will be unable to meet its transformation, change and cost reduction initiatives as outlined in the Plan and, where applicable, the May 2017 Outlook on the Plan.

Whether or not the Restructuring and Recapitalisation is successful, any failure to implement successfully or a delay in implementing the Plan and, where applicable, the May 2017 Outlook on the Plan could have a material adverse effect on the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements, which could also result in the Authorities taking enforcement action against the Bank in relation to any inability of the Bank to comply with its requirements under CRR in relation to credit risk modelling, its ICG, its Combined Buffer, its PRA Buffer and its MREL. For further information, see the risk factor entitled "*Irrespective of the successful implementation of the Restructuring and Recapitalisation, the Bank will not be compliant with its regulatory capital and loss-absorbing capacity requirements and will be subject to any enforcement action the Authorities may take in respect of such non-compliance.*".

4. ***The Bank's ability to deliver its strategy and achieve the targets in the Plan and, where applicable, the May 2017 Outlook on the Plan is based on underlying assumptions that are subject to significant risks and uncertainties.***

The Plan and the May 2017 Outlook on the Plan each include key assumptions on which the proposed actions and targets contained therein are premised. If actual operating results differ from those targeted or the assumptions underlying the Plan and/or the May 2017 Outlook on the Plan prove to be incorrect or require change throughout the life of the Plan, the Bank may be unable to take management actions to address these differences effectively. There is a risk that the Bank will be unable to implement the Plan and, where applicable, the May 2017 Outlook on the Plan as described therein or as assumed or expected or at all. For example, since the Plan was approved on 13 February 2017, there have been significant developments that have affected the Bank's outlook for its business and the prospects of achieving some of the key components of the Plan (or the timing of when they are expected to be achieved). Accordingly, it became necessary to reassess the achievability of the Plan, and to adjust its implementation, to reflect the Bank's view of the impact on the Plan of trading through the first five months of 2017, the prevailing business environment, the differences between the capital raising contemplated in the Plan and the Restructuring and Recapitalisation the Bank is now seeking to implement and discussions that the Bank has had with its regulators since the Plan was adopted (the result being the May 2017 Outlook on the Plan). See paragraph 8.2 of Part 7 of this Circular for a description of the May 2017 Outlook on the Plan.

The forward-looking actions and targets in the Plan and the May 2017 Outlook on the Plan are not statements of historical fact nor are they guarantees of future performance. Rather, they are based on current management views and assumptions that involve known and unknown risks, uncertainties and other factors that are subject to change and which may cause the actual results, performance, achievements or developments of the Bank or the industry in which it operates to differ materially from any targeted future results, performance, achievements or developments expressed or implied from the forward-looking targets. The forward-looking targets of the Plan and the May 2017 Outlook on the Plan have not been subject to an audit by the Bank's accountants or any other professional advisers.

Risks relating to the Bank's ability to implement its strategy include:

- *The Bank's net interest margin target is predicated on assumed interest rate increases that are beyond the control of the Bank and the Bank's response to those increases in assets and liabilities pricing materialising as planned* – the Plan targets increases in the Bank's net interest margin of up to 10 basis points per annum, in line with the 10-day moving average of the market forward-looking implied rates to 22 November 2016 which assumed a Bank of England base rate increase to 0.5 per cent. in May 2018, a further increase to 0.75 per cent. in June 2019, a rise to 1.0 per cent. in August 2020 and a final rise to 1.25 per cent. in November 2021. These targets are most susceptible to interest rate changes and competitive pressures. "Lower for longer" interest rates (including the Bank of England base rate) will restrict the Bank's ability to increase net interest margin and, consequently, restrict organic capital generation and profitability, as well as improvement in the Bank's cost:income ratio (see the risk factor entitled "*The Bank's earnings, net interest margins and credit losses have been adversely affected by factors such as the low Bank of England base rate, and may continue to be adversely affected for so long as one or more of these factors persist*." for further details regarding factors affecting the Bank of England base rate). See paragraph 8.2 of Part 7 of this Circular for a description of how the more recent adverse base rate outlook impacts the Plan's forecasts and the base rate profile now assumed in the May 2017 Outlook on the Plan as a consequence. There is also a risk that base rates may not increase as soon or as much as the Bank has assumed, that competitive pressures, and the need to maintain market share to maintain viable market volumes, could reduce the Bank's market share or that regulatory pressures constrain the anticipated growth in the Bank's business volumes. The Plan assumes asset pricing increases across the market generally as a result of the "lower for longer" interest rate environment generating fewer available options for retail banks to deliver improved net interest margin. If, and to the extent that, these increases are not forthcoming as assumed in the Plan, the Bank's actual net interest margin trajectory could be significantly lower than targeted. Furthermore, there is a risk that a "lower for longer" base rate environment would lead to stagnant or decreasing yields on intra-bank swaps, which would not allow for increases in the Bank's net interest margins across fixed rate products as contemplated in the Plan.

- *The Bank may be unable to preserve its market share in new business mortgage assets or other products through the life of the Plan as assumed in the Plan* – the Plan assumes that the Bank's market share in new business mortgage assets is preserved, allowing the Bank to increase prime residential mortgage asset volumes, particularly in Platform over the life of the Plan, and that unsecured loan and credit card balances decrease from 2017. The personal financial services industry is mature, so growth often requires taking market share from competitors. The Bank risks losing market share to other banks, building societies, insurance company competitors and new "fin-tech" entrants, which may impact the Bank's plans to increase Bank profitability based on preserving its market share of new mortgage origination and other products over the life of the Plan. The Plan also assumes that mortgage margin improvements are driven by the Bank entering new markets or products or increasing the Bank's market share of certain types of products or services, an increase in customers with higher loan-to-income ("**LTI**") ratios, improvements in service offering, an uplift in the number of brokers used, the Bank starting to provide mortgages with up to 95 per cent. loan-to-value, an increase in new build market share through participation in the Government's Help to Buy Equity Loan scheme and the inclusion of personal income when assessing buy-to-let customers. The Plan assumes that the Bank will be able to improve its margin on variable rate savings products as the Bank of England base rate rises due to its assumed interest rate pass-back strategy. There is a risk that, if market forces determine that the timing and proportion of interest rates to be passed back to its customers is not feasible, the Bank may not be able to widen its net interest margin to the extent it has projected or at all. Furthermore, the pricing strategies of the Bank's competitors could directly impact the pricing of the Bank's products. Any resulting downward pricing pressure could result in the Bank not achieving its net interest margin growth targets. These risks may be increased if the Bank's cost saving initiatives result in a lack of ability of the Bank to make the investments necessary in its people, products or systems to preserve and improve its competitive position in an increasingly competitive market within prudent and appropriate risk appetites that do not expose the Bank to additional or new categories of conduct and legal risks.

- *The Bank may be unable to increase its mortgage assets* – the Plan targets growing the Bank's net core customer assets by approximately £1 billion in each year of the Plan from 2018, primarily driven by the Bank's Platform business. The Bank's ability to achieve these targets depends on improvements in its customer proposition and on the success of a limited number of intermediaries who also sell mortgages of the Bank's competitors. There is a risk that the Bank will not be adequately resourced or will not have sufficient expertise to deal with increased business volumes as a result of cost reduction initiatives or an inability to retain and/or attract employees necessary for the implementation of the Bank's strategy. There is also a risk that the growth of these assets will be significantly less than planned, and that mortgage retention and/or new mortgage origination may be significantly less than expected due to any number of internal or external factors. These factors include, for example, a possible contraction of the UK mortgage market, and/or the risk of the Bank being unable to support the underwriting process by improving its existing predictive credit modelling capability, and/or the risk that the Bank's relationships with one or more intermediaries may deteriorate for a variety of reasons, including competitive factors, and/or that the pressure to achieve the targeted increases may create new conduct, legal and regulatory risks.

- *The Bank may be unable to access liquidity and funding and/or adequately manage its liquidity position* – there is a risk that the Bank may be unable to maintain access at an appropriate cost to liquidity and funding to fund the requisite level of asset origination targeted in the Plan, including a risk that the Bank may be unable to gain access or unable to gain access on terms commercially acceptable to the Bank to current or future central bank funding facilities and initiatives which could impact the Bank's ability to implement its strategy. Insufficient funding may prevent the Bank from, for example, implementing product initiatives (including the launch of online mortgage switching functionality) and/or transformation programmes required to deliver its strategy. The Plan assumes certain retention and acquisition levels of core customer assets and liabilities, including anticipated wholesale funding issuances, all of which support the Bank's liquidity position. If the Bank cannot successfully attract or retain business, there is a risk that the Bank may suffer a constraint on liquidity and/or breach its regulatory minimum liquidity requirement. This risk could manifest itself as a result of the wholesale markets being inaccessible to the Bank, or as a deviation in its ability to originate and retain asset and liability balances consistent with the Plan. Whilst the Bank undertakes strategic transactions, such as the Restructuring and Recapitalisation, or during times of continued adverse press attention and speculation, the Bank's liquidity risk may significantly increase as a result of the difficulty in accurately modelling expected customer behaviour in these circumstances. Adverse and unexpected customer behaviour that the Bank is unable to manage could result in the withdrawal of material amounts of customer deposits which would adversely impact the Bank's liquidity position. See paragraph 8.2 of Part 7 of this Circular for a description of customer liabilities balance attrition over and above that expected in the Plan over the five months ended 31 May 2017 and its impact on the Plan's forecasts and outlook, as reflected in the May 2017 Outlook on the Plan. Furthermore, whilst the Bank may be able to manage its liquidity position in such circumstances to avoid a breach of regulatory minimum liquidity requirements through any or a combination of options, or by increasing wholesale funding activity, significant levels of customer withdrawals would be likely to adversely affect its net interest income and/or balance sheet growth and, ultimately, the Bank's ability to deliver its strategy.

- *Actual losses on asset sales may be greater than assumed in the May 2017 Outlook on the Plan* – the Plan assumes reduced losses on the sales and de-leverage of the Bank's non-core corporate assets (these assets are inconsistent with the Bank's current business strategy and risk appetite (known as the "**Legacy Portfolio**")) in 2017 and no further material losses on other asset sales. The May 2017 Outlook on the Plan assumes a further reduction in the Bank's RWAs resulting from an expected reduction in Optimum assets through securitisations and/or whole-loan sales. See paragraph 8.2 of Part 7 of this Circular for a description of such transaction's estimated impact on the Plan's forecasts and outlook, as reflected in the May 2017 Outlook on the Plan, if it is completed on acceptable terms when proposed. There is a risk that this anticipated de-leverage of the Optimum portfolio and any remaining asset disposals or securitisations of the Legacy Portfolio may not be completed on acceptable terms, or at all, or may result in unprovided losses or lower de-leverage than planned.

- *Non-interest income may continue to decrease* – the Bank's non-interest income has decreased in recent years to £66.7 million in the year ended 31 December 2016, principally as a result of the reduction in the Bank's ATM network and lower rates on merchant interchange. The May 2017 Outlook on the Plan assumes a decrease in non-interest income to approximately £50 million for 2017, following which it assumes non-interest income remaining broadly stable at approximately £40 million per annum over the life of the Plan. These targets are based in part on assumed increases in fees relating to transactions on business and commercial banking ("**BaCB**") current accounts and increased non-interest income, primarily from the commission from general insurance referrals. Changes in the fees charged to BaCB customers could result in higher than anticipated outflows of customer deposits and the need for the Bank to replace these outflows with more expensive funding sources, further decreasing net interest income more than assumed in the Plan and/or resulting in lower than expected overall non-interest income. Furthermore, any increases made to the fees the Bank charges could expose the Bank to greater competition risks if similar products are offered at lower fees by the Bank's competitors and any proposed regulatory changes; for example, the Second Payment Services Directive ("**PSD2**") could result in a reduction in interchange income the Bank receives. There is also a risk that, if the Bank does not deliver the required number of general insurance referrals, it may not receive the level of commission it has forecast, which could impact the Bank's ability to achieve its non-interest income targets. Following the launch of the ability for customers to opt-into "Everyday Rewards" (being the Bank's scheme which rewards customers for everyday banking) via online banking at the start of April 2017, there is also a risk that a greater number of customers than assumed in the Plan will opt-into this scheme, which could adversely impact the Bank's non-interest income.

- *Transformation programmes may cost more than expected, take longer, or deliver less benefit than planned* – the May 2017 Outlook on the Plan assumes the Bank is able to deliver the remaining transformation programme without material deviation from planned timescales and cost. The May 2017 Outlook on the Plan also assumes no other or new significant strategic or remediation transformation programmes are needed in the remaining years of the Plan. The Bank is targeting a reduction in project costs to approximately £100 million for the year ending 31 December 2017 (year ended 31 December 2016: £310 million), and an increase to approximately £120 million of project costs in 2018, and thereafter project costs of approximately £50 million per annum over the remaining life of the Plan, which represents a significant reduction compared to the Bank's project costs of recent years. See paragraph 8.2 of Part 7 of this Circular for a description of the May 2017 Outlook on the Plan's re-phasing of project costs between 2017, 2018 and 2019. Historically, the Bank has experienced significant cost overruns when implementing complex large-scale transformation projects, and some projects have not delivered the planned benefits or the benefits delivered have been reduced in scope or delayed. Any deficiencies in project scoping, appropriate governance and related programme management processes to assist with the satisfactory delivery of these activities would have an adverse effect on the Bank's operating results and financial condition compared with those targeted in the May 2017 Outlook on the Plan. There are risks that the Bank may be unable to complete its transformation programmes when planned, that there may be a requirement to upgrade the Bank's systems, infrastructure, processes and controls, and that the programmes as a whole may cost significantly more than targeted or have a reduced scope for the same targeted costs, or deliver less benefit than planned, thereby impacting associated cost reductions or income-generation plans assumed in the May 2017 Outlook on the Plan. The Bank has a number of initiatives in the May 2017 Outlook on the Plan for 2017 to 2019 that support regulatory and mandatory requirements. The majority of these are still in their infancy and more detailed plans and costs are being developed. As the costs are better understood, there is a risk that the restricted budgets that have been agreed are not sufficient to complete these initiatives. In addition, known issues requiring remediation or new transformation programmes may require substantially greater resources than anticipated and new issues requiring remediation or transformation programmes may require substantial resources not anticipated in the May 2017 Outlook on the Plan.

- *Reducing cost base and impact on the Bank's cost:income ratio* – the Bank's high cost:income ratio as at 31 December 2016 inhibits the Bank's profitability and may hinder its ability to generate new capital and may be commercially unsustainable. The Plan, therefore, targets a reduction in operating costs from £445 million in the year ended 31 December 2016 to approximately £410 million in the year ending 31 December 2017, further reducing to a long-term target annual operating costs run rate of approximately £350 million per annum from the end of 2018 onwards (which corresponds to an approximately 21 per cent. reduction from the Bank's operating costs in 2016). These operating cost reduction targets assume that the Bank successfully implements significant cost reduction initiatives in the near-term, and that operating expenditure and operating project costs are significantly lower from 2019 onwards to the end of the life of the Plan than in recent years. The PRA has stated that, as a condition of the PRA's acceptance of the May 2017 Outlook on the Plan, the PRA expects, by the time of the Bank adopting its next five-year strategic plan, that the Bank will provide to the PRA a detailed cost:income strategy setting out how the Bank will achieve in the medium-term a competitive cost:income ratio in line with the Bank's peer group. Furthermore, the PRA has also stated its view that such a cost:income strategy will be critical to ensuring the success of the Plan and the future of the Bank. There is a risk that if the Bank does not deliver its cost reduction initiatives and/or does not grow its net interest margin in line with its targets, its costs relative to income will not decrease, which will continue to negatively impact its profitability and capital position. Furthermore, the implementation of significant cost reduction initiatives, for example branch closures, reductions in full time equivalent ("**FTE**") numbers, changes to third-party supplier arrangements, the reorientation of the Bank's distribution channels and simplification of the Bank's product offering, may not achieve the targeted cost savings and, instead, may impede the Bank from preserving its market share and expose the Bank to competitive pressure from competitors investing in their product offerings and/or expose the Bank to additional or new conduct and legal risks and furthermore may limit the Bank's ability to deliver growth in its core customer asset base and mortgage asset volumes as assumed in the Plan.

- *Conduct and legal risk provisions may need to be increased* – in the three years ended 31 December 2016, the Bank incurred total new conduct risk charges of £319 million. This takes the total level of provision since the start of the Bank's remediation programme in 2011 to just under £1 billion. Since 2011, approximately £800 million of this provision has been utilised, leaving remaining provisions of £169.3 million at the end of 2016. The Plan assumes: (i) no new categories of conduct and legal risk provisions; and (ii) no material increases in provisions for existing categories of conduct and legal risk, charged during the life of the Plan. Conduct and legal risk provisions as at 31 December 2016 did not take into account any issues incurred but not yet identified ("**IBNI**"), for which the Bank held a separate provision of £8.1 million as at 31 December 2016. There is a risk that the Bank becomes exposed to significant new conduct or legal risks, either as a result of the Bank discovering new categories of conduct and legal risk issues (for example, from the Bank's legacy or new systems and controls, product design and implementation, mis-selling mortgages and other products, or from increasing certain types of products or lending, or the pressures to increase the Bank's new customer assets to meet the Bank's targets, or from regulatory changes imposed on banks generally or on the Bank specifically). Furthermore, there is a risk that the current level of provision held for both redress amounts and associated costs is not deemed adequate in the future. Conduct provisions for payment protection insurance ("**PPI**") and other known issues, as well as new categories of conduct and legal risk issues that may emerge during the life of the Plan, including as a result of ongoing remediation work which could lead to the identification of new conduct issues, and related remediation and project costs, may be much higher than expected over the life of the Plan. Each element of the conduct and legal risk provision is reviewed regularly and will continue to be on an ongoing basis over the life of the Plan. As a result of such a review, the Bank assumed in the May 2017 Outlook on the Plan a potential net incremental additional conduct risk charge of approximately £5 million in 2017 (subject to further external and internal review and approval) driven by an increase of £9 million relating to PPI and the requirements of the FCA's policy statement 17/3 offset in part by small provision releases from other conduct risk categories. For further information, see paragraph 8.2 of Part 7 of this Circular.

- *The Bank may not achieve its assumed level of RWAs which could result in the Bank having greater minimum Pillar 1 regulatory capital requirements than anticipated* – the May 2017 Outlook on the Plan assumes RWAs falling to approximately £5.5 billion by the end of 2017 and thereafter RWAs reducing to between approximately £5.0 billion and £5.5 billion in the final years of the Plan. The Bank currently holds IRB status for its RWA modelling, but is presently undertaking a remediation plan to deal with its non-compliance with CRR relating to its credit risk modelling. A failure to address CRR non-compliance by the end of 2017 (or at all) could potentially result in further regulatory action such that the Bank's permission to use an IRB Approach could be removed, resulting in the Bank being required to use a standardised approach to modelling credit risk. This could, among other consequences, expose the Bank to a material increase in the calculation of RWAs which could lead to the Bank not achieving its assumed level of RWAs and requiring the Bank to hold additional regulatory capital. RWAs may be significantly greater than assumed due to deteriorating economic conditions (for example, higher unemployment and lower property prices could result in higher levels of impairments) and any material increases in RWAs will significantly increase the Bank's minimum Pillar 1 regulatory capital requirements beyond those planned for. The Bank's RWAs assumptions are predicated on further de-leverage of the Legacy Portfolio resulting in the losses assumed in the May 2017 Outlook on the Plan. If this de-leverage of the Legacy Portfolio is unsuccessful, RWAs could remain higher than those assumed in the May 2017 Outlook on the Plan, resulting in greater regulatory capital requirements than anticipated and lower CET1 capital ratios than targeted. Furthermore, there remain continued challenges and uncertainty for the UK economy, rising levels of personal debt and the impacts of rising interest rates on customers' abilities to meet their repayments. These pressures could lead to an increase in arrears in the Bank's residential lending portfolios, including Optimum, and an associated increase in retail impairment provisions. See paragraph 8.2 of Part 7 of this Circular for a description of the May 2017 Outlook on the Plan's assumed reduction in the Bank's RWAs resulting from an expected reduction in Optimum assets through securitisations and/or whole-loan sales and the regulatory call of Calico and their estimated impact on the Plan's forecasts and outlook, as reflected in the May 2017 Outlook on the Plan, if completed on acceptable terms when contemplated.

- *The Bank may be unable to complete other capital markets issuances required to meet regulatory capital requirements and MREL compliance (in addition to the Restructuring and Recapitalisation)* – a critical component of the Bank's strategy and the PRA's acceptance of the May 2017 Outlook on the Plan, including the Restructuring and Recapitalisation, is further capital issuances starting with an approximately £250 million Tier 2 debt issuance in 2018. In addition, the May 2017 Outlook on the Plan assumes that the Bank will complete further MREL-qualifying debt issuances in 2020 and 2021, of £200 million and £300 million, respectively so as to meet its ongoing MREL. There are risks that the Bank will be unable to raise the required capital and MREL-qualifying debt on acceptable terms, when planned or at all, and that the Bank will be unable to meet its full ICG when planned, or at all. The Bank's strategy aims to build an efficient, financially-sustainable and capital-resilient UK bank focused on retail and SME customers, differentiated by an ethically-led brand and a customer-centric proposition, and is designed to achieve a surplus to the Bank's PRA Buffer later in 2019 (based on the Bank's own internal assessment of future minimum Pillar 2a and 2b regulatory capital requirements and subject to future SREP). To the extent that the Bank does not perform in line with its strategy, the Plan and, where applicable, the May 2017 Outlook on the Plan or regulatory requirements are increased for any reason, additional CET1 capital may be required over and above that assumed in the May 2017 Outlook on the Plan. Any failure to raise such further capital could have a material adverse effect on the Bank's regulatory capital position, including its ability to maintain adequate loss-absorbing capacity. A failure by the Bank to meet some of its regulatory capital and loss-absorbing capacity requirements (including its ICG), will impact the actions that management are able to take to implement the Plan and, where applicable, the May 2017 Outlook on the Plan and may lead to the Authorities exercising some or all of their powers over the Bank, including, among other things, powers of intervention, the power to mandatorily write-down the Bank's capital instruments and the power to place the Bank within the Special Resolution Regime if they consider the Bank would otherwise be likely to fail.

- *The Bank will remain subject to any enforcement action the Authorities may take against it, which they may do at any time* – the Plan assumes that the Authorities will continue to not take enforcement action against the Bank in relation to the Bank's inability to meet certain regulatory requirements. These are meeting its ICG, Combined Buffer, PRA Buffer, MREL and CRR requirements (relating to the use of an IRB Approach to modelling its credit risk capital requirements). Irrespective of the successful implementation of the Restructuring and Recapitalisation, there is a risk that the Authorities may exercise their discretion and take enforcement action against the Bank at any time in relation to such non-compliance.

- *There is a risk of significant additional pension funding requirements* – the May 2017 Outlook on the Plan includes contributions of £12.5 million per annum for the period from 2018 to 2022. There is a risk that the Bank may be required to pay significantly more than assumed in the May 2017 Outlook on the Plan as a result of: (i) its "last-man standing" risk in Pace, should one or more participating employers fail; (ii) the outcome of contribution negotiations in the absence of the Pace Pensions Sectionalisation (for example, in the context of the 5 April 2016 Pace valuation currently underway); (iii) future actuarial valuations of Pace which may require renegotiation of deficit recovery schedules; and (iv) the implementation of the Pace Pensions Sectionalisation. Implementation of the Pace Pensions Sectionalisation on the terms set out in the Pace Heads of Terms would result in a recovery plan being put in place for the Bank Section immediately after Pace Pensions Sectionalisation which would require the Bank to make deficit payments (in advance) of £12.5 million per annum in respect of each of the calendar years 2018 to 2022 inclusive and £7.5 million per annum in respect of each of the calendar years 2023 to 2027 inclusive (and which will be subject to revision at future actuarial valuations in accordance with scheme funding legislation). There is, therefore, uncertainty as to future levels of Pace contributions payable by the Bank. Furthermore, the Bank may be required to fund an increased level of deficit in connection with the Britannia Scheme depending on the outcome of the next triennial actuarial valuation, which is currently underway or of any future actuarial valuation. An increase in contributions could have a material adverse effect on the Bank's business, operating results, financial condition, prospects and regulatory capital position.

- *The Bank's targeted reductions to its capital requirements may not materialise* – the Bank's current minimum Pillar 2a regulatory capital requirement is elevated relative to its peers. The Bank holds Pillar 2a regulatory capital requirements for operational, pension, model and transformation risks. The May 2017 Outlook on the Plan assumes that if the Restructuring and Recapitalisation is successful and the Bank remedies its credit risk modelling deficiencies, completes the remaining parts of its transformation, remediation and change programme on time and within budget and reduces its operational and pension risks, the Bank's Pillar 2a regulatory capital requirements will reduce over time. If these assumptions do not materialise, or otherwise the PRA does not agree with the Bank's internal assessment of its capital needs or does not agree to reduce the Bank's Pillar 2a regulatory capital requirement, there is a risk that the Bank may require more equity and other forms of loss-absorbing capacity beyond that contemplated by the May 2017 Outlook on the Plan. In relation to the Bank's modelling risk, there is a risk that the Bank could lose its IRB status which would result in consequential increases to its RWAs and capital requirements. See the risk factor entitled "*The Bank's business, operating results, financial condition and prospects and/or its ability to implement its strategy have been and could be adversely impacted by it not maintaining adequate regulatory capital and loss-absorbing capacity. The Bank's targeted reductions in capital requirements may not materialise.*" for further detail. See paragraph 8.2 of Part 7 of this Circular for a description of the net reduction in the Bank's Pillar 2a requirement assumed in the May 2017 Outlook on the Plan as a consequence of the submission by it of its 2016 Internal Capital Adequacy Assessment Process to the PRA.

- *Even if the Bank becomes profitable, there are restrictions on its ability to pay dividends to Shareholders* – the Bank does not expect to pay dividends in the near future, although the Bank believes that if it successfully implements its strategy, the Plan and, where applicable, the May 2017 Outlook on the Plan, there may be potential for a dividend payment in 2021. The Bank's ability to pay any dividends at any time in the future is subject to the Bank's compliance with regulatory capital and loss-absorbing capacity requirements, including the Combined Buffer (currently comprised only of its capital conservation buffer and set at 1.25 per cent. of total RWAs met entirely by CET1 capital. The capital conservation buffer is set to rise to 2.5 per cent. of total RWAs met entirely by CET1 capital in 2019 with a rise of 0.625 per cent. in both 2018 and 2019. In addition to the capital conservation buffer, the counter-cyclical capital buffer will rise from the current requirement of zero per cent. to 0.5 per cent. of total RWAs in June 2018 and is expected to rise to 1 per cent. of total RWAs by the end of 2018, which would result in an aggregate Combined Buffer requirement of 3.5 per cent. of total RWAs in 2019), which dictate the Maximum Distributable Amount available for distribution by way of dividends pursuant to the restrictions under CRD. Furthermore, distribution by way of dividend or variable remuneration will be dependent on the availability of distributable reserves, PRA approval and compliance by the Bank with provisions concerning dividends contained in its Articles of Association (for further information see paragraph 4 of Part 16 of this Circular). In addition, the availability of distributable reserves is expected to be reliant on a shareholder and court-approved reduction of share capital. There is no certainty that any such approvals will be forthcoming if and when such approvals are sought in the future. Furthermore, following completion of the Restructuring and Recapitalisation, the payment of dividends to A Shareholders in Holdco will be subject to, among other things, the availability of distributable reserves in Holdco and otherwise there being no impediment to passing on any dividends paid by the Bank so that they may ultimately be received by A Shareholders of Holdco. There can be no certainty that either of these matters will be satisfied in the future.

- *The Bank may be unable to recognise significant deferred tax assets assumed in the May 2017 Outlook on the Plan* – the May 2017 Outlook on the Plan assumes that the Bank recognises significant deferred tax assets during the life of the Plan. This recognition is dependent on a number of key criteria being achieved, including profitability or a high level of confidence by the Bank in future profitability, the Bank demonstrating a track record of delivery of the Plan and, where applicable, the May 2017 Outlook on the Plan, targets which minimises execution risk of the Plan and, where applicable, the May 2017 Outlook on the Plan, remaining above minimum Pillar 1 regulatory capital requirements in the Bank's Pillar 2b assessment, the Bank meeting its ICG removing the threat of resolution and the removal of the risk of the Authorities taking enforcement action against the Bank in relation to its non-compliance with certain regulatory capital and loss-absorbing capacity requirements, or confidence that this is a realistic near-term proposition, the Bank being in compliance with the Threshold Conditions (as defined below) and no change occurring in the relevant legal and regulatory framework. If the Bank does not deliver on the key elements of its strategy, the Plan and, where applicable, the May 2017 Outlook on the Plan, the expected quantum of deferred tax recognition or recognition itself may not materialise or may be delayed, which would increase the risk of a delay as to when the Bank expects to generate a post-tax profit in the future.

- *RoE targets may not be achieved* – the May 2017 Outlook on the Plan's targeted RoE relies on the Bank's ability to successfully mitigate the risks outlined above, particularly the Bank's ability to widen its net interest margin and develop its interest income and deliver the anticipated cost reductions and resulting improvements to its cost:income ratio. If any of the risks in this Part 3 do materialise, this may result in lower future returns and a lower than targeted RoE. See paragraph 9 of Part 7 of this Circular for the Bank's revised longer-term RoE target.

While the PRA accepted the Plan on 13 February 2017, the PRA stated that it intends to monitor closely the Bank's performance against it. On 27 June 2017, the PRA confirmed its acceptance of the May 2017 Outlook on the Plan, including the terms of the Restructuring and Recapitalisation. The PRA may withdraw its acceptance and/or approval of the Plan and/or the May 2017 Outlook on the Plan at any time, whether or not the Restructuring and Recapitalisation is successful.

The Bank's ability to deliver its strategy, the Plan and/or the May 2017 Outlook on the Plan, is also heavily influenced by external factors which may mean that the underpinning internal assumptions of the Bank may be incorrect and negatively impact the Bank's performance. Many of these factors are similar to those faced by other financial institutions and are described further below in this Part 3. For example, in preparing the Plan, the Bank used the market's forward implied view for market interest rates of base rate, swap rates, LIBOR rates and gilts, using a 10-day moving average on the market interest rates to smooth over any daily volatility. The 10-day moving average of the market forward-looking implied SONIA rates to 22 November 2016 were used (rounded to the nearest increment of 25 basis points), and these assumed a Bank of England base rate increase to 0.5 per cent. in May 2018, a further increase to 0.75 per cent. in June 2019, a rise to 1.0 per cent. in August 2020 and a final rise to 1.25 per cent. in November 2021. The Bank used a third-party model to forecast certain macroeconomic variables, such as inflation, unemployment, GDP and HPI, as at August 2016. The Bank's base rate outlook has been adversely impacted since the forward-looking market implied SONIA rates to 22 November 2016 used in the Plan. See paragraph 8.2 of Part 7 of this Circular for a description of the May 2017 Outlook on the Plan which reflects the more recent adverse base rate outlook. If the Bank's assumptions prove to be incorrect, there is a risk that this would impact the Bank's business, operating results, financial condition, prospects and its ability to achieve the targets set out in the Plan and, where applicable, the May 2017 Outlook on the Plan. Despite the steps taken toward compliance with regulatory requirements and complex transformation changes undertaken by the Bank, there remain a number of further actions that the Bank needs to undertake in order to be able to deliver its strategy, the Plan and/or the May 2017 Outlook on the Plan. The successful development and implementation of the Bank's strategy requires difficult, subjective and complex judgements including those relating to a range of factors which are not within the Bank's control or influence, for example, forecasts of economic conditions. In addition, unanticipated events may adversely affect the Bank's actual results of operations in future periods whether or not the assumptions in its strategy, the Plan and/or the May 2017 Outlook on the Plan otherwise prove to be correct. Historically, the Bank has experienced material variances to internal forecasts and budgets, particularly for significant one-off items including conduct risk, project costs, losses on asset sale de-leveraging, accelerated redundancy and severance costs, the sale of holdings in Unity Trust Bank and in Visa Europe and historical base rate decreases. In addition, the tax receivable balance from the Co-operative Group may vary from internal forecasts and budgets. There is, therefore, a risk that the Bank's actual results of operations could differ from those expressed or implied by any forward-looking statements or targets as a result of many factors, many of which may be outside of the Bank's control, including significant business, operational and economic risks and the risks described in this Part 3 and in the section of this Circular entitled "Forward-Looking Statements", and these differences could be material. Such forward-looking statements and targets should, therefore, be read in this context and construed accordingly, and investors should not place undue reliance on them. If the Bank fails to implement its strategy, the Plan and/or the May 2017 Outlook on the Plan, or if the estimated and expected future financial and operational performance is not achieved, the Bank's businesses, operating results, financial condition and prospects may be materially adversely affected.

5. ***The B Shareholders may seek to influence the governance and oversight of the Bank and change the Bank's current strategy. It is uncertain what if any changes will be made to the Bank's current strategy and whether or not any such changes would be successfully implemented.***

If the Restructuring and Recapitalisation is successfully implemented, there are several important changes that will be made to the governance, oversight and management of the Bank. It remains to be seen to what extent these changes will affect the Bank's current strategy, the Plan and, where applicable, the May 2017 Outlook on the Plan, or the Bank's implementation of that strategy. These changes include:

- the establishment of a new holding company for the Bank with a different governance structure to the existing governance of the Bank that is intended by the Principal Investors to allow B Shareholders greater influence on the governance and oversight of the Bank, although both the Bank and Holdco will have boards with a majority of independent non-executive directors with the same directors serving on both boards;
- providing that the B Shareholders in Holdco – those institutional shareholders that own 10 per cent. or more of the A shares of Holdco and satisfy certain other qualifying conditions – carry all the voting rights except in limited circumstances and have the benefit of certain shareholder approval and notification and other rights;
- up to two B Shareholder Nominee Directors of each of Holdco and, via Holdco's ownership of the Bank, the Bank may be appointed by the B Shareholders. If the B Shareholder Nominee Directors perform any executive function then they shall report to the Bank's and Holdco's CEO (who shall be the same person); and

- a Chief Restructuring Officer (who may, but is not required to, be a B Shareholder Nominee Director) may be appointed by the B Shareholders and report to the Bank's and Holdco's CEO (who shall be the same person).

The Bank expects that any changes in the short-term to its strategy are likely to focus on exploring a number of potential actions that may enable it to achieve enhanced financial performance over that assumed in the Plan, likely to be through a combination of: (i) incremental income growth, resulting from further plans to accelerate, re-launch or digitise asset growth and product sales; (ii) further cost reductions, including an assessment of options to structurally reduce costs by a significant proportion; (iii) active pursuit of funding from the potential RBS fund for business banking investment; and (iv) a review of the Plan to create a more efficient total capital position, including options to lower total capital requirements.

Examples of these actions may include: (i) a significantly enhanced credit risk capability to facilitate asset growth; (ii) a digitised and straight-through-processing approach to customer acquisition, driving income and cost reduction; (iii) further de-leverage of legacy assets; or (iv) investment to rationalise operations and systems, to structurally reduce the Bank's cost base.

The delivery of these potential management actions would require careful planning, phasing and investment choices and may not be possible without further capital. The successful development and implementation of any such new strategy requires difficult, subjective and complex judgements including those relating to a range of factors which are not within the Bank's control or influence, for example, forecasts of economic conditions. In addition, unanticipated events may adversely affect the Bank's actual results of operations in future periods whether or not the assumptions in its strategy otherwise prove to be correct. Such actions have yet to be subject to any detailed planning or investment review, or formal governance process. No assurance can be given that the Bank will decide to implement any or all of such potential management actions and whether or not they would achieve further asset growth and cost savings above those assumed in the Plan and, consequently, these potential management actions do not form part of the Bank's current strategy.

Any such change in strategy may lead to the Bank's actual results of operations materially differing from those expressed or implied by any forward-looking statements or targets contained in this Circular as a result of many factors, many of which may be outside of the Bank's control or influence, including significant business, operational and economic risks and the risks described in this Part 3 and in the section of this Circular entitled "Forward-Looking Statements", and these differences could be material and adverse.

The Bank expects that any changes resulting from the new governance and management arrangements as a consequence of the Restructuring and Recapitalisation will need to be made within the following parameters:

- the Bank's Values & Ethics being incorporated into the Holdco Articles of Association and remaining part of the Bank's Articles of Association;

- the PRA's assessment of the proposed Restructuring and Recapitalisation having been premised on its acceptance of both the proposed Restructuring and Recapitalisation and the May 2017 Outlook on the Plan, which took into account certain proposed management actions described in paragraph 8.2 of Part 7 of this Circular;

- any material changes to the May 2017 Outlook on the Plan or the Plan more generally requiring PRA review and acceptance; and

- the PRA having notified the Bank that it expects that by the time of publication of the Bank's next five-year operating plan, the Bank will provide to the PRA a detailed cost:income strategy setting out how the Bank will achieve in the medium-term a competitive cost:income ratio, in line with the Bank's peer group.

The B Shareholders may seek to influence the governance and oversight of the Bank and change the Bank's current strategy and it is uncertain what if any changes will be made to the Bank's current strategy. In the event that the Bank is unable to implement any chosen additional management actions, or otherwise implement any revised strategy, as expected or planned or at all, this could have a material adverse effect on the Bank's business, financial condition, operating results and prospects.

6. ***Irrespective of the successful implementation of the Restructuring and Recapitalisation, the Bank will not be compliant with its regulatory capital and loss-absorbing capacity requirements and will be subject to any enforcement action the Authorities may take in respect of such non-compliance.***

The Bank is currently non-compliant with respect to certain regulatory capital requirements and loss-absorbing capacity requirements. In summary, these areas of non-compliance comprise:

- the Bank's ICG;
- the Bank's Combined Buffer requirement under the CRD (currently comprised only of its capital conservation buffer and set at 1.25 per cent. of total RWAs met entirely by CET1 capital. The capital conservation buffer is set to rise to 2.5 per cent. of total RWAs met entirely by CET1 capital in 2019 with a rise of 0.625 per cent. in both 2018 and 2019. In addition to the capital conservation buffer, the counter-cyclical capital buffer will rise from the current requirement of zero per cent. to 0.5 per cent. of total RWAs in June 2018 and is expected to rise to 1 per cent. of total RWAs by the end of 2018, which would result in an aggregate Combined Buffer requirement of 3.5 per cent. of total RWAs in 2019);
- the Bank's PRA Buffer (currently set by the PRA at a level in order to withstand prudential stress test scenarios and comprised exclusively of CET1 capital); and
- the Bank's MREL.

The Bank's strategy assumes that the Authorities will continue to not take enforcement action against the Bank in relation to its inability to meet the regulatory requirements described above. There is a risk that the Authorities may exercise their discretion and take enforcement action against the Bank at any time.

In accordance with CRD IV, the Authorities must require the Bank to take the necessary measures at an early stage to address relevant problems where the Bank does not meet the requirements of CRD IV or the Authorities have evidence that the Bank is likely to breach the requirements of CRD IV within the following 12 months. While the PRA has accepted the Plan and the May 2017 Outlook on the Plan, the PRA has stated that it intends to monitor closely the Bank's performance against the Plan and consequently, where applicable, the May 2017 Outlook on the Plan, and the Bank has been subject to a heightened degree of regulatory supervision since 2013.

The PRA may withdraw that acceptance at any time, even if the Restructuring and Recapitalisation is successful. The PRA and, where applicable, the Bank of England, have the discretion to revisit the Bank's capital requirements, loss-absorbing capacity, and other regulatory obligations and any non-compliance by the Bank with its ICG, Combined Buffer, PRA Buffer, MREL and CRR provisions relating to credit modelling. The PRA and, where applicable, the Bank of England, may do this at any time and, if the PRA and, where applicable, the Bank of England does so, the nature or extent of any possible changes to the Bank's ICG requirement, Combined Buffer, PRA Buffer and MREL or other regulatory obligations may significantly increase or expedite the Bank's need to raise additional capital or loss-absorbing capacity. If the Bank fails to meet its ICG, Combined Buffer, PRA Buffer and MREL or other regulatory obligations or its plan to comply with its ICG, Combined Buffer, PRA Buffer and MREL or other regulatory obligations, it is not possible to predict how the PRA would react. The PRA may, in any such circumstances, at its discretion elect to exercise one or more of its various powers over the Bank. This could include, among other things, a variation or withdrawal of the Bank's permissions or restricting the Bank's business. If the PRA concludes that the Bank is "failing or likely to fail", the Bank of England could impose a mandatory write-down of the Bank's regulatory capital instruments (which could include the Ordinary Shares and the Subordinated Notes) and the Bank of England and/or HM Treasury could exercise their powers to resolve the Bank under the Special Resolution Regime, as further described in paragraph 2.8 of Part 11 of this Circular.

Furthermore, there is a risk that the Bank's regulatory capital and loss-absorbing capacity requirements, or PRA expectations and approach with respect to such regulatory capital and loss-absorbing capacity requirements, may increase beyond those currently planned for by the Bank.

7. ***Irrespective of the successful implementation of the Restructuring and Recapitalisation, the Bank will not be compliant with certain other PRA and FCA regulatory requirements and the Bank will be subject to any enforcement action the Authorities may take in respect of such non-compliance.***

The Bank's deficiencies against regulatory requirements and expectations have existed for some time and will continue for some years to come while the Bank implements its strategy, and the Bank has been subject to a heightened degree of regulatory supervision since 2013. The successful implementation of the Bank's strategy depends on the Authorities not taking enforcement action against the Bank regarding any continuing and intervening deficiencies to required regulatory standards.

The Threshold Conditions for which the PRA and FCA are responsible in relation to the Bank, which set out the minimum standards to be met relating to financial and non-financial resources, including capital, risk management, liquidity, and technology, are set out in the FSMA (the "**Threshold Conditions**"). The PRA's and FCA's general policy is not to communicate their assessment of their position in relation to the Threshold Conditions. The FCA did, however, in March 2017, confirm to the Bank that the various IT remediation activities undertaken by the Bank in 2015 and 2016 had brought the Bank back into compliance with the FCA's Threshold Conditions requirements for non-financial resources. The PRA has not communicated to the Bank its assessment of the Bank's position in relation to the Threshold Conditions.

Risks relating to the Bank's credit risk capital modelling requirements

The Bank is not fully compliant with the CRR provisions related to the use of an IRB Approach to modelling its credit risk capital requirements.

A review by the PRA in 2015 identified areas of non-compliance and inadequate procedures relating to use of the IRB Approach requiring improvement and remediation to rectify such non-compliance under supervisory guidance. This involved a re-design of the Bank's model risk policy, redevelopments of some of the Bank's IRB models and the strengthening of the Bank's overall control environment. In March 2016, the Bank received a communication from the PRA levying a CRR-related Pillar 2a regulatory capital requirement in the form of a fixed requirement in order to cover these risks. It is the Bank's objective, subject to successful completion of the remediation plan, to seek and obtain PRA approval of such remediation by the end of 2017 and to have this fixed requirement removed from its ICG during the first quarter of 2018. Irrespective of the success of the Restructuring and Recapitalisation, there is a risk that this objective will not be met within that timeframe or at all.

There is a risk that any failure to address CRR IRB non-compliance by the end of 2017 (or at all) could potentially result in further regulatory action such that the Bank's permission to use an IRB Approach could be removed, resulting in the use of a standardised approach to modelling credit risk. This could, among other consequences, expose the Bank to a material increase in the calculation of its minimum Pillar 1 regulatory capital requirements and, given that many of the Bank's regulatory capital requirements are calculated by reference to the Bank's RWAs, there may be a consequential requirement to hold additional regulatory capital, the creation of an additional ICG deficit and/or a reduction in the Bank's CET1 capital ratio and an impact on the Bank's ability to meet its CET1 capital requirements, its ICG, its Combined Buffer, its PRA Buffer or its MREL.

Accordingly, if the Bank is required to cease using an IRB Approach to its credit risk modelling, there is a risk that the Bank would require more equity and other forms of loss-absorbing capacity beyond that contemplated by the Plan and that any such additional equity or loss-absorbing capacity would not be available when needed, on acceptable terms, or at all.

Deposit Guarantee Scheme Directive and FCA cash savings requirements

The Bank has not met the 2016 regulatory deadlines for the "single customer view" set by the PRA as a result of the Deposit Guarantee Scheme Directive (Directive 2009/14/EC) (the "**DGSD**") and the rules and guidance in the FCA's Banking Conduct of Business Sourcebook introduced following the FCA's market study into competition in the cash savings sector (the "**FCA cash savings requirements**"). The Bank has been in dialogue with the PRA and FCA concerning implementation of the "single customer view" requirement by the end of 2017 and commencement of implementation of the FCA cash savings requirements by June 2017. Any breach of these requirements could result in sanctions against the Bank being imposed, which could range from undertakings being given in relation to future compliance and/or enforcement action taken against the Bank.

8. ***The Bank's business, operating results, financial condition and prospects and/or its ability to implement its strategy have been and could be adversely impacted by it not maintaining adequate regulatory capital and loss-absorbing capacity. The Bank's targeted reductions in capital requirements may not materialise.***

The Bank's current minimum Pillar 2a regulatory capital requirement is elevated relative to the Bank's peers principally due to the Bank's operational, pension, model and transformation risks. The Bank anticipates that if the Restructuring and Recapitalisation is successful and the Bank completes its credit risk modelling deficiencies (part of its model risk) remediation programme, completes the remaining parts of its strategic and remediation projects on time and within budget and reduces its operational and pension risks, and the Bank otherwise delivers the Plan and, where applicable, the May 2017 Outlook on the Plan, these actions will reduce the Bank's minimum Pillar 2a regulatory capital requirement (with a targeted end-state, at the end of the life of the Plan (substantially progressed by the end of 2019) of approximately 8.5 per cent. of RWAs, including the targeted reduction to the Pillar 2a pension risk resulting from the implementation of the Pace Pensions Sectionalisation, the assumed RWAs reduction driven from the expected de-leverage of approximately £2 billion in Optimum assets during the fourth quarter of 2017, alongside other Pillar 2a developments driven from the Bank's 2016 Internal Capital Adequacy Assessment Process (subject to PRA approval and subject to the outcome of future SREP)). The Bank's targeted Pillar 2a reduction as described above, together with the delivery of the Plan and, where applicable, the May 2017 Outlook on the Plan, are expected by the Bank to result in the Bank achieving its target of meeting full ICG during 2018, irrespective of whether the issuance of approximately £250 million Tier 2 debt targeted in the Plan for 2018 takes place (albeit that such Tier 2 debt issuance is required for the purposes of the Bank meeting its regulatory capital and loss absorbing capacity requirements at the end of the life of the Plan). This reduction in the Bank's minimum Pillar 2a regulatory capital requirement and targeted return to meeting its ICG is based on the Bank's internal view of how its ICG will evolve over time and there is a risk that a future SREP may set a requirement different to that which the Bank assumes as part of the May 2017 Outlook on the Plan, including any Pillar 2a pension risk component specific to the Pace Pensions Sectionalisation. Furthermore, following completion of the Restructuring and Recapitalisation, the Bank is also targeting compliance with its Combined Buffer in 2018. The Bank expects that these requirements will also, following Completion, be met at the Holdco consolidated level. See paragraph 8.2 of Part 7 of this Circular for a description of the May 2017 Outlook on the Plan's assumed net reduction in the Bank's Pillar 2a requirement as a consequence of the submission by the Bank of its 2016 Internal Capital Adequacy Assessment Process to the PRA (subject to future SREP).

The Bank must raise and maintain significant amounts of loss-absorbing capacity to comply with the MREL Statement of Policy. The Bank has received a binding MREL requirement for the year ending 31 December 2017 from the Bank of England requiring, in line with other UK banks, MREL which is equivalent to the Bank's ICG requirement. The Bank is not expecting to meet its full ICG until 2018 (assuming the successful implementation of the Restructuring and Recapitalisation, subject to delivery of the Plan and, where applicable, the May 2017 Outlook on the Plan, based on the Bank's own internal assessment of future minimum Pillar 2a regulatory capital requirements and subject to future SREP) and, therefore, the Bank is not expecting to meet its MREL for 2017. The MREL

Statement of Policy includes a transitional requirement for the period up to 1 January 2020 which is equivalent to the Bank's ICG requirement, followed by an interim requirement from 1 January 2020 up to 1 January 2022, which is equivalent to 18 per cent. of its RWAs. End-state MREL, from 1 January 2022, will be set on a case-by-case basis for all UK banks depending on the agreed resolution strategy for that bank. These requirements are currently expected to be either two times ICG or a lower amount determined by the Bank of England based on the Bank's resolution strategy set by the Bank of England, of which the Bank's current planning assumption is the latter of these two options.

As set out in the MREL Statement of Policy, the Bank of England can provide institutions with a non-binding indication of any MREL which the Bank of England expects institutions to meet in future years. The Bank of England's current intention is to set MREL in excess of regulatory capital requirements in 2020 for all institutions for which the preferred resolution strategy is not a bank insolvency procedure. In addition, the Bank of England can provide particular institutions with a non-binding indication of its intention to set a higher or earlier future MREL, or set higher or earlier required MREL levels. As set out in the MREL Statement of Policy, the Bank of England will do so where action is needed to enhance an institution's resolvability and this is necessary to meet the Bank of England's objectives as resolution authority. The Bank of England has chosen to do so for the Bank, in line with the Bank of England having identified a shortage of loss-absorbing capacity as a substantive impediment to the Bank's resolvability.

As such, the Bank of England has provided the Bank with a non-binding indication that its current intention is to set the Bank's MREL for 2018 in an amount which strongly indicated that the Bank would need to issue MREL-qualifying debt earlier than assumed in the Plan (which assumes issuances in 2020 and 2021, following a Tier 2 debt issuance in 2018 (with such same timing assumptions also made in the May 2017 Outlook on the Plan)), possibly as early as before the end of 2017. The Bank does not believe its current capital position, in the absence of the successful implementation of the Restructuring and Recapitalisation, would be sufficient to enable it in the future to issue MREL-qualifying debt on acceptable terms in such amount as would be required. The Bank of England indicated to the Bank that it would review this intention as part of the process for setting the Bank's MREL for 2018, which will include a consideration of any revisions in the Bank's business plan and strategy. Furthermore, the Bank of England has publically stated (as part of its publication of indicative MREL data on 5 May 2017) that "*The Co-operative Bank has been excluded from the calculation of the average because the firm is currently seeking a sale, which has the potential to significantly affect The Co-operative Bank's balance sheet. Therefore an indicative MREL based on The Co-operative Bank's balance sheet today may not be a useful guide to the eventual requirement*". The Bank believes that the Restructuring and Recapitalisation would significantly affect the Bank's balance sheet and, accordingly, the Bank assumes that, if a liability management exercise and capital raising such as the Capital Raising is successfully implemented, the Bank's MREL will be reviewed by the Bank of England to take into account the completed Restructuring and Recapitalisation and subsequently revised to be brought in line with the MREL Statement of Policy. As a result, the May 2017 Outlook on the Plan assumes compliance with the transitional MREL set out in the MREL Statement of Policy during the course of 2018 (for the avoidance of doubt, excluding PRA Buffer – meaning that the Bank meets its MREL by including CET1 capital counted towards its PRA Buffer), when the Bank is targeting to meet its ICG, with such MREL compliance maintained thereafter supported by the targeted MREL-qualifying debt issuances in 2020 and 2021. The above-mentioned MREL issuances may not be completed when planned, on acceptable terms, or at all. The Bank is expected by its regulator to meet its Combined Buffer and PRA Buffer in addition to both its transitional, interim and end-state MREL.

Even if the Restructuring and Recapitalisation is successful, the Bank's ability to complete its targeted Tier 2 capital and MREL-qualifying debt issuances may depend on an improvement in the Bank's credit rating from its current sub-investment grade credit rating and conducive capital markets prevailing at the time. There is, therefore, a risk that the Bank may be unable to complete these issuances when contemplated under the May 2017 Outlook on the Plan or when required, on acceptable terms, in the amounts required, or at all.

The Bank is not currently subject to the PRA's leverage ratio framework which requires firms within it to have a 3 per cent. minimum leverage ratio requirement (in June 2017 the Bank of England's Financial Policy Committee ("**FPC**") and the PRA launched consultations on changes to the UK leverage ratio framework relating to the treatment of claims on central banks (CP 11/17), which include a proposed increase in the minimum requirement from 3 per cent. to 3.25 per cent.). The Bank is not currently within the framework, as it has retail deposit levels below £50 billion (being the threshold at which this becomes a binding requirement). As at 31 December 2016, the Bank's leverage ratio was 2.6 per cent. (3.8 per cent. as at 31 December 2015). Assuming the successful implementation of the Restructuring and Recapitalisation, the Bank expects that its leverage ratio would improve to levels in excess of 3.25 per cent. However, if the Restructuring and Recapitalisation is not implemented successfully, or if it is but the Bank's leverage ratio otherwise falls below the minimum leverage ratio requirement and the Bank is required to comply with the minimum leverage ratio requirement, the Bank would need to take action to improve its leverage ratio, which may have a material adverse effect on the Bank's businesses, operating results, financial condition and prospects. A failure in those circumstances to take actions to avoid a breach of the PRA's requirements could lead to the PRA taking enforcement action and could have a material adverse effect on the Bank's businesses, operating results, financial condition and prospects.

9. ***The Bank's business, operating results, financial condition and prospects and/or its ability to implement its strategy may be adversely impacted by future changes to its regulatory capital requirements driven by regulatory stress-testing results.***

In December 2014, the PRA announced the results of the Bank of England concurrent stress tests and confirmed that the Bank's capital resources were projected to be exhausted in the Bank of England's hypothetical stress scenario and therefore the Bank did not hold sufficient capital resources to meet its PRA Buffer. As a result, the Bank was required to submit a revised business plan to deliver capital resilience against the stress scenario (the "**2014 Plan**"). The 2014 Plan aimed to build a sustainable bank and was designed to create a sustainable surplus to the PRA Buffer in 2019 which theoretically could withstand a severe stress scenario equivalent to the 2014 Bank of England stress test.

Following the 2014 Bank of England concurrent stress tests, the Bank was not included in the 2015 or 2016 Bank of England concurrent stress tests, as these tests were designed to assess resilience to a deterioration in global economic conditions. The Bank was not included as a result of the size of the Bank's balance sheet, which is significantly smaller than the other firms that were included in the concurrent stress test; therefore, the resilience of the Bank is unlikely to affect the resilience of the financial system as a whole. The Bank is not currently a member of the UK concurrent stress-testing regime. However, as part of its annual planning process, the Bank undertakes an appropriate Pillar 2b assessment and the results are discussed with the PRA as part of the Internal Capital Adequacy Assessment Process submission.

The Bank considers that the Plan and the May 2017 Outlook on the Plan are designed to withstand, the H1 2016 PRA stress test, along with other idiosyncratic stress events. The H1 2016 PRA stress test includes a reduction in interest rates from the half year ended June 2017 to zero per cent. across the life of the Plan, a sharp reduction in the house price index ("**HPI**") and commercial real estate ("**CRE**"), a recession in 2017 before GDP recovers, and an increase in unemployment and inflation.

It is not possible for the Bank to predict whether or not it will be required to participate in future stress tests or what form and magnitude of future stress tests may be applied to it and, if required to do so, what balance sheet or other actions may be required to mitigate any assumed stress impacts. There is a risk that the Bank would be subject to increased Pillar 2a and Pillar 2b regulatory capital requirements and be required to raise additional capital if the Bank became subject to the Bank of England's stress-testing regime.

10. ***The Bank anticipates giving formal notice to exercise its right to terminate the Calico Finance Number One synthetic securitisation through a regulatory call, which the Bank will be unable to undertake if, amongst other things, the occurrence of a regulatory event is successfully challenged by investors. This would mean that the Bank would not benefit from the assumed annual interest***

savings expected to result from exercising such call and would mean that the viability of contemplated further reductions of Optimum assets that include Calico referenced assets may be jeopardised, which could adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements.

In 2013, the Bank (as credit protection buyer) entered into a synthetic securitisation transaction to obtain credit protection through a credit default swap with Calico Finance Number One ("**Calico**") relating to the mezzanine risk in a proportion of Optimum residential mortgages. Calico, as the credit default swap protection seller, issued £116.5 million of credit-linked notes to investors at an expense to the Bank of approximately £15 million per annum. The Bank also retained other regulatory capital benefits to capital resources due to the impact on expected loss shortfall regulatory deductions. The Plan assumed Calico would remain outstanding until its legal maturity in March 2021.

Following notice from the PRA dated 23 June 2017 that, in their provisional assessment, Calico no longer met "significant risk transfer" requirements within the meaning of the CRR and EBA technical standards ("**SRT**"), the Bank plans to give formal notice to exercise its right to terminate Calico in September 2017 based upon the occurrence of a "Regulatory Event" (as defined in the documents governing the transaction) as a consequence of the change in SRT status of Calico. As at 31 December 2016, the impact of Calico not meeting SRT requirements would have seen a reduction in the Bank's CET1 ratio of 0.8 per cent., with such impact reducing over time (in accordance with the mismatch rule prescribed by CRR) as Calico approaches its legal maturity in March 2021. A regulatory call, as permitted by the transaction documentation, would allow the Bank to terminate the credit default swap between the Bank and Calico, and repay Calico investors the principal amount of their notes at par plus accrued interest. The May 2017 Outlook on the Plan assumes the successful exercise of this right and redemption of the notes in 2017.

The Bank's exercise of this right is subject to certain uncertainties. In particular, these include a risk that the investors in the Calico notes may seek to challenge or litigate the Bank's exercise of the regulatory call event and associated termination of the credit default swap, which could adversely impact the Bank's business, operating results, financial condition (including its net interest margin) and prospects. The May 2017 Outlook on the Plan assumes an annual benefit to the Bank's income statement from the regulatory call of approximately £15 million per annum up until maturity due to the removal of the interest expense relating to Calico. Should the Bank be unable to complete a regulatory call or otherwise exit Calico on acceptable terms, the Bank would not benefit from the assumed annual interest savings expected to result from exercising such call and this would mean that the viability of contemplated further reductions of Optimum assets that include Calico referenced assets may be jeopardised, which could adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements.

11. ***The Bank anticipates making a further reduction of Optimum assets through whole-loan disposals and/or securitisations. There is a risk that the Bank will be unable to de-leverage its Optimum assets in a capital efficient manner, or may incur greater than expected costs or experience delays in relation to such de-leveraging, which could adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements.***

A key component of the Bank's management actions assumed as part of the May 2017 Outlook on the Plan is the further reduction of Optimum assets through whole-loan disposals and/or securitisations, in a manner that seeks to ensure that any anticipated future losses (through forgone income and any possible loss on sale) from such de-leveraging actions do not materially exceed the capital released from the reduction in capital requirements of the portfolio. The Bank anticipates reducing its Optimum assets by approximately £2 billion during the fourth quarter of 2017 (subject to market conditions, including as to market capacity and available pricing, timing and terms being subject to PRA approval), of which the Bank expects to retain a significant proportion of AAA-rated notes to be issued if the Optimum de-leveraging strategy is achieved through securitisations. The size of this contemplated transaction is deemed by the Bank to be viable on the assumption that the regulatory call of Calico discussed in the risk factor above proceeds. Although the Bank completed two Warwick securitisations in 2015, it is uncertain whether the securitisation markets will absorb further securitisations or that alternative whole-loan portfolio de-leverage exits for Optimum assets will be available at the capacity and economics assumed as part of the May 2017 Outlook on the Plan. In particular, the Bank's Optimum de-leveraging strategy may be adversely impacted by draft EU securitisation regulation that, if implemented would prohibit the securitisation of self-certified mortgage assets from 1 January 2019. A significant proportion of Optimum assets are self-certified. Further, the pricing and size of future securitisation transactions by the Bank are dependent on the prevailing conditions in the securitisation markets or the "whole-loan" residential mortgage portfolio sale market, which may be impacted by macro-economic factors beyond the control of the Bank.

Accordingly, there is a risk that any disposal and/or securitisation of the Bank's Optimum assets may not occur, when planned, be carried out in a capital efficient manner, or at all. Assuming the successful completion of such a de-leveraging transaction, the Bank would expect a significant reduction in RWAs and other non-Pillar 1 capital requirements to result, these impacts are expected to offset the income forgone on the disposed assets. This impact, facilitated by the RWA reduction and other Pillar 2a and Pillar 2b (subject to future SREP) reduction benefits from the regulatory call and termination of Calico (assuming that the Bank proceeds with, and is successful, in making, such a call), are expected to result in a favourable impact to ICG including PRA Buffer over the life of the Plan (subject to further SREP). There is a risk, however, that the benefits assumed may not materialise in the quantum expected or at all. Any failure by the Bank to further de-leverage its Optimum assets in accordance with the May 2017 Outlook on the Plan and/or any failure to carry out such de-leveraging in a capital efficient manner or in a way that does not give rise to greater than expected costs being incurred could negatively impact the Bank's business, operating results, financial condition (including its net interest margin) and prospects as well as its ability to comply with its regulatory capital requirements. For a description of the risk associated with the Bank accessing the wholesale funding market and the volatility of such market see the risk factor entitled "*The Bank faces risks associated with wholesale market access and volatility*".

12. ***If the Restructuring and Recapitalisation is unsuccessful, there is an increased risk that the Bank will fail to comply with its minimum Pillar 1 regulatory capital requirement on a solo-consolidated basis ahead of any breach in the Bank Group's consolidated position.***

The Bank has regulatory approval on an individual basis to operate under a solo-consolidation permission. In March 2016, the Bank was granted a new permission to operate under a solo-consolidation, though with respect to a smaller number of subsidiaries than it previously held in its permission in both 2014, and 2015. The revision mainly comprised the removal of FCA-regulated entities. The Bank's solo-consolidated CET1 capital ratio is lower than its consolidated CET1 capital ratio. Accordingly, there is lower projected headroom above the Bank's solo-consolidated minimum Pillar 1 regulatory capital requirement on a solo-consolidated position as compared to a consolidated position. Consequently, there is a strong likelihood that any possible future breach of the Bank's regulatory capital minimum requirements would occur on a solo-consolidated basis prior to any breach in the Bank Group's consolidated position albeit that the Bank expects to continue to meet its minimum Pillar 1 regulatory capital requirements (based on the Bank's own economic assumptions in both cases). If the Restructuring and Recapitalisation is not successful, there is a risk that this may adversely impact the Bank's ability to comply with its minimum Pillar 1 regulatory capital requirement on a solo-consolidated basis before any breach in the Bank Group's consolidation position. In the event of any such future breach, the Authorities may not be able to accept such non-compliance by the Bank with its minimum Pillar 1 regulatory capital requirement.

13. ***Further capital and loss-absorbing capacity may be required as a result of regulatory requirements or guidance or as a result of further costs or losses exceeding the Bank's estimates and assumptions underlying the Plan and/or the May 2017 Outlook on the Plan.***

The Bank may need to raise further equity, regulatory capital, MREL-qualifying debt, and/or take other management actions not otherwise anticipated by its strategy, the Plan and/or the May 2017

Outlook on the Plan, as a result of regulatory requirements or guidance or as a result of further costs or losses or shortfall in revenues exceeding the Bank's estimates.

If the Bank does not perform in line with its strategy, the Plan and/or the May 2017 Outlook on the Plan or regulatory requirements are increased for any reason, additional CET1 or other regulatory or loss-absorbing capital may be required over and above that included in the Plan and the May 2017 Outlook on the Plan and/or the Bank's RWAs could be reduced by the Bank taking action. Furthermore, absent the successful implementation of the Restructuring and Recapitalisation, in a Working Capital Stress Scenario (as described in paragraph 2.16 of Part 7 of this Circular), the Bank would not have enough CET1 capital to meet its minimum Pillar 1 regulatory capital requirements over the Working Capital Period. Any further or additional CET1 or other MREL or other loss-absorbing capacity may not be available when needed or planned, or on acceptable terms, or at all. Any failure to raise such further capital could have a material adverse effect on the Bank's regulatory capital position, including its ability to maintain adequate loss-absorbing capacity. Furthermore, if the Bank is unable to raise all or part of such additional capital, there is a risk that the Authorities could require further or other actions to be taken by the Bank. If other management actions required by the Authorities to be taken were unable to be taken by the Bank, the Bank of England and/or HM Treasury would be able to take further actions under the range of options available to them, including Special Resolution under the Special Resolution Regime. Whether the Bank is able to meet its ICG and/or Combined Buffer and/or PRA Buffer and/or MREL during the life of the Plan will depend on a number of factors, both within and outside the control of the Bank, including the Bank's ability to implement the Plan and, where applicable, the May 2017 Outlook on the Plan (including the implementation of the Restructuring and Recapitalisation) and changes in regulatory risk appetite and economic and market conditions generally in the UK.

The Bank may be unable to raise any additional capital or loss-absorbing capacity when needed on favourable terms, or at all (for example, as an unlisted entity, the Bank has limited access to the equity capital markets). In such cases, the Bank may as a result be in breach of its approved regulatory requirements or expectations and, there may be a risk of the PRA exercising any of its wide-ranging powers over the Bank. If the PRA concludes that the Bank is "failing or likely to fail", the Bank of England could impose a mandatory write-down of the Bank's capital instruments (which could include the Ordinary Shares and the Subordinated Notes), and the Bank of England and/or HM Treasury could exercise their powers under the Special Resolution Regime to resolve the Bank. See the risk factor entitled "*Shareholders will experience significant dilution to their ownership interests following completion of the Restructuring and Recapitalisation*" for further information.

14. ***Rating downgrades and/or negative market sentiment with respect to the Bank may have an adverse effect on the Bank's ability to implement its strategy, the Plan and/or, where applicable, the May 2017 Outlook on the Plan and on its business. The Bank's ability to raise the capital and debt it needs, including the Tier 2 and MREL-qualifying debt it is targeting under its strategy, when needed, on acceptable terms, or at all, may depend on the Bank improving its credit rating.***

In 2013, Fitch and Moody's downgraded the Bank's senior debt ratings from investment grade to sub-investment grade. The 2013 credit rating downgrades have:

- led to sub-investment grade ratings on the Bank's senior debt, leading to a significant reduction in the demand for these types of instruments and ratings-sensitive customer deposits;
- negatively impacted the Bank's ability to access short-term unsecured wholesale funding; and
- increased the Bank's collateral requirements used in the clearing and payment systems.

On 15 February 2017, Moody's announced that it had downgraded the Bank's long-term senior unsecured rating to Ca from Caa2 with a developing outlook. On 21 February 2017, Fitch downgraded the Bank's long-term issuer default rating to B- from B with an evolving outlook. The Bank is currently rated:

- B- (long-term and evolving outlook) and B (short-term) by Fitch; and

- Ca (long-term senior unsecured rating with a developing outlook) and NP (short-term) by Moody's.

Following the Bank's announcement on 28 June 2017 describing the outline of the Restructuring and Recapitalisation, Moody's subsequently announced on 30 June 2017 that it had placed the Bank's senior unsecured debt rating and the Bank's Ca standalone baseline credit assessment on review for an upgrade. This review reflects Moody's opinion that the probability of the Bank being placed into resolution was reduced. On 30 June 2017, Fitch maintained the Bank's long-term issuer default rating at B- but downgraded the Bank's viability rating from CC to C reflecting its methodology which classifies the proposed exchange of subordinated debt (being a component of the Restructuring and Recapitalisation) as a "distressed debt exchange".

Credit rating downgrades affect the Bank's funding profile and the cost to the Bank of raising new funding. The impact on access to funding and increased cost of funding may, therefore, over the long-term have an adverse effect on the Bank's business, operating results, financial condition and prospects and/or adversely affect the Bank's ability to deliver the Plan and, where applicable, the May 2017 Outlook on the Plan.

The Bank raises the majority of its funding through accepting retail and corporate deposits. The Bank has also issued funding from a range of programmes (including medium-term note, securitisation and covered bond programmes) targeting wholesale investors.

The continuation of the Bank's current rating or any further downgrade in the Bank's credit ratings could:

- increase its borrowing costs;
- undermine confidence in the Bank and/or result in an outflow of deposits from the Bank;
- further limit its access to the capital markets or limit the range of counterparties willing to enter into transactions with the Bank, as many institutions require their counterparties to satisfy minimum ratings requirements; and/or
- result in suppliers requesting special terms (which could include, for example, onerous payment terms) to supply services to the Bank.

Furthermore, any further downgrade of the UK sovereign credit rating or the perception that such a downgrade may occur could depress consumer confidence (which could result in withdrawals of customer deposits), restrict the availability, and increase the cost, of funding for the Bank and/or its customers, further depress economic activity, or inhibit any recovery, increase unemployment and reduce asset prices, destabilise the markets, impact the Bank's own rating and borrowing costs and have a material adverse effect on the Bank's operating results and financial condition.

There is also a risk that the implementation of the Plan and, where applicable, the May 2017 Outlook on the Plan or other actions taken by the Bank may not improve the Bank's credit rating. Further negative change in sentiment to the Bank as a result of continued adverse publicity and market or other conditions could result in the Bank's credit rating remaining below investment grade and/or being reduced further, which may impact the ability of the Bank to raise additional capital or loss-absorbing capacity in the future, when needed, on acceptable terms, or at all. Any future declines in those aspects of the Bank identified by the rating agencies as significant business or a failure by the Bank to achieve its strategic objectives could also adversely affect the rating agencies' perception of the Bank's credit and cause them to take further negative ratings actions.

15. ***The Bank has a significant holding of available-for-sale investment securities, including Warwick Finance One and Two securitisation notes. Negative changes in the carrying value of investment securities could have a material adverse effect on the Bank's business, operating results, financial***

condition and prospects, as well as its ability to achieve the Plan and, where applicable, the May 2017 Outlook on the Plan.

As at 31 December 2016, the Bank's portfolio of listed available-for-sale investment securities had a fair value of £3.5 billion, equal to 12.82 per cent. of its total assets at the same date. The Bank's available-for-sale investment securities are valued on each balance sheet date and any gains and losses arising on the sale of available-for-sale investment securities are recognised in the Bank's income statement and any cumulative fair value gain or loss previously recognised in other comprehensive income, which is re-classified to the income statement at the same date.

There is a risk that valuations of the Bank's investment securities in future periods may result in losses or impairments via valuation reserves, which could have a material impact on the Bank's CET1 capital. In addition, the value that the Bank ultimately realises for its investment securities may be lower than their current carrying value, resulting in losses being recorded in the Bank's income statement, which could be material. Any of these factors could have a material adverse effect on the Bank's business, operating results, financial condition, prospects and its ability to implement the Plan and, where applicable, the May 2017 Outlook on the Plan.

The Bank's available-for-sale investment securities portfolio qualifying as primary liquidity comprises highly rated debt instruments issued by UK and EU governments and supranational bodies. The Bank's investment securities portfolio also includes residential mortgage-backed securities ("**RMBS**") holdings (including Warwick Finance One and Two Class A RMBS), which are classified as other liquid assets. As described in paragraph 8.2 of Part 7 of this Circular, the Bank is currently expecting a further reduction of Optimum Assets through securitisations and/or whole-loan sales and, if such transactions are effected in the future by way of securitisation, the Bank expects that it will retain a significant proportion of the AAA-rated notes to be issued in connection therewith, which will consequently also form part of the Bank's investment security portfolio. Additionally under IFRS 9, the Bank's investment security portfolio may be classified and measured differently to the current fair valuation basis resulting in a gain or loss on day 1 implementation of IFRS 9 on 1 January 2018. The parallel run by the Bank of the requirements of IFRS 9, which is planned to take place in the second half of 2017, is expected to provide reliable quantitative impact information which will be disclosed in the Bank's 2017 annual report and accounts. Until such a reliable estimate is available, there is a risk that IFRS 9 could have a material adverse effect on the Bank's financial condition, operating results and prospects.

As at 31 December 2016, 100 per cent. of the Bank's £3.5 billion investment security portfolio had a rating of AA+ or higher. The Bank is subject to the additional risk that adverse economic and market conditions could reduce its ability to raise adequate liquidity from the portfolio to meet its liabilities when they are expected to fall due, which could in turn have a material adverse effect on its business, operating results, financial condition, prospects and its ability to implement the Plan and, where applicable, the May 2017 Outlook on the Plan.

16. ***The Bank has a high cost:income ratio relative to other UK banks that may be commercially unsustainable. A failure by the Bank to implement its cost reduction initiatives and achieve a competitive cost:income ratio in the medium-term is likely to have a material adverse effect on the Bank's ability to deliver its strategy, its results of operations, financial condition and operating results, and the Bank's ability to return to profitability.***

Although the Bank reduced its operating costs by 22 per cent. in the three years ended 31 December 2016, the Bank continues to have a high cost:income ratio in absolute terms and relative to other UK banks, which inhibits the Bank's profitability and hinders the Bank's ability to generate capital organically and be commercially sustainable. The Plan, therefore, targets a reduction in operating costs from £445 million in the year ended 31 December 2016 to approximately £410 million in the year ending 31 December 2017, further reducing to a long-term target annual operating costs run rate of approximately £350 million per annum from the end of 2018 onwards. These operating cost reduction targets assume that the Bank successfully delivers significant cost reductions during 2017 and 2018. In addition, the PRA has stated that, as a condition of the PRA's acceptance of the May

2017 Outlook on the Plan, the PRA expects, by the time of the Bank adopting its next five-year strategic plan, that the Bank will provide to the PRA a detailed cost:income strategy setting out how the Bank will achieve in the medium-term a competitive cost:income ratio in line with the Bank's peer group. The PRA has also stated its view that such a cost:income strategy will be critical to ensuring the success of the Plan and the future of the Bank.

The Bank's targeted cost reduction initiatives are focused on the following cost categories: people; third-party suppliers; premises; and IT. The Bank intends to make significant cost reductions in 2017 and 2018 to be delivered through:

- the planned removal of permanent, temporary and contractor roles;
- the renegotiation of third-party contracts, demand suppression and/or a change in the scope or standard of service provided by third-party suppliers;
- the rationalisation of the Bank's major occupancies as well as the closure of a further 10 branches, bringing the number of branches to 95 by the end of July 2017; and
- the simplification and rationalisation of the Bank's IT systems, applications and its supporting service model.

There is also a risk that, even if the Bank is successful in implementing the cost reduction initiatives in the Plan, the Bank's cost:income ratio will be reduced but may still be higher than its competitors.

There is a risk that these further cost reduction measures may not be sustainable or may not be achieved. Cost reductions necessary to achieve the Bank's strategy may increase the risk profile of the Bank, exposing it to legal or regulatory risk, and/or negatively impact core operations and service levels, which are critical to preserving the Bank's market share and increasing the Bank's income and net interest margin in line with the Bank's strategy.

There are therefore risks that if the Bank does not deliver its cost reduction initiatives targeted in its strategy and/or the Plan, it will fail to deliver its strategy, the Plan and/or, where applicable, the May 2017 Outlook on the Plan or that, even if it achieves its targeted cost reductions, the Bank does not grow its income and net interest margin in line with its targets, its costs relative to income will therefore not decrease and its cost:income ratios will not improve as planned and expected by the PRA and will continue to negatively impact its results of operation, financial condition and capital position and inhibit its targeted return to profitability.

17. ***Transformation project costs have been significantly higher than expected in the last three years. As the Bank has previously failed to meet its project cost targets, there is a risk that the Bank's project costs will be much higher than those targeted in the May 2017 Outlook on the Plan.***

The May 2017 Outlook on the Plan assumes the Bank will be able to deliver the remaining transformation programmes without material deviation from planned timescales and costs. The Bank is targeting a reduction in project costs to approximately £100 million for the year ending 31 December 2017 (year ended 31 December 2016: £310 million), and an increase to approximately £120 million of project costs for the year ending 31 December 2018, and thereafter project costs of approximately £50 million per annum over the remaining life of the Plan, which represents a significant reduction from the Bank's project costs of recent years. The Bank has experienced significant cost overruns when implementing complex large-scale transformation projects in the past. In addition, certain projects have not delivered the planned benefits. In the year ended 31 December 2016, the Bank's project costs included £81.9 million associated with the programme of work to transform its mortgage outsourcing service, which is no longer being progressed.

Furthermore, the Bank has a number of projects in the May 2017 Outlook on the Plan for 2017 and 2018 that are still in their infancy and more detailed plans and costs for such initiatives are being developed. As the Bank better understands the required scope of work and costs involved, there is a risk that the budgets that have been agreed and included in the May 2017 Outlook on the Plan will not be sufficient to complete these initiatives. In addition, known transformation programmes or new transformation programmes may require substantially greater resources than anticipated in the May 2017 Outlook on the Plan.

In addition, there are risks that the Bank may be unable to complete its transformation programmes when planned and that the programmes as a whole may cost significantly more than targeted, have a reduced scope for the same targeted costs, or deliver less benefits than planned. Failure to deliver any remaining or future transformation programmes to planned timelines and in line with the assumed cost could have a material adverse impact on the Bank's ability to implement its strategy and return to profitability, and have a material adverse effect on the Bank's business, financial condition, operating results and prospects. See paragraph 8.2 of Part 7 of this Circular for a description of the May 2017 Outlook on the Plan's re-phasing of project costs between 2017, 2018 and 2019.

18. ***The Bank is targeting sustainable profitability in the medium-term. The Bank has a history of statutory and operating losses. There are significant risks that the Bank may not return to profitability within that timeframe, or at all.***

The Bank has a history of incurring statutory and operating losses in each year since 2012. The Bank's statutory loss after tax for the year ended 31 December 2016 was £418.7 million. Although this loss is considerably less than the Bank's statutory loss after tax of £622.8 million for the year ended 31 December 2015, the loss remains significant. Furthermore, the Bank forecasts that it will make a statutory loss after tax of between £225 million and £250 million for the year ending 31 December 2017 (excluding the one-off transactional income statement impact of the Restructuring and Recapitalisation explained in the illustrative *pro forma* balance sheet set out in Part 8 of this Circular). The Bank is, however, targeting sustainable profitability in the medium-term. This target is neither a forecast nor a guarantee that the Bank will return to profitability in the medium-term, or at all. This target is premised upon various assumptions in the Plan and, where applicable, the May 2017 Outlook on the Plan regarding matters beyond and within the Bank's control and the Bank achieving the other targets in the Plan and, where applicable, the May 2017 Outlook on the Plan. There are a number of risks and uncertainties, including those set out in this Part 3, as to whether what will happen will correspond to those assumptions and that may cause the Bank's actual results of operations to differ significantly from those targeted and result in the Bank not returning to profitability when targeted, or at all. The most significant of these risks and uncertainties include, but are not limited to:

- whether the Bank meets its project cost targets by delivering the remaining transformation, remediation and change programmes already underway;
- whether the Bank meets its targets to reduce operating costs by implementing proposed cost reduction initiatives without material deviation from planned timescales and targeted cost reductions and meets its targets to reduce its cost base and improve its cost:income ratio;
- whether the Bank's operating costs continue to exceed its income;
- whether the Bank meets its increased income and net interest margin targets (for example, if base rates do not increase as soon or as much as forecast and assumed by the Bank in the May 2017 Outlook on the Plan) and whether competitive pressures reduce the Bank's market share in new business mortgage assets or other products (when the Bank has assumed in the Plan that its market share will be preserved) or do not enable the Bank's margins to increase as planned or regulatory pressures constrain the anticipated growth in business volumes;
- whether the Bank meets its targets in new business mortgage assets or other products as it risks losing market share to other banks, building societies, insurance company competitors and new "fin-tech" entrants;
- whether the Bank executes, as part of the Plan, an increase in its mortgage assets, which depends on improvements in its customer proposition and on the success of a limited number of intermediaries who also sell mortgages of the Bank's competitors;

- whether the Bank maintains access, at an appropriate cost, to liquidity and funding to fund the requisite level of asset origination targeted in the Plan;
- whether the Bank reverses decreases in its non-interest income through assumed increases in fees relating to transactions on BaCB current accounts and increased non-interest income, primarily from the commission received from general insurance referrals;
- whether the Bank may incur conduct or legal risk costs beyond its IBNI provisions or may be required to incur new costs as a result of regulatory change;
- whether the Bank may be required to make substantial additional pensions contributions beyond those currently expected;
- whether the Bank is able to retain current deposits and attract new deposits;
- whether the Bank is able to issue its targeted £250 million of Tier 2 debt on the assumed price provided for in the Plan and/or on acceptable terms;
- whether the Bank will be able to meet all regulatory capital and loss-absorbing requirements when planned and whether its assessment of any such future requirements will be accurate;
- whether the Bank can recognise significant deferred tax assets in the quantum or timeframe targeted; and
- whether there is a deterioration in general economic conditions and the UK housing market and/or whether the Bank faces systemic capital markets volatility.

The successful development and implementation of the Bank's strategy requires difficult, subjective and complex judgements, including those relating to a range of factors which are not within the Bank's control or influence, for example, forecasts of economic conditions. In addition, unanticipated events may adversely affect the Bank's profitability in future periods whether or not the assumptions in the Plan and, where applicable, the May 2017 Outlook on the Plan otherwise prove to be correct. There is, therefore, a risk that the timing or feasibility of the Bank's return to profitability could differ from those expressed or implied by any forward-looking statements or targets as a result of many factors and these differences could be material.

Accordingly, the Bank may not return to profitability when or in the amount targeted in the May 2017 Outlook on the Plan, or at all.

For further information see the risk factor entitled "*No dividends to be paid in respect of the A Shares in the near future*.", paragraphs 6 and 9 of Part 7 of this Circular for the Bank's 2017 Adjusted Loss Forecast and the Bank's outlook and longer-term targets as provided for in the Plan and, where applicable, the May 2017 Outlook on the Plan, respectively, including the principal assumptions upon which the Adjusted Loss Forecast and the Bank's target of sustainable profitability in the medium-term is made, and "*Forward-looking Statements*".

19. ***The Bank's earnings, net interest margins and credit losses have been adversely affected by factors such as the low Bank of England base rate, and may continue to be adversely affected for so long as one or more of these factors persist.***

The Bank's net interest margin and, consequentially, earnings are affected by the pricing on the lending products it offers to its customers and the cost of funding. The Bank's net interest margin has been adversely impacted by a number of factors which have negatively impacted the pricing of its lending products and the cost of its funds.

The very low level of the Bank of England base rate since March 2009 has contributed to a decline in the Bank's net interest margin, as funding costs rose relative to the base rate. The Bank of England base rate remained at 0.5 per cent. until August 2016 before dropping to 0.25 per cent. following the result of the UK's referendum to leave the European Union. The Bank's earnings and net interest margins have been adversely affected over this period due to a number of factors, including a prolonged period of low Bank of England base rates and competition in retail funding and lending markets, which constrain the ability of the Bank to generate capital organically, and may continue to be adversely affected for so long as one or more of these factors persist. A further impact of the low level of the Bank of England base rate for such a prolonged period of time is the unknown impact that this could have on credit losses. Rising interest rates would put pressure on existing and new borrowers whose loans are linked to the Bank of England base rate or LIBOR or the Bank's variable rates and who may have become accustomed to the current low interest rate environment. A significant portion of the Bank's outstanding residential mortgage loan products are potentially subject to changes in interest rates and there is limited relevant previous experience to assist in understanding how the market would react to a significant increase in interest rates and the subsequent uplift in repayments.

The Bank is targeting a widening of, and steady increase in, its net interest margin over the medium-term of the Plan, with increments of 10 basis points targeted per annum from 2018 onwards in line with forecast interest rate increases assumed to begin in 2018. A rise in the Bank of England base rate is the key enabler for this growth. Accordingly, if movements in the base rate do not follow those assumed by the Bank in the May 2017 Outlook on the Plan, it is likely that this will impact the future trajectory of the Bank's net interest margin. A failure to grow its net interest margin as planned could have a material adverse effect on the Bank's financial condition, operating results and prospects.

In preparing the Plan, the Bank used the market's forward implied view for market interest rates of base rate, swap rates, LIBOR rates and gilts, using a 10-day moving average on the market interest rates to smooth over any daily volatility. The 10-day moving average of the forward-looking market implied SONIA rates to 22 November 2016 were used (rounded to the nearest increment of 25 basis points), and these assumed a Bank of England base rate increase to 0.5 per cent. in May 2018, a further increase to 0.75 per cent. in June 2019, a rise to 1.0 per cent. in August 2020 and final rise to 1.25 per cent. in November 2021. The Bank used a third-party model to forecast certain macroeconomic variables, such as inflation, unemployment, GDP and HPI, as at August 2016. GDP is forecast at 1.4 per cent. for 2017 with recovery in outer years. Unemployment is assumed in the Plan to rise to 5.3 per cent. in 2017 before gradually declining from 2020 onwards. CPI is modelled in the Plan as rising to 2.9 per cent. in Q2 2017, and reducing to around 2 per cent. on average between 2018 and 2021. The Bank's base rate outlook has been adversely impacted since the November 2016 10-day average forward market implied rates used in the Plan. See paragraph 8.2 of Part 7 of this Circular for a description of the May 2017 Outlook on the Plan which reflects the more recent adverse base rate outlook. If the Bank's assumptions prove to be incorrect, there is a risk that this would impact the Bank's business, operating results, financial condition, prospects and its ability to achieve the targets set out in the Plan and/or the May 2017 Outlook on the Plan.

20. ***The Bank's ability to achieve its net interest margin targets assumes that the Bank preserves its market share over the life of the Plan. The Bank faces competition in all of the core markets in which it operates. There is a risk that the Bank may lose market share to its competition and be unable to achieve its net interest margin and new mortgage business origination targets, which could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.***

Competition in the UK personal financial services market may adversely affect the Bank's operations. The Bank competes mainly with other providers of personal financial services, including other banks, building societies and insurance companies and, increasingly, new "fin-tech" entrants to the market, and operates in an increasingly competitive UK personal financial services market. Each of the main personal financial services markets in which the Bank operates is mature and slow-growing, such that growth requires taking market share from competitors. This places elevated focus on price and service as the key differentiators, each of which carries a cost to the provider. The quality of the Bank's products and systems, including distribution and IT, in turn impact price and service. If the Bank is unable to match its competitors in these respects it risks losing customers to its competitors, which may adversely affect its business and prospects and consequently its ability to meet its business plan in the intended four to five-year timescale. The Bank's heavy reliance on mortgage revenues to drive income may increase its susceptibility to competitive risks.

Competition could result in the Bank losing existing and potential new customers and, therefore, not preserving its market share as assumed in the Plan in a number of situations, particularly where:

- the Bank is not successful in strengthening its core proposition and brand positioning with retail and SME customers;
- the Bank is unable to match its competitors, for example, in the quality or scope of its product offering and customer service and the provision of additional services such as mobile banking, and in keeping up with consumer demand, regulatory and technological changes;
- the Bank's customer service levels were perceived to be negatively impacted by the implementation of its strategy, including the impact of the Bank's cost reduction measures on service delivery levels, customer service and satisfaction, or were perceived by the market to be only in line with, or materially below, those of the Bank's competitors;
- reputational risk arises in respect of the Bank;
- a loss of customers, or deteriorating customer relationships, as a result of these or other factors, could result in the Bank losing customers' liability/asset balances to competitors, which may in turn have an adverse effect on revenue;
- there remains significant competition for market share across the Bank's retail product lines, and there is a risk that a failure to develop the core proposition and other differentiating factors will result in growth plans reliant on pricing to win market share, which will impact margins;
- given the Bank's cost reduction targets, there is a risk that insufficient investments in its systems (including, in particular, its credit risk systems) will be made relative to regulatory requirements and/or its competitors' level of investment, which will impact its ability to increase market share;
- there is a risk that levels of marketing investment (required to grow customer awareness and consideration) are insufficient;
- there are similar or increased levels of investment from the Bank's competitors;
- as the Bank is seeking to reduce its exposure to commercial real estate lending, but does conduct some lending with SMEs, there is a risk that its competitive position will be damaged in this particular market segment;
- other institutions having greater access to the Government's Term Funding Scheme (the "**Term Funding Scheme**") funds that the Bank does not enjoy (on commercially attractive terms) or other similar initiatives in the future, the result being that the Bank might not be able to economically match the pricing of those competitors in the mortgage market;
- competition for the highest quality mortgages is intense, putting downward pressure on returns available for the lowest risk-weighted mortgage assets;
- risk of competition from a new bank competitor (including, increasingly, new "fin-tech" entrants), which could, for example, offer more innovative and more customer- or user-experience focused services;
- any failure to attract new, or retain existing, customers or to maintain the Bank's market share may result in the loss of the Bank's customer asset and liabilities balance to its competitors, which may in turn impact the Bank's ability to deliver its strategy. See the risk factor entitled "*Reputational risk could cause harm to the Bank, its business, operating results, capital position, financial condition, prospects and ability to meet targets, including a return to*

profitability, and question the Bank's commitment to co-operative values and ethics" for further information; and

- the occurrence of any of the above situations could materially adversely affect the Bank's business, operating results, financial condition and prospects.

Further impacts on the retail savings market are expected from the Term Funding Scheme, where retail banks have access to lower-priced sources of funding in order to support increased lending.

The Bank is eligible to participate in the Term Funding Scheme, but not on commercially attractive terms. The Bank could, therefore, face pricing pressure on its products from competitors who are able to pass on the benefit of access to the scheme. These factors are expected to continue over the medium-term, whilst margin widening across the industry is expected if the Bank of England base rate increases as assumed in the Plan (driven by the 10-day moving average of the market forward-looking implied SONIA rates to 22 November 2016) (rounded to the nearest increment of 25 basis points) and yield curves steepen across the life of the Plan. The Bank's base rate outlook has been adversely impacted since the November 2016 10-day average forward market implied rates used in the Plan. See paragraph 8.2 of Part 7 of this Circular for a description of the May 2017 Outlook on the Plan which reflects the more recent adverse base rate outlook. If the Bank's net interest margin were to remain flat or materially deviate from the Plan, this could have a material adverse effect on the Bank's financial condition, operating results and prospects.

21. ***The Bank is exposed to a number of conduct and legal risks. The Plan assumes no new categories of conduct and legal risk provisions and no material increases in conduct and legal risk provisions charged during the life of the Plan. There is a risk that the Bank's conduct and legal risk provisions will be significantly higher than assumed in the Plan, which could have an adverse effect on the Bank's operating results, financial condition and prospects and the Bank's ability to deliver its strategy.***

The Bank is exposed to many forms of legal and regulatory risk. The Bank is exposed to the inherent risks relating to the mis-selling of financial products, acting in breach of regulatory principles or requirements and giving negligent advice or other conduct determined by the Bank or the Authorities to be inappropriate, unfair or non-compliant with applicable law or regulations. As part of its turnaround strategy to identify and resolve outstanding liability issues, the Bank commenced a structured risk-based assessment of its products of which the primary focus was the discovery and remediation of existing and new conduct and legal issues (the "**Structured Risk-based Remediation Programme**"). Although the Bank has substantially completed this review and the legacy conduct issues identified as part of that structured risk-based assessment have been substantially remediated and/or appropriate provisions raised, there is a risk that further or new issues or breaches will be identified or emerge resulting in new provisions being raised. In addition, in the ordinary course, the Bank may identify conduct issues resulting from systems and process weaknesses which could result in an adverse impact on the Bank's reputation, brand, customers and, if perceived as a systemic or pervasive issue, could result in further investigations or enquires by the Bank's regulators and furthermore could have a material adverse impact on the Bank's business, operating results, financial condition and prospects.

Since 2011, the Bank has provided almost £1 billion for conduct risk issues and, as at 31 December 2016, the Bank had utilised approximately £800 million of this provision with £169 million remaining. The overall conduct risk provision is split between PPI (including *Plevin* – see below) and other issues.

The Bank has made provision for a total of £460 million for PPI to date, and utilisation of the provision has reduced each year since 2012, with a £90 million provision remaining as at 31 December 2016. Of the approximately £510 million relating to other conduct and legal issues, £430 million has been utilised as at 31 December 2016, with a significant majority of such utilisation having occurred in the year ended 31 December 2015 and in the year ended 31 December 2016, as the Bank focused on redressing customers for breaches of the Consumer Credit Act 1974, as amended

("**CCA**"). The £169 million of remaining provisions (which includes the £90 million remaining PPI provision) represents the Bank's best view of the remaining redress due to, and the costs required to remediate customers for known conduct risk issues. The risk exists that the actual provision requirements from known conduct risk issues exceed those currently provided for by the Bank if any of the assumptions currently employed by the Bank change adversely in the future.

The Bank, since 2014, has conducted an annual product review which focuses on retail and business banking products and services, and related terms and conditions and customer marketing material. This product review has, to date, excluded certain products including those within the Optimum portfolio.

As a result, there is a risk that unidentified issues requiring rectification or remediation may emerge. In addition, the Bank's operational structure and processes may lead to limitations in available information and may hinder a complete or adequate view of product risk and, accordingly, hinder the identification of potential conduct issues.

In addition, there is a risk that products have not been implemented and/or are not operating as customers have been led to expect. Those areas which have specifically not been fully covered by the Bank's annual product review are: (i) interest calculation in accordance with the Bank's terms and conditions; (ii) customer correspondence; (iii) documentation issued that has not been reviewed; (iv) the application of limits and eligibility criteria in respect of certain product features; and (v) charges applied to customers' accounts in accordance with the Bank's tariffs. Furthermore, certain savings and mortgages terms and conditions have not been updated for a number of years and a review of these is currently underway. The oversight model in relation to customer correspondence is unclear and this may result in inaccurate communications with customers resulting in further conduct risk. The terms and conditions of mortgages were last reviewed in 2014 and covered those relating to on-sale mortgages under the Britannia and Platform brands. The next review of mortgage terms and conditions commenced in July 2017. This will again cover the current terms and conditions applying to on-sale mortgages under the Britannia and Platform brands but will extend also to those used for transactions by existing borrowers (who port their mortgage to a new property and transfers of equity) on the Bank brand and Optimum back-book mortgage portfolios.

Examples of conduct and legal risk faced by the Bank include:

Mis-selling and unauthorised transactions

- There are a number of areas where the Bank has previously sustained financial and reputational damage due to conduct-related matters and where consequences may endure longer than anticipated in the Plan. There is a possibility that the Bank may face financial and reputational damage in these areas in the future or where new matters may subsequently emerge, such conduct-related matters may have an impact on the Bank. Past conduct-related matters include (amongst others): (i) the alleged mis-selling of financial products (including PPI), including as a result of having sales practices and/or reward structures in place that are determined to have been inappropriate; (ii) early repayment charges ("**ERC**"); (iii) the processing of first payments on certain mortgages; (iv) the mis-selling of interest rate swaps; (v) interest rate changes made without proper legal and/or commercial justification; and (vi) the alleged mis-selling of packaged current accounts. Any such conduct-related matters may have an adverse effect on the Bank, including: (i) disciplinary action (including significant fines); (ii) requirements to amend sales processes, withdraw products or provide restitution to affected customers; and (iii) an adverse impact on future revenues from affected products, all or any of which could result in the incurrence of significant costs, may require provisions to be recorded in the Bank's financial statements, and could adversely impact future revenues from affected products.

- For a number of years, the Bank did not have a centralised document production facility, accordingly, there is a risk that historical commercial lending documentation may be defective and covenants may, therefore, be potentially unenforceable and certain breaches under such documentation not actionable.

- For a number of years, the Bank, along with many other financial services providers, sold PPI alongside mortgage and non-mortgage credit products. The Bank stopped selling unsecured loan PPI in January 2009, credit card PPI in November 2009 and mortgage PPI in March 2012. However, products still exist within the Bank which will include an element of PPI from historical sales. In line with industry practice, provisions have been made in respect of potential customer compensation claims relating to historical mis-selling of PPI. Claims are investigated on an individual basis and, where it is found that the Bank mis-sold PPI to customers (based on the FCA's policy statement 10/12 dated August 2010, which detailed how the FCA expects banks to investigate PPI complaints), compensation is paid to customers.

- In November 2014, the Supreme Court handed down a decision in *Plevin v Paragon Personal Finance Ltd [2014] UKSC 61*. The decision concerns the disclosure of commission amounts received in respect of sales of single premium PPI. The decision has a potential impact on the number of the Bank's customers who may have a claim for PPI redress and the treatment of prior rejected complaints.

- In March 2017 the FCA announced (in its policy statement 17/3) that PPI claims will be time barred after 29 August 2019. The FCA has also announced that it will require firms pro-actively to contact customers whose PPI complaints had previously been rejected by the Bank to advise them of the existence of the *Plevin* judgment referred to above. The Bank took the proposed time-bar into account within the provision raised in the Bank's Annual Report and Accounts 2016, alongside industry claims experience, and the published views and requirements of the FCA (which, for the avoidance of doubt, are not specific to the Bank), the aforementioned requirement to contact customers whose PPI complaints had previously been rejected is a new requirement that was not known and therefore not included. Total PPI provisions of £459.8 million have been taken as at 31 December 2016 (£423.8 million as at 31 December 2015). As at 31 December 2016, the Bank had an unutilised provision of £90.4 million (31 December 2015: £87.0 million) in respect of potential customer redress and costs relating to past sales of PPI. Forecast future complaint volumes are difficult to predict; however, the Bank has seen an increase in complaints between February and April 2017 which has since reduced and is now running at approximately 10 per cent. above the 2016 average. The Bank currently estimates a potential net incremental conduct risk charge of approximately £5 million in 2017 (subject to further external and internal review and approval) driven by an increase of approximately £9 million relating to PPI and the requirements of the FCA's policy statement 17/3, offset in part by small provision releases from other conduct risk categories. This may continue to increase, remain constant or decline more steadily. In particular, the impact of the FCA's communications campaign on future complaint volumes is unknown and, whilst the Bank has utilised information provided by the FCA in June to review its forecasts of future complaint volumes and has increased operational resources to provide additional resilience to deal with higher than forecast volumes of complaints during the key media activity of the campaign, the Bank cannot be certain that complaint volumes will not exceed forecasts. The recent introduction of the new online PPI complaint system will also make it easier for consumers to contact the Bank. A claims management company has recently issued judicial review proceedings challenging the FCA's proposed time-bar. It is not possible to assess at present whether this will be successful. Any change in the FCA's current approach, including as a result of this or other judicial reviews, such as any further extension of the period covered by the time-bar or further requirements for proactive contact with customers, could have a material impact on the financial condition of the Bank, and there is a risk of greater scrutiny and/or regulatory action from the FCA.

- As well as PPI, the Bank continues to monitor developments in product-related areas that attract increased focus from regulators, the courts and the Financial Ombudsman Service (the "**FOS**"), such as ERCs in both commercial and secured lending and variation of certain product terms and conditions. To date, the Bank has seen a small number of complaints at the FOS in some of these areas. Changes in the approach to any of these issues in the market and/or increased complaints volumes could adversely affect the Bank.

Mortgages

- The Bank, in selling regulated mortgages, must adhere to specific guidelines, principles and regulations. The Bank outsources its mortgage origination system and servicing operations but remains liable for the mortgages originated through such outsourcing model.

- Following the Structured Risk-based Remediation Programme, the Bank has identified further issues and defects in certain of its historical mortgage documentation which raise legal and conduct risks. As at 31 December 2016, the Bank held a provision of approximately £20.1 million for conduct issues in relation to miscalculation of monthly mortgage payments resulting from the misconfiguration of mortgage systems affecting certain mortgage books largely acquired at the time of the merger with Britannia, as well as in relation to unauthorised consent to lets on the Optimum portfolio. There is a risk that such provisioning may prove inadequate if the actual costs of remediation and redress, and any additional costs of enforcing affected mortgages, are higher than currently estimated or that the assessment of the impact of such defects proves to be incorrect or incomplete. Since 31 December 2016, further issues have been identified which arise from incidences where customer terms and conditions have either not been issued or where the Bank's mortgage systems do not correctly operate in accordance with customer terms and conditions.

- The FCA issued its finalised guidance on 24 April 2017 regarding "The fair treatment of mortgage customers in payment shortfall: impact of automatic capitalisations" ("**FG 17/4**"). FG 17/4 sets out a possible framework firms can use when providing customer remediation relating to correcting the effects of automatic capitalisation of payment shortfalls and, where appropriate, paying any compensation that is due to the customer. The Bank holds a provision of £6 million with regards to remediation and is working to conclude its remediation programme by 30 June 2018 (as required by the FCA). There is a risk that remediation costs, including the cost of paying any compensation to customers, may exceed the £6 million provision.

- The Bank initiated a redress programme in respect of various breaches of mortgage conduct of business rules and is the subject of a skilled persons review into potential detriment to its mortgage customers arising from poor arrears handling. The Bank has substantially completed the recommendations from this review and has implemented enhanced policies and processes which are designed to deliver improved customer outcomes. The outcome of the final review is not yet finalised but, whilst the risk of further enforcement action by the FCA is considered to be largely mitigated, there is a risk that this will not be the case, and there remains a risk that the Bank or the FCA may identify further issues.

- Mortgages bulk redress and mortgages rectification programmes have sought to address issues relating to: (i) arrears fees and charges; (ii) incorrect application of terms and conditions; (iii) early repayment charges; (iv) discount rate expiry; (v) Platform first payments; (vi) issues arising in relation to FG17/4 and the auto capitalisation of arrears; and (vii) CCA further advances. Furthermore, mortgage monthly repayment miscalculations continue to be remediated. The Bank has taken provisions totalling £127.5 million for issues (i) to (vii) and mortgage monthly repayment miscalculations described above of which £28.2 million remained unutilised as at 31 December 2016, this includes anticipated costs pursuant to redress and its delivery, arising in connection with FG17/4. There is a risk that the costs in rectifying issues (i) to (vii) above as well as in relation to mortgage monthly repayment miscalculations may exceed the £127.5 million provision.

- The Plan targets growing the Bank's net core customer assets by approximately £1 billion in each year of the Plan, primarily driven by the Bank's Platform brand, including the introduction of retention capability together with other initiatives aimed at maintaining market share. In order to achieve the increased targets, the Bank will require investment and remediation of its mortgage systems. There is a risk that the pressure to achieve the targeted increases without an adequate level of investment in its mortgage systems infrastructure may create new conduct, legal and regulatory risks. Should the Bank not comply with applicable requirements in relation to mortgage selling in the future and the FCA were to take enforcement action, it could be required to cease this activity until such time as it can demonstrate compliance with the relevant rules and guidance.

CCA

- In the event that the highly technical requirements of the CCA are not precisely complied with, the Bank is exposed to the risk that its agreements with customers are not enforceable without the benefit of a court order and/or that during a period of non-compliance the Bank's customers are not liable to pay interest or default charges. The Bank has identified that it has breached certain provisions of the CCA and has therefore been subject to these risks. The Bank has recognised provisions totalling £259.5 million in respect of the total expected cost to the Bank of potential customer redress relating to the above alleged failings, following near-completion of the programme £16.7 million remained unutilised as at 31 December 2016, with the remainder of the provision required to continue to work to develop a solution to address and avoid accounts becoming non-compliant again. As at 31 December 2016, the Bank had a provision of £16.7 million (31 December 2015: £123.1 million) in respect of breaches of the technical requirements of the CCA.

- The Bank has largely completed the remediation of historical breaches of the CCA, including the payment of appropriate redress to customers. Significant work continues to be undertaken on the underlying issues which led to such historical CCA breaches. If this work is not fully completed or if other breaches of the CCA emerge, then there is a risk of further or continued breaches of the technical requirements of the CCA. In certain circumstances, the Bank may be unable to rectify the underlying issues accurately or at all, which may lead to continuing non-compliance with the CCA.

Given the high level of scrutiny regarding financial institutions' treatment of customers and business conduct from regulatory bodies, there is a risk that aspects of the Bank's current or historical business may be determined by the PRA, the FCA, HM Treasury, the FOS, the CMA or other regulatory bodies or the courts as not being conducted in accordance with applicable laws or regulations (or, in the case of the FOS, in accordance with what is fair and reasonable in the opinion of the FOS). If the Bank fails to comply with any relevant laws or regulations, there is a risk of an adverse impact on its business due to sanctions, fines or other actions imposed by these regulatory authorities. There is also a risk of greater scrutiny and/or intervention from regulators, further regulatory action and/or litigation.

The Bank's conduct and legal risk provisions as at 31 December 2016 include £8.1 million relating to IBNI. There is a risk that the Bank becomes exposed to significant new conduct or legal risks which will require additional provisions in excess of this amount. As described in paragraph 8.2 of Part 7 of this Circular, the Bank is currently estimating a potential net incremental additional conduct risk charge of approximately £5 million in 2017 (subject to further external and internal review and approval) driven by an increase of £9 million relating to PPI and the requirements of the FCA's policy statement 17/3 described above offset in part by small provision releases from other conduct risk categories. While progress has been made in resolving conduct issues, there is a risk that the Bank's provisions – whether in aggregate, specific or IBNI – are insufficient, or that already identified issues or further issues may require significant further or new provisioning and/or significant redress and remediation costs, which could have a material adverse effect on the Bank's business, operating results, financial condition and prospects and inhibit its targeted return to profitability.

22. ***The Bank may have to recognise significant additional pension liabilities in its accounts, deduct accounting deficits from its CET1 capital and increase Pillar 2a requirements where accounting deficits arise which may have a material adverse effect on its business, financial condition, operating results and prospects.***

The Bank participates in Pace (whose principal employer is the Co-operative Group), which provides benefits on both defined contribution and defined benefit bases. The Pace defined benefit section is closed to accrual (albeit with certain benefits maintaining a salary link). The Bank is the sole substantive sponsor of the Britannia Scheme. The Britannia Scheme is a scheme providing defined benefits which is closed to accrual. For further details about Pace and the Britannia Scheme, see paragraphs 14.1 and 14.2 of Part 16 of this Circular.

Pension costs in respect of the Britannia Scheme are accounted for on a defined benefit basis such that any accounting surplus or deficit remains on the Bank's balance sheet. The Bank currently accounts for its pension costs in respect of the defined benefit section of Pace on a defined contribution basis (as there is insufficient information available to consistently and reliably identify the Bank's share of Pace liabilities) such that the Bank's contributions to Pace are recognised as an expense on the Bank's income statement as incurred. The Bank would have to account for defined benefits in the Bank Section on a defined benefit basis following implementation of the Pace Pensions Sectionalisation. The Bank would also have to account for a share of Pace defined benefits on a defined benefit basis in the absence of the Pace Pensions Sectionalisation if sufficient information becomes available to consistently and reliably identify the Bank's share of Pace defined benefit liabilities. In addition, in the absence of the Pace Pensions Sectionalisation and if the Bank is required to account for defined benefits in the Bank Section on a defined benefit basis, the Bank would not have an unconditional right to a refund of surplus upon wind-up of Pace (unless the Pace rules were to be amended with the agreement of Group and the Pace Trustee to give such a right), which would result in the Bank not being able to recognise a share of any Pace accounting surplus on its balance sheet and any committed schedule of deficit recovery payments payable by the Bank being an upfront deduction from the Bank's CET1 capital.

Currently, both the Britannia Scheme and Pace have an IAS19 surplus (and such surplus does not increase CET1 regulatory capital); however, should the IAS19 valuation of the Britannia Scheme or, if and when the Bank accounts for Pace on a defined benefit basis, of Pace/the Bank Section deteriorate and move into an IAS19 accounting deficit, the Bank would be required to deduct the IAS19 deficit from its CET1 capital. As such, there is a risk that the Bank will have to recognise significant additional liabilities and CET1 regulatory capital deductions in respect of the Britannia Scheme and/or Pace in its accounts. In addition, the Bank is required to make a Pillar 2a assessment for pension risk, including consideration of the stressed IAS19 position. An IAS19 deficit would become an increased deficit under an IAS19 stress, potentially increasing the Bank's Pillar 2a requirement. In addition, there is a risk that in the future amendments will be required to the Britannia Scheme and, if the Pace Pensions Sectionalisation is implemented, the Bank Section rules to support an analysis that the Bank has an unconditional right to a refund of surplus upon wind-up of the Britannia Scheme or the Bank Section and failure to secure the Britannia Trustee's or the Pace Trustee's agreement to such amendments would result in the Bank not being able to recognise a share of any Britannia Scheme or Bank Section accounting surplus on its balance sheet and any committed schedule of deficit recovery payments being an upfront deduction from the Bank's CET1 capital.

These potential accounting and CET1 and Pillar 2a capital implications could have a material adverse effect on the Bank's business, operating results, financial condition, prospects and regulatory capital position.

23. ***The Bank may become obliged to provide additional security in respect of, or make large one-off or ongoing payments to its pension schemes, or pension schemes to which it is connected and/or associated which may have a material adverse effect on its business, financial condition, operating results, prospects and regulatory capital position.***

Funding/security risks relating to the Britannia Scheme

There is a risk that following the next triennial valuation of the Britannia Scheme (to be undertaken as at 5 April 2017) or following another future valuation the Bank will be required to pay higher contributions and/or offer additional security (beyond the security already provided for in the form of £165.1 million AAA rated retained Warwick Finance Two securitisation notes, with a 17 per cent. haircut) as a result of any deterioration in the Britannia Scheme's funding position. A deterioration in a pension scheme's funding position might arise from a higher assessment of the scheme's liabilities (for example a pension scheme trustee might seek to use more conservative assumptions to value liabilities in a future valuation and the assessment of liabilities is highly sensitive to assumptions, *inter alia*, on life expectancy, inflation, discount rates and expenses, including the Pension Protection Fund levy) and/or as a result of the investment performance of a pension scheme's assets (which may be impacted by any changes made to the investment strategy of such assets from time to time by a pension scheme's trustee). Where the value of the security assets is less than the Britannia Trustee's maximum potential claim pursuant to the security, the Bank will be obliged to top-up the security assets in the charged accounts accordingly. The security will become enforceable in its entirety when there is an event of default, which includes insolvency events as defined in section 121 of the Pensions Act 2004, bank insolvency, bank administration, the Bank ceasing to carry on business, un-remedied breaches by the Bank of the security arrangement, un-remedied misrepresentations under the security arrangement by the Bank, and events which make the security arrangement ineffective (for example where the Bank's obligations in relation to the security arrangement become unlawful or are repudiated).

The valuation basis, deficit funding and security arrangements agreed in respect of Pace might also prompt the Britannia Trustee to seek a revised approach to its own valuations, deficit funding and security arrangements.

There is a risk that the Bank may not have sufficient capital to make significant cash contributions and may not have enough acceptable securities available to support the security. There is a risk that following the next or any future actuarial valuation, the Bank will be required to pay higher contributions and/or offer additional security as a result of any deterioration in the scheme funding position. There is a risk that an event of default will occur, resulting in the security becoming enforceable in its entirety.

Funding risks relating to Pace if the Pace Pensions Sectionalisation is not implemented on the terms of or when proposed in the Pace Heads of Terms or at all

If the Pace Pensions Sectionalisation is not implemented on the terms of or when proposed in the Pace Heads of Terms or at all, there is a risk that, following the triennial actuarial valuation of Pace as at 5 April 2016 or a future actuarial valuation, and as a result of any deterioration in the scheme funding position, the aggregate rate of deficit contributions that the sponsoring employers are required to make to Pace could increase, which could result in the Bank paying higher deficit contributions. There is also a risk that the proportion of employer deficit contributions to Pace paid by the Bank while it continues to participate in Pace on a non-sectionalised basis could increase. The Pace Trustee might also seek security from the Bank.

Pace is currently operated as a "last-man standing" scheme and, accordingly, whilst the Bank participates in Pace as a non-segregated scheme (i.e. prior to implementation of the Pace Pensions Sectionalisation), the Bank could become solely responsible for funding Pace if all employers other than the Bank (including the Co-operative Group) exit Pace or become insolvent. The level of the ongoing funding burden for the Bank in such circumstances would depend on the funding position of Pace at that time, including the extent to which the other employers have paid their section 75 debts arising on exit/insolvency.

There is also a risk that the wind-up of Pace could occur in circumstances where the Bank has no ability to prevent such wind-up, for example in the event that the Co-operative Group goes into liquidation and the Pace Trustee does not agree to the Bank taking over the role of principal employer in relation to Pace in place of the Co-operative Group. In the event of Pace winding-up a section 75 debt would become payable by the Bank. Such liability is calculated by reference to the cost of buying out Pace's liabilities in the insurance market, which commonly results in a much greater liability than the ongoing deficit contributions payable by an employer. The Bank's section 75 debt in respect of the Pace Pension Scheme would currently be expected to be several hundred million pounds (and could increase significantly if other employers become insolvent and are unable to pay their section 75 debts in full). A section 75 debt liability for the Bank could therefore have a material adverse effect on the Bank's business, operating results, financial condition, prospects and regulatory capital position.

A section 75 debt would also arise in respect of the Bank if the Bank ceases to employ active members of Pace (in circumstances where the Pace Pensions Sectionalisation has not been implemented) whilst other employers continue to employ active members of Pace. However, the Co-operative Group has agreed with the Bank not to require the Bank to cease to participate in Pace without the Bank's prior written approval except: (i) where the Bank is in breach of the rules of Pace and does not remedy the breach within a reasonable time (to be agreed between the Co-operative Group and the Bank and not to be less than 90 days) of being notified of the breach, (ii) where required by law or (iii) following the Co-operative Group giving the Bank at least 6 months' prior written notice where all other employers cease participation at the same time so that such cessation does not trigger a section 75 debt payable by the Bank. A section 75 debt could also arise in respect of the Bank on the occurrence of an "insolvency event" as defined in section 121 of the Pensions Act 2004 in relation to the Bank.

Funding/security risks relating to Pace if the Pace Pensions Sectionalisation is implemented

If the Pace Pensions Sectionalisation is implemented, the Bank will be solely responsible for funding the Bank Section of Pace. The Pace Heads of Terms provides that the recovery plan put in place for the Bank Section immediately after the Pace Pensions Sectionalisation will require the Bank to make deficit payments of £12.5 million per annum payable in advance in respect of each of the calendar years 2018 to 2022 inclusive and £7.5 million per annum payable in advance in respect of each of the calendar years 2023 to 2027 inclusive (and which will be subject to revision at future actuarial valuations in accordance with scheme funding legislation). The recovery plan will be backed by a security arrangement pursuant to which the Bank will charge in favour of the Pace Trustee (unless cash or gilts are used as the security assets) certain AAA rated debt securities which will be subject to haircuts described more fully in the description of how an "asset value" will be calculated in paragraph 14.1 of Part 16 of this Circular. The Pace Trustee's maximum claim in the event the security becomes enforceable will initially be at a level of £216 million (being the indicative deficit for the Bank Section on the agreed "low risk target basis" had the Pace Pensions Sectionalisation taken place as at 31 March 2017), and will reduce in line with deficit payments made by the Bank (but subject to upward revision up to a maximum of £216 million before 1 January 2028 and a maximum of £250 million on or after 1 January 2028 in the event of increased deficit contributions becoming payable which exceed the then maximum claim following later valuations). If the Co-operative Group still has potential "last-man standing" risk for the Bank Section on 1 January 2028, the Pace Trustee's maximum claim will increase to £250 million, reducing in line with deficit payments made by the Bank from 1 January 2028. Where the value of the security assets is less than the Pace Trustee's maximum potential claim pursuant to the security, the Bank will be obliged to top-up the security assets in the charged accounts. The security is enforceable if the Bank fails to pay a contribution to the Pace Pension Scheme, but only to the extent required to discharge the unpaid amounts. The security will become enforceable in its entirety where there is an event of default, which will include insolvency events in relation to the Bank (which includes an "insolvency event" as defined in s121 of the Pensions Act 2004, bank insolvency, bank administration, where the Bank is unable to pay its debts as and when they fall due or fails or admits in writing its inability generally to pay its debts as they become due, certain insolvency proceedings in respect of the Bank or where the Bank makes a general assignment, arrangement or composition with or for the benefit of its creditors), the Bank ceasing to carry on business, un-remedied breaches by the Bank of the security arrangement, unremedied misrepresentations by the Bank under the security arrangement, and events which make the security arrangement ineffective (e.g. the Bank's obligations in relation to the security arrangement become unlawful or are repudiated).

There is a risk that the Bank may not have sufficient capital to make significant cash contributions and may not have enough acceptable securities available to support the security. There is a risk that following the next or any future actuarial valuation of the Bank Section, the Bank will be required to pay higher contributions and/or offer additional security as a result of any deterioration in the scheme funding position. There is a risk that an event of default described above will occur, resulting in the security becoming enforceable in its entirety.

Risk of intervention by the Pensions Regulator

The Pensions Regulator has the power to require an employer of a defined benefit scheme or a person connected or associated with such employer to make a contribution to or provide financial support for that scheme in certain circumstances. The Pensions Regulator also has the ability to initiate the process for exercising such "moral hazard" powers for up to six years after a targeted entity has ceased to be connected or associated with such an employer. If the Pensions Regulator exercised its powers against the Bank in relation to Pace (including in relation to the Bank Section and/or the Co-operative Group Section if Pace Pensions Sectionalisation is implemented), the Britannia Scheme or any defined benefit pension scheme within the Co-operative Group, obligations imposed by the Pensions Regulator could have a material adverse effect on the Bank's business, operating results, financial condition, prospects and regulatory capital position. Formal clearance has been obtained from the Pensions Regulator in relation to the transactions expected to be implemented pursuant to the Pace Heads of Terms (and on the basis of completion of the Restructuring and Recapitalisation before 19 October 2017), which substantially mitigates the risk of the Pensions Regulator exercising its "moral hazard" powers against the Bank in relation to the Co-operative Group Section following Pace Pensions Sectionalisation.

Trustees of defined benefit schemes are subject to a legal requirement to carry out formal funding valuations at least every three years and details of each valuation need to be submitted to the Pensions Regulator. The Pensions Regulator also has the power to intervene in valuations if it wishes, including determining a scheme's deficit and deficit contributions payable. In May 2017, the Pensions Regulator announced it intends to take a tougher approach where trustees and employers, as part of its drive to raise governance standards, fail to agree a valuation and schemes do not without reasonable cause submit their valuations on time. The Pensions Regulator announced it will take enforcement action where necessary and will consider the range of powers available to it, including issuing orders to improve behaviour, appointing independent trustees, and issuing penalties for non-compliance.

The Pensions Regulator has the power to direct that a pension scheme be wound up if satisfied that, *inter alia*, wind-up is necessary in order to protect the interests of the generality of members of the pension scheme. Section 75 debts become payable where a pension scheme winds up. As at 31 December 2016, the Bank's combined section 75 debts in respect of Pace and the Britannia Scheme were estimated to be approximately £1.1 billion net of the Britannia Trustee's maximum claim of £137 million pursuant to the security arrangement in place for the Britannia Scheme (although this figure is an estimate, based on an independent valuation prepared for the Bank at 31 December 2016 and, therefore, could materially change).

Risks where increased contributions and/or security as outlined above are required

There is a risk that the Bank may not have sufficient acceptable securities available to provide increased security, or that by pledging additional acceptable securities the Bank removes a potential source of liquidity since the securities cannot then be sold to generate liquidity. If the Bank cannot provide increased security, the pension scheme trustee is likely to seek to address more quickly the increased deficit through cash contributions.

Increased cash contributions would erode the Bank's CET1 capital, and the effect on profits and distributable reserves could have a negative credit rating impact and a negative impact on the Bank's ability to attract future capital.

The provision of additional security and/or any increase to the level of the Bank's pension deficit contributions could have a material adverse effect on the Bank's business, financial condition, operating results, prospects and regulatory capital position.

24. ***The Bank's agreement with the Co-operative Group and the Pace Trustee on the Pace Pensions Sectionalisation is subject to a number of risks and may not be implemented on the terms currently envisaged or at all.***

The only condition left to be satisfied for implementation of the Pace Pensions Sectionalisation is completion of the Restructuring and Recapitalisation. If this condition is not met, the Pace Pensions Sectionalisation will not be implemented. The Pace Heads of Terms will also terminate (such that the Pace Pensions Sectionalisation will not be implemented) in the event of, prior to the Pace Pensions Sectionalisation taking place, Bank insolvency, Bank resolution or the occurrence of a corporate transaction as an alternative to the Restructuring and Recapitalisation.

See the paragraph entitled "*Funding risks relating to Pace if the Pace Pensions Sectionalisation is not implemented on the terms of or when proposed in the Pace Heads of Terms or at all*" of the risk factor entitled "*The Bank may become obliged to provide additional security in respect of, or make large one-off or ongoing payments to its pension schemes, or pension schemes to which it is connected and/or associated which may have a material adverse effect on its business, financial condition, operating results, prospects and regulatory capital position.*" in this Part 3. See also the risk factor entitled "*The implementation of the Restructuring and Recapitalisation faces a number of significant risks and relies on the Members' Scheme (including the Members' Equity Subscription) and the Creditors' Scheme (including the Scheme Creditors' Equity Subscription) and the Consent Solicitation being executed successfully and the Resolutions being passed. If the Restructuring and Recapitalisation does not succeed, the Bank believes the most likely outcome is that the Ordinary Shares and the Subordinated Notes will be subjected to a mandatory write-down, either as a preliminary step to, or in the course of the Bank's entry into, Special Resolution. In such a scenario, the Bank believes that Shareholders will receive no recovery in respect of the Ordinary Shares that they hold, and that Subordinated Noteholders will receive no recovery in respect of the Subordinated Notes that they hold.*" in this Part 3.

Risks relating to the implementation agreement and to timing

Although the Sectionalisation Parties have agreed to enter into an implementation agreement by 31 December 2017 setting out more detailed terms of the Pace Pensions Sectionalisation (where the Sectionalisation Parties agree further detail is appropriate or necessary) which must be consistent with the Pace Heads of Terms, there is a risk that the Sectionalisation Parties fail to enter into an implementation agreement by 31 December 2017 or at all and this could delay or even prevent implementation of the Pace Pensions Sectionalisation. There is also a risk that the detailed provisions agreed in an implementation agreement result in the Bank Section (when formed) having materially different assets and/or liabilities and/or having a materially lower funding level on the "technical provisions basis" and the "low risk target basis" from what is currently envisaged/estimated. The "technical provisions basis" and "low risk target basis" are bases that have been agreed in the Pace Heads of Terms. A key feature of the "technical provisions basis" is that the discount rate is set at gilts plus 0.5 per cent. per annum for the period until 31 December 2027 and then at gilts plus 0.25 per cent. per annum thereafter. The discount rate for the "low risk target basis" is set at gilts plus 0.25 per cent. per annum at the outset. The margin in the mortality assumption also differs between the two bases, with the margin in respect of the "technical provisions basis" incrementally increasing from zero for the purposes of the 5 April 2016 valuation by 0.83 per cent. at each of the next 3 triennial valuations (as at 5 April 2019, 5 April 2022 and 5 April 2025) so that the margin is 2.5 per cent. by 5 April 2025. The margin in the mortality assumption in respect of the "low risk target basis" is set at 2.5 per cent. at the outset. The "technical provisions basis" and the "low risk target basis" are in all other respects the same, and the "technical provisions basis" will equal the "low risk target basis" by 31 December 2027.

The Sectionalisation Parties have agreed to use their best endeavours to implement the Pace Pensions Sectionalisation by 30 June 2018, but there is a risk that this timetable will not be met. The longer the period is to implement the Pace Pensions Sectionalisation, the greater the risk that the Bank Section (when formed) contains materially different assets and/or liabilities and/or has a materially different funding level on the envisaged "technical provisions basis" and the "low risk target basis" from what is currently envisaged/estimated. This could adversely impact future contribution and security requirements in respect of the Bank Section.

Risks relating to proportion of Pace assets and liabilities forming the Bank Section on the Pace Pensions Sectionalisation

There is uncertainty as to the quantum of Pace benefit liabilities for which the Bank will take responsibility on the Pace Pensions Sectionalisation. It is estimated that the division of assets (estimated to be £11,128 million as at 31 March 2017) and liabilities (as assessed on the "low risk target basis") of Pace will be broadly 20.55 per cent. for the Bank and 79.45 per cent. for the Co-operative Group (and other employers). However, these estimated proportions were calculated as at 5 April 2016 (and if the Pace Pensions Sectionalisation had been implemented on 31 March 2017 using these proportions, it was estimated that the deficit in the Bank Section on the "low risk target basis" would have been £216 million) and there is uncertainty as to whether they will have changed by the time the Pace Pensions Sectionalisation is implemented, for example because further analysis by the Pace Trustee means that the Pace liabilities which relate to Bank (that is, the benefits of current and former Bank employees) needs to be revised, or because the allocation of the Pace benefit liabilities that do not relate to any current employer participating in Pace, and which the Sectionalisation Parties in the Pace Heads of Terms envisage will be allocated on a *pro rata* basis between the Pace employers ("**Orphans**") and therefore between the Bank Section and the Co-operative Group Section, is re-visited due to circumstances which subsequently come to light , or because the quantum of liabilities for any members is re-assessed (for example as a result of the investigation of historical benefit equalisation issues as between male and female members, including any decision to equalise guaranteed minimum pensions which, in common with many schemes, have not to date been equalised), or because of routine membership movements over the intervening period, or because of changes to long-term market implied interest rates and/or market implied inflation rates, which underpin the "low risk target basis". There is a risk that the Bank Section (when formed) contains materially different liabilities from what is currently envisaged/estimated, and this could adversely impact future contribution and security requirements in respect of the Bank Section.

Risks relating to asset allocation

The choice of assets to be allocated to the Bank Section will be determined by the Pace Trustee following consultation with the Bank and the Co-operative Group. There is therefore uncertainty as to what assets will be allocated by the Pace Trustee to the Bank Section upon the Pace Pensions Sectionalisation, and whether they will need to be changed once the Bank Section has been formed to reflect the anticipated investment strategy for the Bank Section. There is a risk that where assets allocated to the Bank Section do not reflect the investment strategy for the Bank Section, costs will be incurred making changes to the assets forming the Bank Section and the investment performance of the assets before changes are implemented could result in the Bank Section having a materially different funding level on the "technical provisions basis" and the "low risk target basis" from what is currently envisaged/estimated. This could adversely impact future contribution and security requirements in respect of the Bank Section.

Risks relating to investment strategy

The Pace Heads of Terms provide that, if the Pace Pensions Sectionalisation is implemented, the investment strategy for the Bank Section is expected to be low risk, consistent with the "low risk target basis". This is expected to involve substantial investment in bonds and similar assets. The Pace Heads of Terms also provide that the Pace Trustee will consult with the Bank and the Co-operative Group on the investment strategy for the Bank Section to be implemented immediately upon the Pace Pensions Sectionalisation and in the future. However, as is the case for all UK pension schemes, the Pace Trustee has the power to set the investment strategy in consultation with the sponsoring employer and having taken appropriate investment advice. There is therefore a risk that the Pace Trustee may change the investment strategy. Further, investment on this basis may only occur after the implementation of the Pace Pensions Sectionalisation. There will therefore be a (potentially lengthy) period until the Pace Pensions Sectionalisation where the assets to be allocated to the Bank Section may be invested on a different basis and may change. There is a risk that the investment approach applied prior to the Pace Pensions Sectionalisation, given the lead in time, will mean that the actual deficit for the Bank Section on the "technical provisions basis" and the "low risk target basis" is significantly different by the time the Pace Pensions Sectionalisation is implemented from the estimated deficits on these bases (which was £216 million in the case of the "low risk target basis") had the Bank Section existed as at 31 March 2017; for example this could arise as a result of changes to long term market implied interest rates and/or market implied inflation rates. This could adversely impact future contribution and security requirements in respect of the Bank Section.

Reputational risks relating to desectionalisation

In the event of the Bank's insolvency (which means the occurrence of an "**insolvency event**" as defined in section 121 of the Pensions Act 2004, bank insolvency or bank administration), the Bank Section of Pace may revert to operating in the way that it did prior to the Pace Pensions Sectionalisation (i.e. with all assets of Pace held on a non-segregated basis, and from which all benefits are payable). This may result in the Bank Section members being disadvantaged compared to the position they may have been in had the Bank Section been wound-up, and there is therefore a risk of adverse publicity for the Bank and its investors. For example, the combination of the Bank Section targeting full funding on a "low risk target basis" by 31 December 2027, the security arrangements to be put in place and the level of recovery achieved by the Pace Trustee on Bank insolvency might mean that the Bank Section benefits could be secured with an insurance company with little or no reduction, but such funding position might be materially diluted if desectionalisation occurs such that the assets of both sections are available to pay all Pace benefits.

Risks relating to bulk transfer

If the Pace Pensions Sectionalisation is implemented, the Pace Heads of Terms provides that if the Bank Section reaches 100 per cent. funding on the "low risk target basis" and in the Pace Trustee's opinion (having obtained covenant advice) the Bank's covenant is strong or the Pace Trustee otherwise decides in its discretion that the Bank's covenant is sufficient to provide adequate support to the Bank's liabilities, the Pace Trustee has agreed that there will no longer be any reversion to Pace operating as a non-segregated scheme as it was prior to the Pace Pensions Sectionalisation and, as a result, the Co-operative Group will no longer have any "last-man standing" risk in respect of the Bank Section. The Pace Trustee has also agreed that it may, in such circumstances, if the Bank so requests, at its discretion implement a bulk transfer of all of the Bank Section assets and liabilities to another of the Bank's pension schemes (of the Bank's choosing) with mirror image benefits. The Pace Trustee may also, at its discretion, decide to terminate "last-man standing" risk for the Co-operative Group and/or implement such a bulk transfer in other circumstances. A bulk transfer may be viewed by the Bank as preferable to continuing to participate in Pace (for example because the constitution of the Pace Trustee includes a number of individuals appointed by the Co-operative Group or members of the Co-operative Group Section, and the Bank may prefer a trustee constituted wholly or mainly of Bank Section members and Bank appointees). There is a risk that any transfer into a current Bank pension scheme may not be possible as the trustees (of each scheme) would need to explicitly approve the transfer. There is an additional risk that, should the trustee of an existing Bank pension scheme reject the bulk transfer, the Bank would need to create a new scheme which would result in additional costs to the Bank and may be subject to regulatory constraints.

25. ***The Bank's business is subject to inherent risks concerning liquidity, particularly if the availability of traditional sources of funding such as retail deposits becomes limited and/or becomes more expensive, and this may have an adverse effect on the Bank's business, profitability and ability to meet its liabilities as they fall due.***

The Bank is subject to liquidity risk as an inherent part of its business. Liquidity risk is the risk that an institution may not have sufficient funds at any point in time to make full payment in respect of liabilities falling due, or can only do so at excessive cost. This may result in an inability to operate in the ordinary course and/or a failure to meet liquidity or regulatory capital requirements, and/or may adversely impact the Bank's business and/or the implementation of its strategy.

The Bank raises the majority of its funding through accepting retail and commercial deposits. As at 31 December 2016, retail and commercial customer deposits amounted to £22.4 billion compared to £22.8 billion as at 31 December 2015, representing 84.3 per cent. and 82.4 per cent. respectively of total liabilities at these year-end dates. Whilst the Bank undertakes strategic transactions, such as the Restructuring and Recapitalisation, or during times of continued adverse press attention and speculation, the Bank's liquidity risk may significantly increase as a result of the difficulty in accurately modelling expected customer behaviour in these circumstances. Adverse and unexpected customer behaviour that the Bank is unable to manage could result in the withdrawal of material amounts of customer deposits which would adversely impact the Bank's liquidity position. Over the three months ended 31 March 2017, customer liabilities (being retail and commercial customer deposits and current accounts) reduced by £1.2 billion. See paragraph 8.2 of Part 7 of this Circular for a description of management actions taken or proposed to address the impact of customer liabilities balance attrition over this period and its impact on the Plan's forecasts and outlook, as reflected in the May 2017 Outlook on the Plan. See also paragraph 2.15 of Part 7 of this Circular for further details regarding the Bank's liquidity.

The Bank uses a combination of asset pools to manage its liquidity. Primary liquidity consists of liquid assets that are eligible under European Banking Authority regulations (high quality liquid assets). Secondary liquidity comprises liquid unencumbered investment securities not included as part of primary liquidity, as well as other forms of contingent liquidity sources.

The Bank's liquidity resources, as at 31 December 2016, amounted to £8.2 billion compared to £10.2 billion as at 31 December 2015. As at 31 December 2016, the Bank's liquid asset ratio was 13.8 per cent. (31 December 2015: 15.6 per cent.).

As part of its liquidity risk management approach, the Bank runs a series of liquidity stresses against its forecast balance sheet. The applicable stress selected by the Board determines the amount of liquidity the Bank holds in order to maintain compliance with regulatory liquidity requirements at the end of the applicable stress period. The Bank assumes within this stress that it is able to undertake liquidity management actions. To the extent that any stress of funding is greater than the applicable stress selected by the Bank, and that management actions under-deliver against the assumed actions, there is a risk that the Bank may breach its minimum regulatory liquidity requirements.

Notwithstanding the level of liquidity the Bank holds, and its compliance with regulatory minimum expectations, given the reliance by the Bank on its customer deposits to provide funding, any severe decline in customer confidence in the Bank could lead to unanticipated deposit withdrawals in a short space of time or over a sustained period. Should the Bank experience an unusually high level of withdrawals which exceed the Bank's ability to manage its liquidity, this may have an adverse effect on the Bank's day-to-day operations and its ability to maintain the Bank's planned lending. This in turn may have an adverse effect on the Bank's business, operating results and financial condition and could, in extreme circumstances, prevent the Bank from meeting its financial obligations as they fall due, meeting its regulatory minimum liquidity requirements or fulfilling its commitments to lend, thereby impacting the Bank in its ability to deliver its strategy. In such circumstances, the relevant Authorities may exercise any of their wide-ranging powers over the Bank, including imposing a resolution procedure under the Banking Act.

The Bank's ability to access retail and wholesale funding sources on satisfactory economic terms or at all is subject to a variety of factors, some of which are outside the control of the Bank. Factors which apply generally include: general economic conditions (including interest rates) and market volatility, market dislocation, confidence in the UK banking system and the economy in general and the financial services industry specifically, regulatory requirements and major disasters. These risks can also be exacerbated or driven by institution-specific factors also, such as over-reliance on a particular source of funding, perceived credit risk of institutions, and any inability to access central bank liquidity facilities at all or on commercially acceptable terms. There is also a risk that the funding structure employed by the Bank may prove to be inefficient, giving rise to a level of funding cost that is not sustainable in the long term for the Bank to grow its business.

The Bank is a participant in the Bank of England's sterling monetary framework and, as such, is subject to certain eligibility criteria at the Bank of England's discretion (as detailed in Chapter VIII of the Bank of England's Red Book). The Bank may be granted access to the Bank of England's Discount Window Facility (the "**DWF**"). This is a bilateral facility which offers liquidity insurance for idiosyncratic and system-wide shocks and is designed in order to address short-term liquidity shocks without disturbing the Bank of England's incentives for prudent liquidity management. At the Bank of England's discretion, eligible banks may, therefore, borrow gilts or cash for 30 days, against a wide range of collateral in return for a fee. Eligible banks can apply to roll DWF drawings in order to achieve an effectively longer term of drawing. In the event that the Bank was not granted access to the DWF and the Bank at such time was dependent on the contingent or actual provision of liquidity from the DWF, the absence of such liquidity may have an adverse effect on the Bank's business, results and financial condition, and could, in extreme circumstances, prevent the Bank from meeting its financial obligations as they fall due, from meeting its minimum liquidity requirements or from fulfilling its commitment to lend. Furthermore, the Bank is eligible to participate in the Term Funding Scheme but not on commercially attractive terms, and is thereby deprived of a source of low-priced wholesale funds. See the risk factor entitled "*The Bank's ability to achieve its net interest margin targets assumes that the Bank preserves its market share over the life of the Plan. The Bank faces competition in all of the core markets in which it operates. There is a risk that the Bank may lose market share to its competition and be unable to achieve its net interest margin and new mortgage business origination targets, which could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.*" for further information.

While the Bank has managed its retail offering in order to mitigate against the risk of depositors withdrawing funds, a failure by the Bank to achieve the objectives of its strategy, a deterioration in the Bank's operating results or financial condition, any actions taken by the Authorities in relation to the Bank, or the continued press attention and speculation to which the Bank is subject may result in a severe decline in customer confidence which could result in the withdrawal of retail deposits. This could have a material adverse effect on the Bank's liquidity, which in turn could adversely affect the Bank's business, profitability and ability to meet liabilities as they fall due.

26. ***The Bank faces risks associated with wholesale market access and volatility.***

The Bank supplements its retail funding base by accessing debt capital markets to raise wholesale funding. The Bank's wholesale funding capability includes securitisation and repurchase agreements and the Bank is targeting an issuance of approximately £250 million Tier 2 debt in 2018 and is also targeting MREL-qualifying debt issuances in 2020 and 2021, of approximately £200 and £300 million respectively. The Bank is also expecting to undertake a further reduction of Optimum assets of approximately £2 billion through securitisations and/or whole-loan sales, for further information see the risk factor entitled "*The Bank anticipates making a further reduction of Optimum assets through whole-loan disposals and/or securitisations. There is a risk that the Bank will be unable to de-leverage its Optimum assets in a capital efficient manner, or may incur greater than expected costs or experience delays in relation to such de-leveraging, which could adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements.*" Whilst the Bank does not rely heavily on wholesale funding, periodic access may be required to supplement its retail fundraising activities, and there is a risk that such wholesale funding is not available to the Bank or is only available using certain debt capital instruments, such as securitisations or repurchase agreements.

Secured and unsecured wholesale markets are impacted by factors outside of the Bank's control, including the fiscal and monetary policies of governments and central banks (including interest rate setting), the UK and international political and economic environment, and specific wholesale funding product market conditions. Market volatility in isolation, or combined with the markets' assessment of the Bank's credit strength may adversely affect the Bank's ability to access wholesale markets on commercially favourable terms, or at all, which could result in a significant increase in its cost of funding or result in other material adverse effects on its business, operating results, financial condition, prospects and its ability to achieve its strategy.

27. ***The Bank could be negatively affected by a deterioration or a perceived deterioration in the soundness of other financial institutions and counterparties.***

There is a high level of interdependence between financial institutions as a result of their credit, trading, clearing and other relationships. The Bank routinely executes a large number of transactions with counterparties in the financial services industry, resulting in large daily settlement amounts and significant credit exposure. As a result, the Bank is, and will continue to be, subject to the risk of deterioration of the commercial and financial soundness, or perceived soundness, of other financial services institutions and the Bank faces concentration risk with respect to specific counterparties and customers. Within the financial services industry, the default of any one institution could lead to defaults by other institutions. Concerns about, or a default by, one institution could lead to significant liquidity problems, losses or defaults by other institutions. Even the perceived lack of creditworthiness of, or questions about, a counterparty may lead to market-wide liquidity problems and losses or defaults by the Bank or by other institutions. This systemic risk could have a material adverse effect on the Bank's ability to raise new funding and on its business, financial condition, operating results, liquidity and/or prospects.

28. ***The Bank is currently involved in litigation and may in the future become involved in further litigation. The outcome of any legal proceedings is difficult to predict.***

The Bank is engaged in various legal proceedings in the United Kingdom, involving claims both by and against it, which arise in the ordinary course of business, including (but not limited to) debt collection, mortgage enforcement, consumer claims and contractual disputes. Whilst the Bank does not expect the ultimate resolution of any of these known legal proceedings to which the Bank is party to have a material adverse effect on the operating results, cash flows or its financial condition, and whilst provisions have been recognised for those cases where the Bank is able reliably to estimate the probable loss where the probable loss is not *de minimis*, the outcome of litigation is difficult to predict and there is a risk that such provisions will not be sufficient to cover the costs associated with such litigation. The outcome of any such litigation could adversely impact the Bank's reputation and brand, could result in additional similar claims being brought and/or, if perceived as a systemic or pervasive conduct issue, could result in further investigations or enquiries by the Bank's regulators. The costs of pursuing or defending legal proceedings, and the outcome of any such proceedings, could have a material adverse impact on the financial condition of the Bank.

In addition, the Bank is exposed to future litigation claims as a result of any future regulatory investigations, enforcement actions and remediation programmes. Furthermore, there is a risk that Shareholders, Subordinated Noteholders or other parties may seek to bring claims or raise arguments in Court with respect to historical events or matters or with the objective of preventing or delaying the implementation of all or part of the Restructuring and Recapitalisation. See the risk factor entitled "*Litigation seeking to challenge the implementation of the Restructuring and Recapitalisation or certain aspects of it could materially impact or prevent the successful implementation of the Restructuring and Recapitalisation or result in all or part of the Restructuring and Recapitalisation being declared to be unlawful and invalid retrospectively*" for further information. The costs of defending any such legal proceedings, and the outcome of any such proceedings, could have a material adverse impact on the financial condition of the Bank.

In addition, the Bank is exposed to the inherent risks relating to the mis-selling of financial products, and giving negligent advice or other conduct determined by the Bank or the Authorities to be inappropriate, unfair or non-compliant with applicable law or regulations (including regulatory principles or guidance). Any failure to manage these risks adequately could lead to further litigation leading in turn to significant provisions, costs and liabilities and/or reputational damage.

The Bank also faces legal, financial and reputational risk where legal or regulatory proceedings are brought against it, including as a result of the Bank's day-to-day business activity or encouraged by adverse findings of various investigations into events and activities at the Bank.

There are a number of regulatory and other investigations and enquiries into events at the Bank and circumstances surrounding them. These include:

- the Treasury announced by press release on 22 November 2013 that it intends to conduct an independent investigation into events at the Bank and the circumstances surrounding them from 2009. The investigation will review the conduct of relevant authorities (regulatory and government) and the Bank itself but is not anticipated to commence until it is clear that the investigation will not prejudice the outcome of any FCA and PRA enforcement investigations (which have now concluded in relation to the Bank itself, but not in relation to individuals). The Bank is not aware of the status of this investigation and has received no communication in respect of its status. The Bank has co-operated, and will continue to co-operate with the investigating authorities as and when requested to do so; and

- the Financial Reporting Council ("**FRC**") has launched an investigation under its accountancy scheme into the preparation, approval and audit of the Bank's accounts up to and including its 2012 annual accounts, which focuses on the role of the previous auditors and individual accountants. The FRC concluded its investigations into the former Chief Executive Officer of the Bank during 2016 and the investigation in relation to previous auditors and the audit of the 2012 and prior financial statements of the Bank is ongoing.

It is not possible to conclude if there may be any further investigations into the Bank arising as result of the above.

The Bank may also face legal, financial and reputational risk if proceedings brought by it against customers or third parties, or third-party proceedings or enforcement actions involving other financial institutions, are determined adversely to the interests of financial institutions generally or the Bank. Any adverse determinations, for example, concerning the enforcement of mortgages and/or other products or the impact on enforceability of operational practices or documentary deficiencies by the Bank or financial institutions in general such as a failure to provide all appropriate documentation, or the impact more generally of operational practices or documentary deficiencies, may have an adverse effect on the Bank's assets, funding facilities, operating results and financial condition. Furthermore, liability for damages may be incurred by third parties harmed by the conduct of the Bank's business. See the risk factor entitled "*Reputational risk could cause harm to the Bank, its business, operating results, capital position, financial condition, prospects and ability to meet targets, including return to profitability, and question the Bank's commitment to co-operative values and ethics.*" for further information.

29. ***The financial services industry continues to be the focus of significant legislative and regulatory change which has imposed, and could continue to impose, operational restrictions on the Bank, increase the Bank's costs and/or capital requirements and/or otherwise materially adversely affect its business, operating results, financial condition and prospects.***

Future changes in regulation, fiscal or other policies are unpredictable, beyond the Bank's control and could materially adversely affect its business or operations. Regulators and other bodies in the UK and worldwide have implemented and continue to consider a range of legislative and regulatory changes which could impose operational restrictions on the Bank, cause or require the Bank to raise further capital, increase the Bank's expenses and/or otherwise adversely affect its business, operating results, financial condition and prospects. These include, amongst others:

- in common with other regulated UK deposit takers, the Bank is responsible for contributing to compensation schemes such as the FSCS. By virtue of the Bank holding deposits under the FSCS, the Bank has an obligation to pay levies in respect of the outstanding borrowings that the FSCS has borrowed from HM Treasury. The Bank provided £6.6 million during the year ended 31 December 2016 (31 December 2015: £10.8 million) for its share of the levies raised by the FSCS. Further provisions in respect of these costs are likely to be necessary in the future. The ultimate cost to the Bank and the industry, which will also include the cost of any compensation payments made by the FSCS and, if necessary, the cost to the Bank of meeting any shortfall after recoveries on the borrowings entered into by the FSCS, remains uncertain but may be significant;

- there are likely to be further changes to MREL to reflect the BRRD II (as described in paragraph 2.11 in Part 11 of this Circular). There is a risk that future changes to MREL could require the Bank to raise additional capital or adjust its current capital levels beyond those contemplated by its strategy, which could have a material adverse effect on the Bank's business, financial condition, results of operations and prospects;

- Member States are required to transpose PSD2 into national law by 13 January 2018. PSD2 broadens the geographical scope of the Payment Services Directive (2007/64/EC) ("**PSD1**"), extends provisions on transparency and information requirements to all currencies, not just EU currencies, broadens the definition of payment services to include payment initiation services and account information services, and amends exemptions and conduct-of-business rules. Whilst primarily impacting current accounts, PSD2 will also impact credit cards, business accounts and certain savings accounts. Financial and other impacts as a result of these additional products are not yet clear, but are likely to be high. PSD2 includes a requirement to share access to account information with third parties with the consent of the client. This is likely to impact the Bank, as customer payments trends may change, as well as reducing interchange fees, as payments may circumvent traditional card schemes by using third parties, or raise costs for the Bank, which may not be passed on to customers in full. The Bank, in common with the rest of the payment services industry, has to achieve compliance with PSD2 by January 2018. Regulatory clarification is awaited on certain aspects before the industry can move forward with final implementation plans, particularly in relation to data access issues and related systems changes;

- the General Data Protection Regulation (Regulation (EU) 2016/679) ("**GDPR**") will apply in the UK from 25 May 2018 and will increase the obligations and responsibilities of both Data Processors and Data Controllers of which the Bank is both. There is a risk that the Bank may not be able to implement in whole or in part the full requirements of the GDPR which may lead to the potential of regulatory censure and/or fines;

- on 9 August 2016, the Competition and Markets Authority (the "**CMA**") published its final report on its retail banking investigation. The CMA decided, amongst other things, to implement open banking to accelerate technological change in the UK banking sector by early 2018. Open banking will enable personal customers and small businesses to share their data securely with other banks and with third parties, enabling them to manage their accounts with multiple providers, to take more control of their funds (for example, to avoid overdraft charges and manage cash-flow) and to compare products on the basis of their own requirements. Banks, including the Bank, are required to publish information on quality of service, and to issue suitable periodic and event-based prompts such as increase in charges or closure of branches. Within the May 2017 Outlook on the Plan, the Bank's only funded project in respect of open banking is to deliver certain mandatory elements that enable limited exchange of data. Open banking is likely to create substantial challenges in relation to implementation, particularly in respect of technological and IT changes, which could prove to be substantially more expensive for the Bank than anticipated or, if not delivered on time, or at all, lead to regulatory and reputational risks which could have a material adverse effect on the Bank's business, financial condition and operating results. Open banking will also likely reduce the level of visibility and control the Bank has over customer data and account usage (for example, through the implementation of overdraft alerts), which could reduce the Bank's ability to generate income and may, in turn, have a material adverse effect on the Bank's business, financial condition and operating results. The Bank is currently in dialogue with the CMA concerning its ability to comply with certain implementation deadlines set for August 2017 and February 2018, and applicable to all firms, in relation to the CMA-required remedies, following its investigation into the retail banking market. Dispensation can only be given by the CMA in certain circumstances in respect of these requirements and, accordingly, any breach of these requirements could result in sanctions against the Bank being imposed, which could range from undertakings being given in relation to future compliance and/or enforcement action taken against the Bank;

- as part of its 2017/2018 business plan, the FCA announced a strategic review of retail banking business models, expanding upon the CMA's market investigation. The FCA has stated that, as the CMA investigation did not look holistically at market outcomes in the retail banking sector, its strategic review will focus on the links between different parts of retail banking businesses and their relative profitability. The date for publication of the strategic review has not yet been decided, but any regulatory change could have a material adverse effect on the Bank's business, financial condition and operating results;

- Directive 2014/65/EU and its associated regulation (Regulation 600/2014) on markets in financial instruments (together, "**MiFID II**") will apply within Member States from 3 January 2018. MiFID II introduces a number of new measures which are designed to overhaul existing rules for market infrastructures. These new requirements may increase regulatory compliance costs for the Bank. MiFID II may also increase the cost of distributing financial products to both retail and wholesale clients and increase the risk of non-compliance. Due to the Bank's current business model this is not expected to have a material effect on the Bank's business, financial condition, results of operations and prospects, but it could impact the profitability of any future strategic decisions, by making compliant implementation and ongoing operations for any relevant products, services or related activities more costly, which could have a material effect on the Bank's business, financial condition, results of operations and prospects;

- on 12 December 2016, the FCA published the terms of reference for its mortgages market study (MS16/2) ("**MMS**"). The MMS will consider: (i) the effectiveness of the tools available to consumers at each stage of the consumer's journey in making decisions; and (ii) whether the commercial arrangements between lenders, brokers and other players lead to conflicts of interest or misaligned incentives to the detriment of consumers. The FCA aims to publish its interim report in summer 2017, setting out its analysis, preliminary conclusions and, where practicable, appropriate proposed solutions to address any concerns identified. Stakeholders will then have an opportunity to provide comments prior to publication of the final report in early 2018. The risks arising from the MMS will be the same for all UK banks. Depending upon the outcome of the MMS, the Bank may have to make changes to its operating model, which could have a material adverse effect on the Bank's business, financial condition and operating results. Any material changes to the mortgages market could lead to a review of the Bank's business model which could impact the Bank's mortgage volumes and margins and the Bank's ability to meet the growth targets assumed by the Plan and/or the May 2017 Outlook on the Plan;

- the Financial Services (Banking Reform) Act 2013 introduces a number of measures which could adversely affect the business of the Bank (summarised in paragraph 2.10 of Part 11 of this Circular), including a ring-fence around retail deposits held by UK banks to separate certain core banking services critical to individuals and SMEs from wholesale and investment banking services. At present, given the size of the Bank's retail deposits and its focus on retail and SMEs, it has not reached the threshold at which point ring-fencing will be required. However, if the Bank increases over time the size of its retail deposits held, it may reach the threshold for deposits at which it will be required to implement ring-fencing (£25 billion of retail deposits, excluding deposits from financial institutions, and high net worth individuals that "opt out") and separate its business on the basis described above. Effecting a reorganisation or introducing new policies and procedures to comply with ring-fencing requirements is likely to give rise to implementation costs and may have a material adverse effect on the Bank's business, operating results, financial condition and prospects;

- on 27 June 2017, the FPC increased the UK counter-cyclical capital buffer rate to 0.5 per cent. from 0 per cent. Absent a material change in the outlook, and consistent with its stated policy for a standard risk environment and of moving gradually, the FPC expects to increase the ratio to 1 per cent. at its November 2018 meeting. Furthermore, in June 2017 the FPC and the PRA launched consultations on changes to the UK leverage ratio framework relating to the treatment of claims on central banks (CP 11/17). The FPC's consultation relates to its proposed recommendation to the PRA to exclude claims on central banks from the leverage exposure measure in the UK leverage ratio framework and compensate for the resulting reduction in capital needed to meet the leverage ratio minimum requirement and leverage ratio buffers by increasing the minimum requirement from 3 per cent. to 3.25 per cent. The PRA's consultation paper sets out the PRA's proposals for implementing the FPC's proposed recommendation should it be adopted by the FPC. CP 11/17 is relevant to PRA-regulated banks and building societies with retail deposits equal to or greater than £50 billion on an individual or a consolidated basis (which is not the case of the Bank). The Bank is not currently within the leverage ratio framework, as it has retail deposit levels below £50 billion (being the threshold at which this becomes a binding requirement). However, if the Restructuring and Recapitalisation is not implemented successfully, or if it is but the Bank's leverage ratio otherwise falls to below 3.25 per cent. and the Bank is required to comply with such increased minimum leverage ratio requirement in due course, the Bank would need to take action to improve its leverage ratio, which may have a material adverse effect on the Bank's businesses, operating results, financial condition and prospects;

- the European Commission published its proposal to amend and supplement CRD IV through CRD V and CRR II. CRR II introduces a binding 3 per cent. leverage ratio, a binding detailed net stable funding ratio and an overhaul of the regulatory capital framework for market risk. CRD V introduces measures to clarify aspects related to minimum Pillar 2 regulatory capital requirements, the stacking order for regulatory capital requirements and a clarification of the relationship between Pillar 2 and the Maximum Distributable Amount triggers for the purpose of clarifying the circumstances in which certain distributions must be cancelled or reduced. CRD V also introduces a requirement that where an institution fails to meet the Combined Buffer preference must be given to AT1 distributions over other distributions in the Maximum Distributable Amount framework (such as distributions on CET1 capital or discretionary employee bonus or pension payments) (see paragraph 2.7 of Part 11 of this Circular for a description of the restrictions on distributions under CRD). These proposals could have a material impact on the Bank's regulatory capital requirements and could require the Bank to raise additional capital or adjust its current capital levels beyond those contemplated in the Plan and, where applicable, the May 2017 Outlook on the Plan, which could have a material adverse effect on the Bank's business, financial condition, results of operations and prospects; and

- On 11 July 2017, the text of the new EU Securitisation Regulation and an associated regulation to amend the CRR (together, the "**Securitisation Regulations**") became substantially finalised, following its approval on behalf of the European Parliament and the Council of the European Union. The Securitisation Regulations aim to update and streamline existing regulatory requirements surrounding securitisation. The regulatory requirements updated include the risk retention and transparency requirements imposed variously on the issuer, originator, sponsor and/or original lender of a securitisation and the due diligence requirement imposed on certain institutional investors in securitisation. In general, the requirements imposed under the

Securitisation Regulations are more onerous and have a wider scope than those imposed under current legislation. In particular, the risk weights attached to securitisation exposures for credit institutions and investment firms will in general increase substantially under the new securitisation framework implemented under the Securitisation Regulations. The provisionally approved text of the Securitisation Regulations imposes a ban on securitising "any loan that is marketed and underwritten on the premise that the loan applicant or, where applicable, intermediaries were made aware that the information provided by the loan applicant might not be verified by the lender" ("**Affected Loans**"). This ban, if adopted is expected to apply from 1 January 2019. Such a ban, if, implemented, may restrict the potential financing and Optimum de-leveraging opportunities available to the Bank for such Affected Loans both from and before this date, as re-financing opportunities for Affected Loans, whether through securitisations or whole loan sales, may be adversely impacted. Any increased risk of the Warwick 1 and 2 Notes not being called will likely have an adverse impact on secondary pricing and the carrying value of the Warwick 1 and 2 class A Notes held by the Bank. Either of these risks, should they materialise, may have an adverse effect on the Bank's business, financial condition, results of operations and prospects. For further information see the risk factors entitled "*The Bank anticipates making a further reduction of Optimum assets through whole-loan disposals and/or securitisations. There is a risk that the Bank will be unable to de-leverage its Optimum assets in a capital efficient manner, or may incur greater than expected costs or experience delays in relation to such de-leveraging, which could adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements.*" and "*The Bank has a significant holding of available-for-sale investment securities, including Warwick Finance One and Two securitisation notes. Negative changes in the carrying value of investment securities could have a material adverse effect on the Bank's business, operating results, financial condition and prospects, as well as its ability to achieve the Plan and, where applicable, the May 2017 Outlook on the Plan*".

It is not possible to predict with any certainty the effect that any of the proposed changes in the list above will have on the Bank or how any of the proposals discussed above will be implemented and whether the Bank will be able to implement the proposed changes in accordance with regulatory deadlines and regulatory required outcomes in light of these changes to the regulatory environment. These proposed changes could require new transformation programmes beyond those anticipated by the Bank or require the scope of existing programmes to be expanded and/or could result in the Bank incurring greater than anticipated or budgeted costs. Depending on the specific nature of the requirements and how they are enforced, these changes could have a material adverse effect on the Bank's business, balance sheet composition, operations, profitability, financial condition, structure, strategy, costs and/or capital requirements.

The Bank has carried out an initial assessment of the implications arising from the UK's decision to leave the EU and continues to monitor developments. As a UK-centric bank, key areas where the Bank expects to be affected by such developments are expected to relate to customer service requirements for EU based customers, payment services and internal treasury counterparty transactions.

The Bank is also exposed to the risk that changes in regulation and enforcement policy may give rise to further conduct issues. There is a risk that further conduct and legal risk issues may arise, that any such further or already identified issues may require new or further provision, and that changes in regulation may give rise to further conduct risks emerging. The occurrence of any of these could have an adverse effect on the Bank's ability to reach its cost:income ratio target in accordance with the Plan and therefore require further capital and could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

30. ***In common with other banks and financial institutions, the Bank is under intense regulatory scrutiny and expects that environment to continue. The Bank may be the subject of regulatory and other investigations and subject to legal and/or regulatory proceedings.***

As a financial services firm, the Bank is subject to extensive and comprehensive regulation under the laws of the jurisdictions in which it does business. These laws and regulations significantly affect the way that the Bank does business, and can restrict the scope of its existing businesses and limit its ability to expand its product offerings, or can make its products and services more expensive for clients and customers. There has also been an increased focus on regulation and procedures for the protection of customers and clients of financial services firms. This has resulted in increased willingness on the part of regulators to investigate past practices of financial services firms, both on an industry-wide basis and focusing on particular firms.

The Bank is exposed to many forms of legal and regulatory risks, including that:

- its business may not be, or may not have been, conducted in accordance with its products' or other terms and conditions, or applicable laws and regulations (including competition law), and financial and other penalties may result, as well as potential liabilities to customers by way of redress for prior breaches;
- its contractual obligations with customers, suppliers or other third parties may either not operate or be enforceable as intended or may be enforced in a way adverse to the Bank or the Bank may fail to comply with its contractual obligations;
- the Bank's assets, such as intellectual property, may not be adequately protected and the Bank may use intellectual property which infringes, or is alleged to infringe, the rights of third parties; and
- litigation by or against the Bank may not be appropriately managed to protect the Bank's reputation and achieve the best outcome, and that liability for damages may be incurred to third parties harmed by the conduct of the Bank's business.

The nature of any future disputes and/or legal, regulatory or other enquiries, investigations or proceedings cannot be predicted in advance. Furthermore, the outcome of any disputes and/or legal, regulatory or other investigations or proceedings arising out of any allegations made against the Bank, or members of its current or former management (including in each case with respect to prior public disclosure relating to financial or other information concerning the Bank), is difficult to predict. There is a risk that any such disputes and/or legal, regulatory or other investigations or proceedings will involve the Bank incurring significant expense in investigating and, where applicable, defending such claims as well as experiencing possible related negative publicity.

Consequently, the Bank could be exposed to:

- substantial monetary damages and fines;
- other penalties and injunctive relief;
- potential for additional civil or private litigation (including as a result of the Consumer Rights Act 2015);
- potential for criminal prosecution in certain circumstances;
- public reprimand and/or regulatory censure;
- potential regulatory restrictions on the Bank's business;
- greater scrutiny and/or investigation from regulators;
- regulatory or legislative actions;
- a reduction in the attractiveness of the Bank to stakeholders;

- a negative effect on the Bank's reputation and its brand and its ability to recruit and retain personnel and customers; and/or
- questions as to the Bank's commitment to co-operative values and ethics arising from any association, action or inaction which is perceived by stakeholders to be inappropriate or unethical.

Any of these risks, should they materialise, could have an adverse impact on the Bank's ability to implement its strategy, achieve its near-term and long-term cost:income ratio targets, its operating cost, project cost and other expenditure targets, meet its conduct and legal risk provision targets as provided for in the Plan and, where applicable, the May 2017 Outlook on the Plan, its business, operating results, financial condition and prospects, its regulatory capital resources or its ability to comply with regulatory capital requirements, as well as taking up a significant amount of management time and resources away from management of the Bank's business, including execution of the Bank's business plan.

Any adverse findings of any legal, regulatory or other enquiries, investigations or proceedings may cause reputational damage to the Bank's brand and question the Bank's commitment to co-operative values and ethics arising from any association, action or inaction which is perceived by stakeholders to be inappropriate or unethical. There is also a risk that the outcome of such investigations or proceedings may give rise to changes in law or regulation as part of a wider response by relevant lawmakers and regulators. Furthermore, an adverse decision in one matter, either against the Bank or another financial institution facing similar claims, could lead to further claims against the Bank. Sustained damage arising from any adverse findings and/or conduct and reputation risks could have a materially negative impact on the Bank's business, operating results, financial condition and prospects.

31. ***The Bank's business and financial performance has been and may continue to be affected by general economic conditions in the UK, and adverse developments in the UK or global financial markets could cause the Bank's earnings and profitability to decline and result in the Bank not meeting its net interest margin, regulatory capital requirements and RoE longer-term targets.***

The Bank is directly and indirectly subject to inherent risks arising from general economic conditions in the UK and other economies and the state of the global financial markets both generally and as they specifically affect financial institutions. Since mid-2008, the global economy and the global financial system have experienced a period of significant turbulence and uncertainty. The severe dislocation of the financial markets around the world that began in August 2007 and significantly worsened in mid-2008 triggered widespread problems at many commercial banks, investment banks and other financial and related institutions in the UK and around the world. The dislocation severely impacted general levels of liquidity, the availability of credit and the terms on which credit is available. This crisis in the financial markets led the Government and other governments to inject liquidity into the financial system and take other forms of action relating to financial institutions, including bank recapitalisations and the provision of government guarantees for certain types of funding, aimed at both supporting the sector and providing confidence to the market. This support may not be provided in the future, and, if provided, such support is likely to be on more punitive terms for financial institutions than in the past.

These market dislocations were also accompanied by recessionary conditions and trends in the UK and many economies around the world. The widespread deterioration in these economies affected, among other things, consumer confidence, levels of unemployment, the housing market, the commercial real estate sector, bond markets, equity markets, counterparty risk, inflation, the availability and cost of credit, transaction volumes in wholesale and retail markets, the liquidity of the global financial markets and market interest rates, which in turn had, and continues to have, in a number of respects, a material adverse effect on the Bank's business, operating results, financial condition and prospects.

A sovereign debt crisis in Europe led to an increase in the cost of funding. The initial impact of this increase was felt in the wholesale markets, and there was a consequential increase in the cost of retail funding, with greater competition in the market for savings. A number of policy interventions have helped to ease these funding pressures. However, if there was to be a re-emergence of a European sovereign debt crisis, the cost of funding could increase again. There remain continued challenges and uncertainty for the UK economy, including the combined economic prospects of the Eurozone, which presents a risk of a slowdown in economic activity in the UK's principal export markets, the impact of any future Government austerity measures, and the continued squeeze on household incomes. As discussed below, there is also considerable uncertainty as to the UK's proposed exit from the EU on the general economic conditions in the UK, the EU, the financial services industry and the legal and regulatory environment. Such volatility and uncertainty may persist or worsen throughout the process of negotiation that may be required to determine the future terms of the UK's relationship with the EU.

Whilst there have recently been improvements in UK GDP and the commercial and residential property markets, macroeconomic risk remains. In particular, macroeconomic instability may arise as a result of political conditions in Europe (including the recent elections in the UK and France and the forthcoming elections in certain other EU Member States, including Germany) and the United States (including the impact of the new U.S. presidential administration). There is also uncertainty surrounding the UK banks' reaction to the Bank of England's stimulus package (including in relation to its base rate, its gilt purchases and its Term Funding Scheme). Should a reversal of the improvements occur or the improvements of other factors lead to increased interest rates, these could have a potential impact on the credit performance of the Bank's assets leading to increased impairments. See the risk factor entitled "*Worsening economic and market conditions and/or increasing interest rates and/or a fall in house prices and/or commercial property prices could result in increased residential mortgage, commercial lending and unsecured loan losses which would adversely impact the Bank's financial and operational performance*." for further information.

The continued effect of margin compression and exposure to both retail and commercial loan impairment charges, resulting from the impact of general economic conditions, means that the results of the Bank's operations and financial condition may continue to be adversely impacted by such factors, and there remains the possibility of further downward pressure on its operating results and financial condition, prospects and growth depending on a number of external influences, such as the consequences of a more austere economic environment.

Any adverse developments in the UK or global financial markets could cause the Bank's earnings and profitability to decline and result in the Bank not meeting its net interest margin, regulatory capital requirements and RoE longer-term targets, which could in turn have a material adverse effect on the Bank's business, financial condition, operating results and prospects.

32. ***The Bank is exposed to risks relating to the supply and affordability of residential property in the UK.***

The Bank's owner-occupied and buy-to-let mortgage lending is dependent on a number of factors related to the supply and affordability of property in the UK.

In October 2014, the PRA issued rules and the FCA issued guidance to limit the volume of new mortgage lending for owner-occupied housing for loans with a loan-to-income ratio of over 4.5 times to no more than 15 per cent. of new loans, implementing a recommendation made in June 2014 by the FPC, a Bank of England committee responsible for ensuring financial stability. For the Bank to maintain and grow its mortgage portfolio, the prices of new and existing properties must be at levels, relative to the income of purchasers, to allow them to borrow within the parameters of these regulatory restrictions on lending. If house prices are at too high a multiple of customer income, whether as a result of rising house prices and/or low customer income growth, potential customers will be unable to borrow and the supply of mortgages will decrease.

The Bank's owner-occupied mortgage lending requires a supply of newly-built or developed property coming to the market that relies on mortgage lending for financing, as well as transaction volumes within the market for existing property being at a sufficiently high level to support a profitable level of owner-occupied mortgage lending and income from mortgage fees. A decrease in housing transaction volumes could lead to a reduction in demand for owner-occupied mortgages and a fall in related mortgage fees, which could have a material adverse effect on the Bank's business, financial condition, operating results and prospects.

33. ***Worsening economic and market conditions and/or increasing interest rates and/or a fall in house prices and/or commercial property prices could result in increased residential mortgage, commercial lending and unsecured loan losses which would adversely impact the Bank's financial and operational performance.***

The personal borrowing sector in the UK remains heavily indebted and vulnerable to increases in unemployment, rising interest rates and/or falling house prices.

Increased unemployment could lead to higher levels of arrears in the Bank's mortgage loan, unsecured consumer loan, and commercial lending portfolios which, in turn, would lead to an increase in the Bank's impairment charges in respect of these portfolios and increase the Bank's RWAs. This may, therefore, increase capital requirements and adversely impact capital adequacy ratios. Increased unemployment could also result in less demand for the Bank's products, reducing the Bank's ability to meet its targets of increasing Bank customer assets and net interest margin, which could in turn have a material adverse effect on the Bank's business, financial condition, operating results and prospects.

Rising interest rates would put pressure on existing and new borrowers whose loans are linked to the Bank of England base rate or LIBOR or the Bank's variable rates and who may have become accustomed to the historically low interest rate environment, such as the Bank's residential mortgage loan, credit card and current account products. A significant portion of the Bank's outstanding residential mortgage loan products are potentially subject to changes in interest rates. In particular, Optimum, being a portfolio of predominantly interest-only intermediary and mortgage book assets (as at 31 December 2016, £2.6 billion), may be particularly sensitive to changes in interest rates as they impact affordability, particularly in stressed economic scenario forecasting. In an increasing interest rate environment, borrowers seeking to mitigate increased monthly payments caused by interest rate increases by refinancing their mortgage loans may not be able to find available replacement loans at comparably low interest rates and this could lead to an increase in arrears in the Bank's secured lending portfolios, as well as an increase in the Bank's secured loan impairment charges. The majority of the Bank's unsecured loan portfolio is on fixed rates.

If UK house prices and/or UK commercial property prices were to fall generally or in particular regions to which the Bank has significant exposure, this would likely result in an increase in the Bank's secured loan impairment charges as the value of the security underlying its mortgage loans and/or commercial property loans was eroded. In addition, a key assumption in the judgement of estimated future credit losses is the Bank's estimate of future house price index and commercial property price movements. Optimum, which had an average loan-to-value ratio of 63.8 per cent. as at 31 December 2016, is more exposed than the retail mortgage portfolio to movements in house prices. The combined non-retail customer portfolios of the Bank (Legacy Portfolio and business and BaCB) are both exposed to falling commercial property prices. This is particularly relevant to the non-performing portfolio and the impact falling prices will have on impairment levels.

The Bank is also exposed to the risk of customers who have interest-only owner-occupied mortgage loans being unable to repay their loans in full at maturity. As at 31 December 2016, of the £16.8 billion of total outstanding mortgage balances, 67.5 per cent., or £11.3 billion, are capital repayment mortgages and 32.5 per cent., or £5.5 billion, are interest-only loans. In respect of the Bank's £3.5 billion of residential owner occupied interest-only mortgage customers, assessments of capital repayment plans may be incomplete or out-of-date and, consequently, the Bank may lack information to accurately evaluate the related repayment risk. As a result, the Bank may have reduced visibility of future repayment issues in respect of its interest-only residential mortgages, which could limit the Bank's ability to estimate and establish provisions to cover exposures resulting from these mortgages.

Where the terms of certain mortgages extend past the retirement age of customers which are potentially unable to service or repay their loans, there is a risk that the Bank may not have adequately assessed the affordability of such loans for these customers and anticipated life events (such as retirement) at the outset to ensure that such customers would be able to meet their monthly payments for the term of the mortgage.

In addition, increasing interest rates could trigger unforeseen movements in the Bank's existing mortgage portfolio, in particular in relation to accelerated run-off of demand savings balances or standard variable rate mortgage balances, as customers perceive that there is greater incentive to review their finances. This could adversely affect the Bank's ability to meet its financial targets and operational and financial performance.

34. ***The Bank is a supplier of credit to the buy-to-let sector in the UK. Many borrowers in the sector have yet to operate through an entire economic cycle, and any weakness in their credit quality may impact the financial and operational performance of the Bank.***

The buy-to-let market in the UK has expanded rapidly in recent years and the Bank is a supplier of credit to this market. As at 31 December 2016, 12.9 per cent., or £2.2 billion, of the Bank's outstanding mortgage balances were buy-to-let loans and 91.9 per cent., or £2.0 billion, of such buy-to-let loans were on an interest-only basis. Borrowers of buy-to-let mortgages have benefitted in recent years from a combination of low interest rates, rising house prices and increasing rents, as first time buyers have struggled to raise the required deposit to allow them to purchase their own homes. The Finance (No. 2) Act 2015 introduced provisions to limit the income tax relief on mortgage interest expense available on residential property to buy-to-let landlords from 6 April 2017. These factors, and the introduction of a 3 per cent. stamp duty surcharge on purchases of buy-to-let and second homes which has applied generally to sales completed on or after 1 April 2016 and any other adverse tax changes for buy-to-let investors, could make the purchase of buy-to-let properties a less viable investment opportunity and reduce the demand for buy-to-let mortgages. If rental rates were to decrease or remain stagnant, interest rates were to increase, further tax changes were to reduce the post-tax return on buy-to-let investments and/or the economy were to weaken and place pressure on employment, consumer incomes and/or house prices, the credit performance of the Bank's buy-to-let mortgage book could deteriorate, which in turn could have a material adverse effect on the Bank's business, financial condition, operating results and prospects.

35. ***The Bank is exposed to a number of political, social and macroeconomic risks relating to the UK's pending exit from the EU.***

The pending exit of the UK from the EU and related political events in the UK and Europe could result in prolonged periods of uncertainty or significant macroeconomic deterioration, including, but not limited to, decreased GDP in the UK, increased foreign exchange volatility, in particular a further weakening of the pound sterling as against the euro and other leading currencies, decreases in global stock exchange indices and a downgrade of the UK's sovereign credit rating. Additionally, as a result of uncertainty following the referendum, the pound sterling experienced sharp depreciation against a range of currencies, including the euro and dollar. There are concerns that economic and political uncertainty relating to the pending exit of the UK from the EU could push the UK into an economic recession.

Because a significant proportion of the regulatory regime applicable to the Bank is derived from EU directives and regulations, the UK's exit from the EU could materially change the regulatory framework applicable to the Bank's operations. The directives and regulations cover a range of the Bank's operations and activities and have a broader impact on the financial services industry and the legal and regulatory environment in the UK.

The Bank has carried out an initial assessment of the implications arising from the UK's decision to leave the EU and continues to monitor developments. As a UK-centric bank, key areas where the Bank expects to be affected by such developments are expected to relate to customer service requirements for EU based customers, payment services and internal treasury counterparty transactions.

The exit of the UK from the EU could result in changes in the position of UK banks in respect of participation in European payment schemes such as the Single European Payments Area, which in turn could create additional operational costs and/or costs associated with making alterations to the Bank's payments systems and processes.

If a recession were to occur in the UK, sterling were to further depreciate materially, or the Bank's regulatory environment were to change dramatically, it could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

36. ***The Bank's business and financial performance would be adversely affected by a break-up of the single European currency.***

A number of countries in Europe, such as Greece, Italy, Ireland, Portugal and Spain, together with Cyprus, have been particularly affected by the difficult financial and economic conditions since 2008 and are struggling with large sovereign debts and/or public budget deficits. This has raised concerns about the contagion effect a potential sovereign default would have on other EU economies, as well as the ongoing viability of the euro currency and the Economic and Monetary Union ("**EMU**").

The effectiveness of actions aimed at stabilising European economies and reducing debt burdens is not assured and the possibility remains that the euro could be abandoned as a currency by countries that have already adopted its use or, in an extreme scenario, abandonment of the euro could result in the dissolution of the EMU. This would lead to the re-introduction of individual currencies in one or more EMU member states. The effects on the European and global economies of the potential dissolution of the EMU, exit of one or more EU member states from the EMU and the redenomination of financial instruments from euro to a different currency, are impossible to predict fully.

However, if any such events were to occur, they would likely result in significant market dislocation and heightened counterparty risk, and affect adversely the management of market risk, including asset and liability management due, in part, to redenomination of financial assets and liabilities.

The Bank anticipates that the occurrence of any of the events described above would be likely to adversely impact the cost and availability of wholesale funding, thereby increasing competition for retail funds and adversely impacting the Bank's net interest margin, which could in turn have a material adverse effect on the Bank's business, financial condition, operating results and prospects.

37. ***The Bank is dependent on certain key management and personnel, the loss of whom, or the failure to recruit and retain key management and personnel, may have an adverse effect on the Bank's business, operating results, financial condition and prospects and its ability to achieve its strategy.***

The Bank depends on the continued contributions of its Directors, Senior Managers and other key personnel with the experience, knowledge and skills in banking necessary for its success. Furthermore, in connection with the Restructuring and Recapitalisation, certain corporate governance changes are being proposed which will lead to changes to the Bank's Board. Following such changes, there is a risk that these changes, or the uncertainty created as a result of the change in ownership of the Bank, may have an adverse impact on the Board's proper functioning, the performance of its role and its cohesiveness. See Section A of Part 5 of this Circular for further details about Holdco's corporate governance arrangements, including the rights of B Shareholders to appoint the B Shareholder Nominee Directors to the Holdco Board and, via Holdco's ownership of the Bank, the Board.

Whilst the Directors and Senior Managers have extensive relevant experience of working within the financial services industry, a certain number have worked for the Bank for a relatively short period or are in their first roles at their current level of seniority, with significant and wide-ranging responsibilities. In addition, the Bank's recent announcements have increased the demands and competing priorities on Directors and Senior Managers and may divert management attention away from business as usual activities. Should the Bank lose one or more members of its executive team without finding suitable replacements or having appropriate succession plans in place, the Bank may struggle to replace them with appropriate and sufficiently experienced and/or skilled candidates in a timely fashion, exposing the Bank to operational disruption and potential delay in essential activities necessary for the Bank's strategy to be successfully delivered. Following changes amongst the Bank's executive leadership in January 2017, a renewal of succession-planning coverage for senior roles is required. Failure to adequately improve the Bank's succession planning could negatively impact the effective governance and oversight of the Bank. The requirements of CRD IV constrain the Bank's ability to award variable pay until capital compliance and profitability are restored, which may impact recruitment and retention of staff until the Bank is compliant with its ICG and Combined Buffer, which in the case of ICG is targeted for 2018 (based on the Bank's own internal assessment of future Pillar 2a and 2b regulatory capital requirements and subject to future SREP).

Retention and recruitment of key Bank personnel remains a significant risk for the Bank and is currently heightened by the Bank's inability to use variable pay to reward performance, budgetary constraints limiting changes to fixed pay, as well as requiring headcount reductions and rationalisation of premises that form part of the Bank's implementation of its strategy. Furthermore, the Bank has experienced increasing challenges in recruitment for certain roles with potential candidates expressing concerns about the future of the Bank. There is a risk that the loss of key Bank personnel could require permanent replacement of such personnel or the deployment of contractor resources to cover key activities at an incremental cost to the Bank, which could result in higher than forecast operating costs.

Whilst employee engagement levels remained relatively stable over the course of 2016, employee confidence in the future of the business declined. Following the Bank's announcement on 13 February 2017, the Bank's ability to recruit personnel has become more challenging, with fewer applications being received per vacancy than the Bank would normally receive. Additionally, following the announcement, response rates for pro-actively sourced roles through LinkedIn fell from approximately 65 per cent. to 35 per cent. Furthermore, the Bank is aware that certain skilled colleagues are being pro-actively targeted by businesses who are actively looking to capitalise on any prevailing concern amongst colleagues as to their position and prospects at the Bank. The recent announcements relating to the FSP and Restructuring and Recapitalisation, and the adverse press and market speculation in relation to the Bank and its prospects and subsequent media speculation, may unsettle staff, impacting engagement levels and are also likely to heighten retention risk. Any significant reduction in staff engagement may have a consequential impact on the Bank's service delivery, customer service and, potentially, its brand.

The regulatory requirements of the Senior Manager Regime impact the responsibilities and potential personal liability of Directors and members of senior management, and may make it more difficult to recruit in the banking industry in general. This could have a greater negative effect on attracting people to work in financial services which may be perceived as a more difficult and constrained regulatory environment in which to work, including remuneration regulations that impact the way variable remuneration is paid and, therefore, the effectiveness of traditional reward mechanisms.

The Bank also remains reliant, to a limited extent, on other personnel employed by members of the Co-operative Group to support separation activities in the short term. The recent announcements made by the Bank in relation to the FSP and Restructuring and Recapitalisation has posed further challenges to attracting and retaining appropriately skilled and experienced individuals, which may result in a loss of subject-matter expertise and institutional knowledge. In addition, and more generally, competition for personnel with specialist skills, particularly those with financial, banking, IT and specialist control competencies such as risk, legal and finance, is intense among financial institutions. This creates an additional challenge in the northwest region where there is a shortage of specialist banking skills and the Bank may be required to pay higher wages compared to its competitors to attract specialist personnel.

Examples of risks associated with the recruitment, employment and management of individuals within the Bank include the following:

- the Bank is dependent on a small number of individuals working on a large number of initiatives. Resources are stretched and there is a risk that a sufficient number of skilled employees might not be retained or recruited to alleviate the resource issues;
- the risk that the Bank does not have the personnel to support its strategy and/or that individuals are not directly engaged by the Bank, are on short-term contracts or are not fully aware of the scope or accountability of their role;
- the risk that the Bank, employee and trade union relationships deteriorate, leading to industrial action, resulting in operational losses and reputational damage; and
- the risk that continued high levels of change have a detrimental impact on colleague engagement and performance.

There is a risk that the Bank will be unable to retain, attract or recruit a sufficient number of appropriately skilled and experienced employees critical to the implementation of the Bank's strategy, and a failure to do so may impact the Bank's ability to implement the Bank's strategy, which, in turn, may adversely impact its business, operating results, financial condition, prospects and competitive position.

Furthermore, the Bank's Non-Executive Directors are all new to the Bank since the 2013 Liability Management Exercise took place. A number of the Bank's Non-Executive Directors joined the Bank anticipating they would serve one term of three years and are reaching a point in time at which they may stand down in the next 12 months. There is a risk that the Bank may not be able to replace any departing Non-Executive Directors with suitably-skilled and experienced candidates, particularly in the case of chairs of key committees, in the timescale required.

38. ***Union representation subjects the Bank's business to the risk of interruptions through strikes or delays resulting from any restructuring of the Bank or in renegotiating labour contracts.***

The Bank collectively recognises two trade unions: Britannia Staff Union and Unite. While the Bank has not experienced any significant business interruption as a result of labour disputes at any of its businesses since September 2005, and the Bank considers its relations with employees to be good, the Bank believes that it does have a significant number of staff who are members of a trade union. Union representation subjects the Bank's business to increased risk of interruptions through strikes or delays resulting from any restructuring of the Bank or in renegotiating labour contracts.

The Bank's strategy includes significant ongoing cost-cutting, which includes continuing to reduce the number of the Bank's employees. The Bank has recently successfully consulted on a number of business change activities that include significant organisational change, a change of pension scheme and renegotiation of a number of terms and conditions. Given this recent volume of activity, further change activity could increase tension in the trade union relationship. The terms and conditions for the majority of the Bank's staff are negotiated through collective bargaining with the unions. There is a risk that the Bank may be unsuccessful in concluding any negotiations with unions or reaching an agreement with the unions, including in relation to planned organisational changes impacting redundancies. A failure to conclude negotiations and reach agreement, or any protracted negotiations, or any breach of an agreement with the unions may result in interruptions to the Bank's business through strikes or delays, a diversion of management time from running the Bank's business and implementing the Bank's strategy and, in particular, achieving the Bank's cost reduction targets, a deterioration in employee relationships, an adverse impact on the Bank's reputation and/or an adverse impact on the Bank's customer relationships. Such interruptions may, in turn, impact the Bank's business, operating results, financial condition and its ability to implement its strategy.

39. ***The Bank's operations are highly dependent on the proper functioning of IT and communication systems which comprise a complex array of legacy systems and some newer in-house and third-party IT systems. Any significant failure of the Bank to remedy the existing IT estate and operate its legacy and new IT systems to meet the requirements of its strategy may adversely affect the future operational and financial performance of the Bank's business.***

The Bank relies extensively on IT and communication systems to conduct its business, including the pricing and sale of its products, payment processing, data collection, assessing acceptable levels of risk exposure, financial reporting (including reporting of capital) and maintaining customer service (including the delivery of key regulatory documents and other customer correspondence) and accurate records and security. The Bank's complex IT landscape has arisen from the Bank's past acquisitions and mergers that have not been fully integrated and rationalised.

Although a large proportion of the Bank's critical services are now supported by technology that was migrated to new hardware in an IBM environment in the first quarter of 2017, a proportion of the Bank's systems and technology remain on extended support arrangements or are nearing end-of-life (meaning that there is limited or no support provided by the vendor or specialist third-party supplier) including the Bank's telephony and desktop systems. While the Bank has such systems in its IT estate, it remains exposed to potential service disruptions, security weaknesses and operational inefficiencies. Those aspects of the IT estate requiring further remediation include, but are not limited to, the desktop IT environment and the Bank's telephony systems.

There is duplication of systems in some critical areas of the Bank including mortgages, savings and general ledgers. Some of the Bank's IT applications remain particularly complex and are poorly documented and rely on significant subject-matter expert knowledge to maintain and are, therefore, susceptible to operational interruptions and inefficiencies. There is a risk that obsolescence will cause a greater number of service interruptions. Furthermore, the time required to fix these incidents may be greater than the time normally needed, given that mainstream support is no longer available.

Even after any remediation, there remains a risk that the processes and systems may not operate as expected, may not fulfil their intended purposes, or may be damaged or interrupted by disruptive events. Any outage of the Bank's IT systems and infrastructure could result in increased demand within the Bank's contact centres as customers seek assistance and redress during such outage period, resulting in the Bank incurring additional costs beyond those anticipated in the May 2017 Outlook on the Plan. Any failure of the IT and communications systems and/or infrastructure on which the Bank relies could lead to significant costs and disruptions that could adversely affect the overall operational or financial performance of the Bank's business, as well as harm the Bank's reputation and could cause the Bank to breach its obligations as a regulated entity and/or attract increased regulatory scrutiny.

Following the Restructuring and Recapitalisation, the addition of a new parent company, Holdco, and, in due course, an expected intermediate issuance parent company to the Bank, Issuerco, may lead to additional unplanned IT expenditure in order to implement the increased financial (including regulatory) reporting requirements to meet appropriate time, efficiency or control standards.

The complexity of systems and the end-of-life position described above may also lead to increased delivery risk in relation to the planned transformation agenda because change is inherently more difficult to deliver in such an environment, leading to an increased risk that projected delivery costs are exceeded and that projected delivery timetables are missed.

Even after the planned remediation activities are completed, any subsequent failure in systems as a result of not remediating the IT risks properly, or in the period leading up to such remediation being completed, could adversely affect the Bank's ability to conduct its business and could lead to the PRA and/or the FCA imposing additional requirements on the Bank or subjecting the Bank to additional regulatory scrutiny. Further, the actual act of working on and changing the legacy IT systems increases the risk of systems failure.

40. ***The Bank has chosen to use third-party service providers to support aspects of its IT and operations, notably providers of IT hosting and management services, systems, software, data and other assets for its critical infrastructure and operational capabilities. These third-party service providers, some of which supply their services under long-term contracts, may be expensive or difficult to replace.***

The Bank is dependent on a number of third-party outsourcing contracts and partners for its critical infrastructure and operational capability, often at significant expense. These include long-term contracts that the Bank has entered into with the Co-operative Group (including CFS Management Services Limited ("**CFSMS**")), IBM, Sopra Steria, Western Mortgage Services Limited (a subsidiary of Capita PLC) ("**Capita**") and other suppliers and third parties (including in relation to UK and international payment schemes such as CHAPS, BACS, Cheque and Credit Clearing, SWIFT and Faster Payments).

There is a risk that third-party providers could fail to supply services, IT, software, data or other assets that they have agreed to provide, either adequately or at all. If third-party providers, including IBM and Capita, fail to provide or procure the services that they have contracted to provide, or to provide them in a timely manner or to agreed levels, or the arrangements with those providers are terminated for whatever reason, such a failure or termination could have a material adverse effect on the Bank's ability to conduct its business, which could have a material adverse effect on the Bank's business, operating results, financial condition and prospects. Significant failures by either side could lead to either party invoking the relevant dispute resolution procedures within the relevant agreements which could, at worst, lead to disputes, litigation and/or a loss of customer confidence. Some of these services are supplied under long-term contracts which may be expensive or difficult to replace. The Bank may be unable to source an alternative provider for the services, IT, software, data or other assets on a timely basis, on equivalent terms, or without significant expense, within the short time required, or at all. The additional costs and expenses incurred in procuring alternative supply arrangements may have a material adverse effect on the Bank's cost base and, therefore, on the Bank's business, operating results, financial condition and prospects.

There is a risk that contracts with third-party providers on which the Bank relies may be or may have been poorly negotiated and/or poorly managed and/or a product of a poor commercial bargaining position. The Bank's dependence on third-party suppliers increases reliance on the Bank's internal procurement and supplier management function. The Bank is exposed to the risk that any outsourcing arrangements are not properly scoped by the Bank. The Bank has encountered challenges in this area, for example, in the need to extend the scope and cost of the IBM contract. The Bank is also exposed to a risk that a supplier may default on or otherwise seek to avoid its contractual requirements and obligations, or that an outsourcing is not properly managed by the Bank or delivered upon as expected by the outsourced provider on an ongoing basis.

IBM is a key supplier to the Bank, providing IT infrastructure-hosting and related IT services for the majority of the Bank's IT estate. Capita is a key supplier to the Bank providing outsourced mortgage application processing mortgage administration and arrears management across the Bank's entire mortgage portfolio, aside from some limited activities retained by the Bank (see paragraph 17.6 of Part 16 of this Circular for more detail). The Bank also has substantial reliance on Sopra Steria for application development and support and, due to the length of the relationship with Sopra Steria, knowledge of many of the Bank's applications rest with Sopra Steria. In addition, the Bank has a number of other suppliers that the Bank regards as critical to the operation of the Bank. See paragraph 17 of Part 16 of this Circular for further information on the contracts with these suppliers. In addition, if any of the Bank's key outsourcing partners of critical services cannot, or will not, continue to provide the outsourced functions and services for a sufficient time and without provision of adequate assistance to enable transfer to an alternative provider, then the Bank may face significant disruption to its services and functions, reputational damage and possible regulatory scrutiny, which could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

The Bank has recently settled a legal dispute with its exclusive mortgage process outsourcer, whom the Bank depends on to service all of its retail secured lending portfolios. As a part of this settlement, the Bank renegotiated the commercial terms and reduced the duration of the contract. In addition, the settlement involved cessation of the contracted transformation activity with the mortgage process outsourcer. The project costs in the Bank's Annual Report and Accounts 2016 included £81.9 million associated with the programme of work to transform the mortgage outsource service, which is no longer being progressed. This amount included: expenses and fee payments associated with cessation of the transformation contract with the outsourced mortgage provider (£11.0 million); a write-off of assets no longer expected to be in use (£48.5 million); and other programme costs (£22.4 million). If this outsourcer were unable or unwilling to provide the contracted services in the future, the Bank would be unlikely to have sufficient time to enable it to transfer to an alternative service provider without seeing a significant disruption to its mortgage processing. Any such disruptions could adversely affect the overall operational or financial performance of the Bank's business, as well as harm the Bank's reputation, and could cause the Bank to breach its obligations as a regulated entity and/or attract increased regulatory scrutiny.

Any reduction in third-party service or product quality, which may be an indirect or unintended consequence of the Bank's cost reduction initiatives for third-party suppliers, or any failure by a third-party to comply with the Bank's licensing or regulatory requirements, including requirements with respect to the handling of customer data, could cause a material disruption to or adverse financial and/or reputational impact on the Bank's business. In addition, there is a risk that suppliers may not wish to contract, or only agree to contract on terms providing for the protection of their payments, with the Bank, or otherwise seek to introduce terms that that are less favourable for the Bank, whilst there is uncertainty about the Bank's future direction. Any of these events could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

Reliance on third parties for key services accentuates the need for the Bank to implement strong supplier management capability. In the event that the Bank is unable to create or maintain this capability, services provided by these third parties may deteriorate or fail, costs may escalate and the Bank may fail to meet its obligations to ensure operational continuity, which could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

See paragraphs 17.6, 17.7, 17.8, 17.9, 17.11 and 17.12 of Part 16 of this Circular for a description of the key terms of the Bank's contracts with the Co-operative Group, Capita, Sopra Steria and IBM.

41. ***Risks associated with the Bank's digital platform.***

Following the Bank's 2015 digital transformation programme, the Bank has made significant progress with, and investments in, its digital offering, having delivered a scalable online banking platform which was launched in May 2016, an update of its mobile banking app made available in September 2016 and the launch of Apple Pay in October 2016. The Bank intends to continue to make further improvements to its digital banking proposition. If the Bank fails to improve its digital platform to the same extent as its competitors, the Bank's business, operating results, financial condition and prospects could be materially adversely affected. Furthermore, failure to invest in the Bank's digital platform, could also materially adversely impact the Bank's business, operating results, financial condition and prospects. Any perception that the Bank's digital offering is not of the same quality as that of its competitors could adversely impact the Bank's ability to attract and retain new and existing customers, which could have an adverse effect on the Bank's business and prospects.

The Bank may also be required to make further expenditure or investments, such as marketing, customer incentives or pricing changes, to achieve the Bank's strategic targets. Further innovation by competitors, for example through "digital disruption" of existing product or service markets causing changes in consumer demands and behaviours, or other changes in consumer behaviour, may require the Bank to adapt its plans and/or revise its strategy, causing delays in its implementation or resulting in additional costs. The Bank is also subject to the risk of not appropriately responding to innovation in financial technologies and the industry-wide risk of traditional banking information technology infrastructure and digital technologies becoming obsolete yet difficult and/or costly to replace. Failure to keep pace with industry changes could result in a reduction in the retention of the Bank's prime current account customer base and/or have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

42. ***The Bank's strategy to grow its new mortgage business volumes principally through mortgage intermediaries is exposed to risks relating to its relationships with such intermediaries.***

In maintaining and growing its mortgage portfolio, the Bank relies on a number of intermediaries in the mortgage lending market, which exposes it to the risk of deterioration of the commercial, financial or operational soundness of those organisations. The Bank is also exposed to the risk that its relationships with one or more intermediaries may deteriorate for a variety of reasons, including the inability to process mortgages in a timely manner relative to its competitors or other competitive factors or a loss of confidence in the continuation of the Bank. As the Bank seeks actively to grow the volume of mortgages introduced by intermediaries, its exposure to those risks increases. Future changes in regulation, fiscal or other policies are unpredictable, beyond the Bank's control and could materially adversely affect its business or operations. See the risk factor entitled "*The financial services industry continues to be the focus of significant legislative and regulatory change which has imposed, and could continue to impose, operational restrictions on the Bank, increase the Bank's costs and/or capital requirements and/or otherwise materially adversely affect its business, operating results, financial condition and prospects*." for further information relating to the FCA's mortgages market study and the risk posed to the Bank.

The Bank has relationships with a network of approximately 4,658 intermediaries who actively submitted business to the Bank in the year ended 31 December 2016, with approximately 73 per cent. of business originating from the top five clubs and networks. In the year ended 31 December 2016, £2.8 billion of the Bank's gross new mortgage lending was originated through intermediaries, which represented 91 per cent. of total gross new mortgage lending. If a major intermediary were to cease operations or switch allegiance to other lenders in the market, there could be a negative effect on the Bank's mortgage lending volumes. The Bank pays intermediaries structured fees and commissions for introducing new customers and retaining existing customers to it at rates that the Bank believes are consistent with the wider mortgage market. Were competitors to increase remuneration or other payments to intermediaries with whom the Bank does business, the Bank could be forced to increase its fees and commissions or risk a reduction in the amount of new business referred, which, in either case, could have an adverse impact on demand for its mortgages.

In addition, the Bank is exposed to many of the risks inherent in intermediaries dealing with its prospective customers. For example, the Bank has limited oversight of the intermediaries' interactions with prospective customers and, consequently, the Bank faces risks related to the conduct of the intermediaries with which it does relevant business. If intermediaries are found to have violated applicable conduct regulations or standards in the sale of the Bank's mortgage products, the Bank's brand and/or reputation could be harmed as a result. In addition, the structure of the intermediary mortgage market is also subject to change. For example, there may be a change in customer sentiment or regulation that results in customers dealing with financial institutions directly, which would reduce the flow of business from intermediaries and thus could have a material adverse effect on the Bank if this business was not replaced through other channels. Also, there could be consolidation in the intermediary mortgage market which may change the behaviour of intermediaries in ways which may have a material adverse effect on the Bank. Any of these factors could have a material adverse effect on the Bank's ability to meet its strategic objectives for mortgage asset growth, including its net interest margin and core customer asset growth targets and, consequently, its business, financial condition, operating results and prospects.

43. ***The Bank's Platform business is highly dependent upon its embedded relationship management team and its ability to deliver technological improvements.***

With the reduction of the Bank's branch network since 2013, distribution of mortgages through intermediaries has become an important distribution channel for the Bank's strategy, and for the year ended 31 December 2016, Platform originated 88 per cent. of the Bank's new mortgage lending by value. To support the Platform business, the Bank distributes intermediary mortgage products through a limited number of corporate partners. Relationships and panel management of the corporate partners and their associated members are managed by a relatively small team. One of the key strategies of the Bank is to continue to focus on growing its core mortgage portfolio acquired predominantly through Platform. Consequently, any loss of all or a part of the Platform relationship management team without adequate replacement would adversely affect the Bank's existing relationships with, and offering provided to, intermediaries which could materially adversely impact the level of new business driven from Platform, which could result in the Bank not achieving its target growth in net core customer assets as assumed in the Plan. Furthermore, if the Bank were to lose all or a part of the Platform relationship management team, there is a risk that it may be unable to find adequate replacements on a timely basis or at all.

The delivery of service levels for Platform is led by the Bank's outsourced partners. The Bank has determined that technology improvements are required to ensure the delivery of market driven service levels. Any failure by the Bank to make the identified technological improvements as planned, in a timely manner, or at all, could result in the Bank's removal from certain intermediary networks and clubs upon which its business is dependent, which could in turn materially adversely impact the Bank's origination of new mortgage business and its ability to achieve its targets for mortgage growth. A failure to remediate legacy systems could also result in an increase in conduct and legal risk.

44. ***Pursuant to its obligations to Visa International under a loss sharing agreement, the Bank has exposure to potential litigation in relation to merchant interchange.***

The Bank was previously a shareholder in Visa Europe, a payment services provider, holding one EUR 10 share in Visa Europe. As a former shareholder of Visa Europe, the Bank was liable for certain claims made against Visa Europe relating to merchant interchange under an indemnity clause included in the terms of its membership. Visa International acquired 100 per cent. of the shareholding in Visa Europe on 21 June 2016. The terms of the acquisition included the conversion of the existing indemnity to a loss sharing agreement ("**LSA**") between the 11 banks that were former shareholders of Visa Europe. Specific losses were allocated among these former members, including a specific indemnity for UK and Europe-wide merchant interchange claims. In return for the sale of its share in Visa Europe and its commitments under the LSA, the Bank received consideration which it discounted to account for any potential litigation for which the Bank could be liable for claims under the LSA. Currently, in the UK, various retailers and corporate businesses which paid merchant interchange fees are pursuing actions, including class actions, in the English courts claiming that the levels of merchant interchange fees charged by Visa Europe in the past were excessive. There is a risk that, should these actions be successful, the Bank may be responsible for a proportion of these claims or any settlements, in a quantum that may be greater than anticipated by the Bank. There is also a risk that any successful action could result in a large number of claims or a class action being pursued. Any such outcomes could have a material adverse effect on the Bank's business, operating results, financial condition and prospects. As a result of the Visa Europe sale, the Bank booked a total gain of £58.1 million in June 2016. There is a risk that should the Bank incur losses over and above the discount applied to the consideration referred to above, the Bank's CET1 capital position could be materially impacted by fair value adjustments required to be made to the value of the preference shares on the Bank's balance sheet. There is also a further risk that should the Bank incur losses over and above the gross value of the preference shares, then any additional loss would erode the CET1 capital of the Bank via a loss to the income statement and ultimately retained earnings. The potential value of any such additional loss is unknown owing to the unlimited indemnity put in place as part of the transaction.

45. ***There are numerous risks associated with the changes in the Bank's relationship with the Co-operative Group. The Bank's relationship with the Co-operative Group will be materially affected by the Restructuring and Recapitalisation, the termination and run-off of the Relationship Agreement and the termination of the Co-Existence Principles, as well as the Co-operative Group's reducing influence over and co-operation with the Bank.***

As at 25 July 2017, being the latest practicable date prior to publication of this Circular, the Co-operative Group owned 20.16 per cent. of the issued ordinary share capital of the Bank through CBG. Following completion of the Restructuring and Recapitalisation, the Co-operative Group's ownership interest in the Bank will be significantly reduced, reflecting its approximate one per cent. holding of A Shares in Holdco (assuming that the Co-operative Group does not participate in the Members' Equity Subscription). At this level of holding in the A Shares, the Co-operative Group will have no right to subscribe for B Shares and, accordingly, will have no right to vote except in limited circumstances.

The interests of the Co-operative Group could conflict with those of the Bank or other Shareholders. The existing concentration of ownership in the Co-operative Group has risked having the effect of delaying, deferring or preventing the Bank's ability to effect certain types of transactions that require approval by the Co-operative Group. To manage these risks, in 2013 the Bank entered into the Relationship Agreement with the Co-operative Group which regulates (in part) the relationship between the Co-operative Group and its subsidiaries. With the reduction of the Co-operative Group's shareholding, following the Restructuring and Recapitalisation, the Relationship Agreement itself will terminate, though certain provisions will continue in effect (as discussed below). In addition, the Co-operative Group will lose its right to appoint and remove a director to the Board in accordance with the terms of the Variation and Director Appointment Deed.

The Relationship Agreement includes certain obligations on the Co-operative Group to use the Bank's services, to promote the Bank's business and support the enhancement and rejuvenation of the Co-operative brand and franchise. Upon completion of the Restructuring and Recapitalisation, these obligations will continue until 20 December 2020, when they expire in accordance with the terms of the Relationship Agreement.

The Relationship Agreement also includes certain non-compete obligations on the Co-operative Group not to operate a business which principally involves the provision of banking and other services in the UK that were provided by the Bank at the date of the Relationship Agreement or in the 12 months prior to it (excluding any business activities carried on by the Co-operative Group as at 20 December 2013). These obligations will continue until three years after the termination of the Relationship Agreement.

Accordingly, upon expiry of these provisions, and in view of the Co-operative Group's diminished influence over the Bank, there is a risk that the Co-operative Group may decide to terminate its use and promotion of, and support for, the Bank's business and brand and to offer competing banking services. As of 31 December 2016, approximately 1.6 million of the Bank's approximately 4 million customers were also members of the Co-operative Group's membership scheme and approximately 600,000 customers actively traded with both the Bank and the Co-operative Group. There is a risk that some of these customers may cease to be customers of the Bank as a result of the Relationship Agreement and Co-existence Principles terminating and the Relationship Agreement going into run-off, particularly if the Bank's participation in the Co-operative Group's membership scheme terminates for whatever reason. Whether and to what extent the Bank will experience customer attrition is uncertain and will depend on a variety of factors, including the relative loyalties of customers to the respective brands of the Co-operative Group and the Bank. There is a risk that any significant customer attrition following the termination of the Relationship Agreement and Co-existence Principles and run-off of the Relationship Agreement, whether or not in conjunction with the termination of the Bank's participation in the Co-operative Group's membership scheme, may have a material adverse impact on the Bank's results of operations, financial condition and prospects.

See paragraphs 17.3 and 17.4 of Part 16 of this Circular for a further description of the terms of the Relationship Agreement and the Variation and Director Appointment Deed. See paragraph 4 of Part 16 of this Circular for a description of the terms of the Articles of Association of the Bank.

46. ***There are numerous risks associated with the changes in the Bank's relationship with the Co-operative Group. The Bank continues to be operationally dependent on the Co-operative Group and its affiliates to provide a number of services including critical IT services and on-supply certain services and has significant counterparty exposure to the Co-operative Group.***

The Bank is dependent upon the Co-operative Group which was, until December 2013, the Bank's ultimate parent undertaking and single largest shareholder, taking a number of actions or decisions in a variety of different capacities, including as a shareholder, debtor, customer, supplier, landlord and tenant, and in relation to any joint liabilities to third parties such as, for example, the pension trustees under Pace. A number of these actions or decisions could require the approval of the Co-operative Group's board and/or, the Bank understands, the consent of its banking syndicate.

The principal risks that the Bank faces given its continuing dependence on, and arising from its relationship and arrangements with, the Co-operative Group and its affiliates, include:

- *Pensions* – the risks and uncertainties relating to the Bank's obligations to Pace and, specifically, the last-man standing and orphan liabilities issues discussed under "*The Bank may become obliged to provide additional security in respect of, or make large one-off or ongoing payments to its pension schemes, or pension schemes to which it is connected and/or associated which may have a material adverse effect on its business, financial condition, operating results, prospects and regulatory capital position*." above and the risks and uncertainties relating to the implementation of sectionalisation of Pace described in "*The Bank's agreement with the Co-operative Group and the Pace Trustee on the Pace Pensions Sectionalisation is subject to a number of risks and may not be implemented on the terms currently envisaged or at all*." above;

- *Co-operative status and name (including trademark and membership issues)* – the risk that the Co-operative Group may cease to support the Bank's continued use of the term "co-operative", may not agree to the Bank's continued participation in the Co-operative Group membership scheme (which may require a re-appraisal of the Matrix required by its Compliance Statement (both as defined below) with Co-operatives UK Limited ("**Co-operatives UK**"), which could result in a loss of support from Co-operatives UK for the Bank's continued use of the term "co-operative") and has objected to the Bank's application to register "the Co-op Bank" and "Co-op Bank" as trademarks, each as discussed under "*The Bank's differentiated customer proposition depends in part on its continued use of the "Co-operative" name*." below;

- *Risks relating to the termination of the Relationship Agreement with the Co-operative Group, and its diminished influence relative to other shareholders, as a result of the Restructuring and Recapitalisation* – risks relating to the Co-operative Group ceasing to be the Bank's largest shareholder and termination of the Relationship Agreement and the Variation and Director Appointment Deed and the Co-Existence Principles, including the ability of the Co-operative Group to offer competing services as discussed under "*There are numerous risks associated with the changes in the Bank's relationship with the Co-operative Group. The Bank's relationship with the Co-operative Group will be materially affected by the Restructuring and Recapitalisation, the termination and run-off of the Relationship Agreement and the termination of the Co-Existence Principles, as well as the Co-operative Group's reducing influence over and co-operation with the Bank.*" above;

- *Supply of services* – the risk that the Co-operative Group may cease to continue to supply or provide critical IT services including the management of shared data centres, or cease to on-supply certain other services, including data, licences and assets, from third-party suppliers, as further discussed below;

- *Ongoing dependency on services provided to the Bank on contractual terms or arrangements that may be inadequate* – the Bank is exposed to the limitations of the 2006 Agreement, and other agreements and arrangements with the Co-operative Group or its affiliates which may be inadequate by customary "arms-length" service standards, and as required under Chapter 8 of the outsourcing rules set out in the FCA Handbook ("**SYSC8**"). The 2006 Agreement did not envisage, and, therefore, may not be appropriate for, the Bank operating independently from the Co-operative Group. In addition, the ITSA (for IT services) and the PSMSA (for non-IT services) were not negotiated as customary third party "arm's-length" agreements and do not contain all of the obligations, commitments and protections that might be expected of such agreements. It also included an unlimited indemnity in favour of CFSMS for all liabilities under the 2006 Agreement. As a result, the Bank may not have adequate contractual recourse against the Co-operative Group and may be exposed to the risk of onerous terms and conditions or regulatory intervention relating to non-compliance with SYSC 8 requirements. Furthermore, the 2006 Agreement, ITSA and PSMSA include rights for the Co-operative Group to terminate the provision of services by giving six (in the case of the 2006 Agreement) or 12 (in the case of the ITSA and PSMSA) months' notice. This notice period may not provide the Bank with sufficient time to make arrangements for alternative supply on acceptable terms, or at all. As of the date of this Circular, discussions are ongoing between the Bank and the Co-operative Group to seek to secure a longer period of service continuity under the ITSA but there is a risk that these discussions may not conclude successfully;

- *Cost of replacing assets and services provided through the Co-operative Group* – the Bank is currently dependent on members of the Co-operative Group (notably CFSMS) to provide key assets and to on-supply certain services, data and assets supplied by third-party providers. If the contractual arrangements with the Co-operative Group are terminated, the staff providing the services may not transfer to the Bank and/or the Bank may not find an alternative outsource provider or supplier for the services, on a timely basis, on equivalent or acceptable terms, without expense above that contemplated by the Plan, or at all;

- *Third-party service provision is not a core focus of the Co-operative Group's business* – the Co-operative Group has limited experience of providing services to a third-party, such as the Bank, and such provision of services is not in line with their business strategy. Consequently, there is an enhanced risk of failure of those services or that those services may not be provided as they would by a third-party supplier on customary arm's-length terms. Any failure by CFSMS or another Co-operative Group entity to provide or procure those assets, services or personnel in a timely manner or to agreed levels could have a material adverse effect on the Bank's business, operating results, financial condition and prospects;

- *Benefit of the Loss Sharing Deed* – in 2015 the Bank and the Co-operative Group entered into the Loss Sharing Deed which related to the surrender of group relief from entities in the Bank's tax group to entities in the Co-operative Group tax group. The Loss Sharing Deed addresses, amongst other things, the terms on which the Co-operative Group will pay the Bank for certain tax losses surrendered historically. As part of the Restructuring and Recapitalisation, on 14 July 2017, the Bank and the Co-operative Group entered into the Tax Deed of Amendment (further described in paragraph 17.17 of Part 6 of this Circular) to amend the Loss Sharing Deed to clarify that: (a) the Co-operative Group will not take any action the principal purpose of which is to avoid making or reducing a payment to the Bank under the Loss Sharing Deed; (b) the Co-operative Group will provide such information consistent with past practice that the Bank reasonably requires to enable the Bank to calculate what payments are or may become due under the Loss Sharing Deed; and (c) the Co-operative Group shall not be required to pay the next £4 million after the implementation of the Restructuring and Recapitalisation which would otherwise be due. The Bank's Annual Report and Accounts 2016 include a group relief debtor of £84.1 million (31 December 2015: £60.1 million). In summary, the Bank will receive payment from the Co-operative Group under the Loss Sharing Deed when the Co-operative Group realises the benefit of the losses surrendered and at the corporation tax rate at which the benefit is realised. The group relief balance of £84.1 million assumes a period of recovery to

2048 and is discounted on the Bank's balance sheet. The balance may vary as a result of changes to the discount rate or other changes to valuation methodology required as a result of IFRS 9. The balance will reduce as a result of the amendment to the Loss Sharing Deed under which the Co-operative Group shall not be required to pay the next £4 million after the implementation of the Restructuring and Recapitalisation which would otherwise be due. Under the Loss Sharing Deed, the Bank is exposed to the credit risk of the Co-operative Group with respect to the remaining balance. There is also a risk that the group relief debtor on the Bank's balance sheet may be reduced or lost if there is a reduction in the Co-operative Group's capacity to claim tax losses, there is a decrease in the rate of corporation tax, the Co-operative Group has other reliefs available to it or the Co-operative Group does not have sufficient taxable profits in the future as a result of underlying profitability, management of its tax affairs, corporate restructuring or any other reason to realise the benefit of the losses. A loss or material reduction in the amount of the Bank's group relief debtor may, in turn, have a material adverse impact on the Bank's financial and capital condition;

- *Counterparty exposure to the Co-operative Group* – the Bank has counterparty risk exposures to the Co-operative Group as customer of the Bank and through the banking services it provides the Co-operative Group. The risks presented by the Bank's banking exposure to the Co-operative Group involve the provision of a £55 million multi option facility comprising overdraft facilities of approximately £52 million along with approximately £3 million of facilities for foreign exchange, Visa, bonds and guarantees, as well as significant intraday credit exposure to the Co-operative Group, which the Bank monitors and manages in line with the risk mitigation techniques used across the Bank's other business customers. The Bank will, therefore, continue to be subject to the risk of deterioration of the commercial and financial soundness or perceived soundness of the Co-operative Group. Additionally, the Bank has counterparty exposure to the Co-operative Group as set out under the "*Benefit of the Loss Sharing Deed*" set out immediately above; and

- *Reputation* – there may be reputational risks arising from termination of the Relationship Agreement and how the run-off of the Relationship Agreement is managed and communicated. See the risk factor entitled "*The Bank's differentiated customer proposition depends in part on its continued use of the "Co-operative" name."* below for further information.

These multiple dependencies expose the Bank to the risk that the Co-operative Group could have a material impact on the Bank if, for whatever reason, it were to cease to supply services, IT, software, data or other assets that it has agreed to provide, either adequately, on the agreed terms or at all, or to terminate the above-mentioned agreements and arrangements. Accordingly, the Bank's multiple dependencies on, and exposures to, the Co-operative Group could result in events and uncertainties that may have a material adverse effect on the Bank's ability to conduct its business, which could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

To-date, the Bank has benefited from collaborative and responsive working arrangements with the Co-operative Group in relation to the delivery of IT services and projects. There is a risk that existing working relationships may deteriorate if the Bank and the Co-operative Group's overall business objectives start to diverge, giving rise to an increased risk of delays in the Bank's transformation and change activities, and potential earlier termination of IT agreements with the Co-operative Group than currently envisaged in Bank's plans.

In addition, the Bank faces several risks relating to any inability to separate itself from the Co-operative Group as discussed as discussed under "*The Bank faces risks arising from any inability to separate its business and operations from the Co-operative Group*." below.

47. ***The Bank's differentiated customer proposition depends in part on its continued use of the "Co-operative" name.***

The Bank's differentiated customer proposition depends in part on its continued use of the "The Co-operative Bank" name (the trademark for which is owned by the Bank) and its ethical values and reputation with customers and potential customers of the Bank. The term "Co-operative" included in its name (as used by the Co-operative Group and other co-operative societies) does not belong exclusively to the Bank (certain trademarks incorporating the word "Co-operative" and "Co-op" are owned by the Co-operative Group). By using the term "Co-operative", the Bank is exposed to the risk that the Bank, the Co-operative Group or other co-operatives that use that term in their branding, fail to act or are speculated to act in a way such as to bring the Bank's brand into disrepute. This could include litigation, employee misconduct or the misconduct (including criminal activity) of anyone associated with the Co-operative movement or brand (whether through the Co-operative Group, the Bank or otherwise), operational failures, accidents, the outcome of regulatory investigations, press speculation and negative publicity, disclosure of confidential customer information, inadequate products and services, amongst other factors, and could negatively impact the brand and reputation of the Co-operative movement, the Bank or the Co-operative Group. If, as a result of matters relating to the Co-operative movement, the Bank or the Co-operative Group, the Bank's brand, levels of customer satisfaction or the Co-operative movement more generally are damaged, this could have a negative effect on the Bank's business, operating results, financial condition and prospects and negatively impact the ability of the Bank to achieve its strategy.

The "The Co-operative Bank" trademark is owned by the Bank, which the Co-operative Group acknowledged in the Group Implementation Deed, described in paragraph 17.15 of Part 16 of this Circular. However, there is a risk that the Bank's right to use the term "co-operative" could be challenged or removed. The Secretary of State for Business, Energy and Industrial strategy may direct the Bank to change its registered name if, in his or her opinion, it gives so misleading an indication of the nature of its activities as to be likely to cause harm to the public. Furthermore, the FCA has the power to prevent the use of the term "co-operative", or to take other actions regarding the Bank's branding, if the FCA considers this desirable to protect consumers or to protect the integrity of the UK financial system. A loss of support from key stakeholders (such as the Co-operative Group, Co-operatives UK or other influential commentators) for the Bank's continued use of the term "co-operative" may result in a risk that the FCA and The Secretary of State for Business, Energy and Industrial strategy could look to exercise their powers, which could have a negative effect on the Bank's business, operating results, financial condition and prospects and negatively impact the ability of the Bank to achieve its strategy.

The Bank maintains a non-legally binding agreement in the form of a "compliance statement" with Co-operatives UK, the national representative body for co-operatives in the UK (the "**Compliance Statement**"). In consultation with the International Co-operative Alliance, Co-operatives UK has determined that it is appropriate for the Bank to use the term co-operative provided that the following criteria are met: the Bank must: (i) exist in order to promote co-operative activity and be recognised by the co-operative movement in relation to this role; (ii) operate in line with co-operative values, and not discredit the co-operative business model; and (iii) not use the term in ways that serve to mislead others as to whether the organisation itself is in fact a co-operative. To protect the integrity of this determination, Co-operatives UK reviews areas of the Bank's business, governance, operations and practice against the first two criteria listed above. In relation to the third criteria, the Bank confirms and commits not to use the term co-operative in ways that serve to mislead as to whether the organisation is in fact a co-operative. The Compliance Statement includes a process detailing that a matrix identifying the above criteria shall be drawn up by the Bank in conjunction with Co-operatives UK. The matrix includes details of the Bank's ethical policy, values and culture, governance framework, products and services, including its participation in the Co-operative Group's membership scheme, and the Bank's vision (the "**Matrix**"). The content of the Compliance Statement and Matrix are to be reviewed by Co-operatives UK on an ongoing basis when significant changes are planned to the Bank's business, governance, operations and practice, which might require the content of the Matrix and Compliance Statement to be amended. The contents of the Matrix and Compliance Statement were last updated following review by the V&E Committee in November 2016. Should Co-operatives UK not be content with changes in the foregoing, including as a result of the Restructuring and Recapitalisation, there is a risk of a loss of support from Co-operatives UK for the Bank's continued use of the term "co-operative", which in turn could result in an increased risk that

The Secretary of State for Business, Energy and Industrial Strategy or the FCA could look to exercise their respective powers detailed above.

In 2013 the Bank and the Co-operative Group agreed non-legally binding branding co-existence principles (the "**Co-existence Principles**"). See paragraph 17.8 of Part 16 of this Circular for a further description of the Co-existence Principles. Subsequently the parties sought to finalise, though did not sign, a more detailed co-existence agreement, to provide for the means by which the Bank could use the "Co-op" and "Co-operative" names to allocate trademarks and domain names into appropriate ownership, and to govern the future use by each party of trademarks such as "Co-op" or "Co-operative", to prevent any likelihood of confusion between the parties' use of such trademarks and to avoid any disputes in the future. The Group Implementation Deed terminated the Co-existence Principles from 22 July 2017. The Group Implementation Deed also imposes obligations on the Bank (without reciprocal contractual obligation on the part of the Co-operative Group) to: (i) ensure that all the Bank's brands are distinguishable from the brands of the Co-operative Group; and (ii) use all reasonable endeavours to avoid confusion on the part of the public into believing that the Bank or any of its subsidiaries are part of the Co-operative Group of companies or otherwise associated with the Co-operative Group. The Bank owns the registrations for the trading names that it uses (such as "The Co-operative Bank" and "smile"). Some trademarks used by the Co-operative Group are owned by the Bank and *vice versa*. Without a co-existence agreement or the Co-Existence Principles, there is a risk of disagreements about the use of certain similar brands or names, such as, the "Co-op" and "Co-operative" names, "The Co-op Bank" and "Co-op Bank" as to the specifications of goods/services for which each party's trademarks are used and registered.

Further, the Bank has applied to register "The Co-op Bank" and "Co-op Bank" trademarks. The Co-operative Group has objected to those applications for registration. The Co-operative Group has also applied for a number of trademarks against which the Bank has raised objections. These objections form one of the matters on which the Bank continues to liaise with the Co-operative Group. The cross-objections by the Co-operative Group and the Bank are all currently stayed (with the first scheduled to be dealt with by the Trademarks Registry in September 2017). If consensual outcomes in respect of these trademark and intellectual property matters are not agreed, this could lead to potential legal, financial and reputational risk to the Bank. The risk of not achieving consensual outcomes may increase with the proposed reduction in the Co-operative Group's shareholding and the run-off of the Relationship Agreement, the Bank's obligations in the Group Implementation Deed, or any changes to the Bank's governance and management (including amendments to or removal of the Values & Ethics in its Articles of Association) following the Restructuring and Recapitalisation or future changes and evolution of the brands of the Bank and the Co-operative Group. As a result of any of these factors, there is a risk that the Co-operative Group may also decide to object to the Bank's continued use of the terms "co-op" or "co-operative", which in turn could result in an increased risk that The Secretary of State for Business, Energy and Industrial Strategy or the FCA could look to exercise the powers detailed below.

Many of the Bank's customers participate in the Co-operative Group's membership scheme and are currently able to record "spend" or "points" by virtue of their trade with the Bank. The Bank's broader participation in the Co-operative Group's re-launched membership scheme has been under discussion with the Co-operative Group. These discussions have been put on hold by the Co-operative Group while it awaits further clarity on the future ownership of the Bank and the parties discuss funding of the membership scheme. Following implementation of the Restructuring and Recapitalisation, the Bank plans to re-commence negotiations with the Co-operative Group in relation to its participation in the Co-operative Group's membership scheme. Should these discussions not resume or, should the Bank for whatever reason, cease to participate in, the Co-operative Group's membership scheme, this may increase the risk of the Co-operative Group objecting to the Bank's continued use of the terms "co-op" and "co-operative" and, in turn, may require a re-appraisal of the Matrix with Co-operatives UK, which could result in a loss of support from Co-operatives UK for the Bank's continued use of the term "co-operative", either of which could result in an increased risk that The Secretary of State for Business, Energy and Industrial Strategy or the FCA could look to exercise their powers detailed above. There is also a risk that the Bank ceasing to participate in the Co-operative Group's membership scheme could lead to customer attrition, see the risk factor entitled "*There are numerous risks associated with the changes in the Bank's relationship with the Co-operative Group. The Bank's relationship with the Co-operative Group will be materially affected by the Restructuring and Recapitalisation, the termination and run-off of the Relationship Agreement and the termination of the Co-Existence Principles, as well as the Co-operative Group's reducing influence over and co-operation with the Bank.*" below.

The Bank has entrenched Values & Ethics into its Articles of Association and the Principal Investors have agreed that those provisions will continue following the Restructuring and Recapitalisation. These will also be incorporated into the Holdco Articles of Association and the articles of association of Issuerco (if and when it is interposed between Bank and Holdco). If the Shareholders of the Bank decide to remove those entrenched provisions, there is a risk that the Bank may be compelled by the Co-operative Group, The Secretary of State for Business, Energy and Industrial Strategy or the FCA to cease the conduct of any business under a brand that combines the words "Co-operative" or "Co-op" and "Bank", which could have a negative effect on the Bank's business, operating results, financial condition and prospects and negatively impact the ability of the Bank to achieve its strategy.

48. ***The Bank faces risks arising from any inability to separate its business and operations from the Co-operative Group.***

Since December 2013, when the Bank ceased to be wholly owned by CBG, the Bank has been working on operational separation from its former parent, CBG, its ultimate former parent, the Co-operative Group, and its former sister companies, CFSMS and CISGIL. The separation process has been, and continues to be, complex and time-consuming, with progress much slower, and costs higher, than initially foreseen. Whilst substantial elements of separation have been completed, notably for day-to-day operations and technology supporting many of the Bank's core business processes, significant dependencies remain. The risks associated with the remaining process of separation and the inability of the Bank to separate its business and operations from the Co-operative Group include:

- *Co-operative Group's parallel exit of shared IT infrastructure* – due to inter-dependencies between the Bank's exiting of the IT infrastructure shared with the Co-operative Group and the Co-operative Group's General Insurance business' parallel exit from the same shared IT infrastructure, there is a greater risk of delay to the successful completion of the Bank's IT programmes that relate to the Bank's exit from the shared IT infrastructure and any such delay may result in additional costs above those contemplated in the Plan;

- *Costs of separation* – the costs of separation have already been significant and further significant costs may be incurred in excess of those contemplated by the Bank in the Plan and adversely impact the Bank's ability to meet its project cost targets;

- *Indemnification obligations* – the Co-operative Group has generally been insistent upon indemnification in relation to transition assistance provided, which may increase the Bank's contingent liabilities;

- *Co-mingling of data following separation* – there is a continuing mix of customer, employee and financial data between the Bank and members of the Co-operative Group on the shared IT infrastructure, which creates a risk that the Bank or the Co-operative Group may breach applicable data protection legislation. See the risk factor entitled "*The Bank and the Co-operative Group continue to share and co-mingle data and access to data, creating an increased risk of breaches of data protection and privacy laws sanctions and/or fines from regulators*." below for further information;

- *Separation programme interdependencies* – the various activities that need to occur to achieve complete separation have multiple interdependencies, such as the Bank's desktop programmes, telephony, and data centre migrations, which need to be completed contemporaneously to achieve overall IT separation from the Co-operative Group, including separation from the shared network and exit from the shared data centres. These interdependencies increase the risk to separation completing in a timely or cost-effective manner;

- *Separation plans remain subject to change* – as the Bank and the Co-operative Group jointly and individually plan and execute the separation activities, unforeseen factors may arise which necessitate adjustments to the plans, including adjustments which extend the period of service dependency which may in turn lead to an extended period where operating costs and/or complexities are above those envisaged by the Plan;

- *Requirements for assistance in connection with an exit in part from the ITSA and PSMSA* – the Co-operative Group is required to provide significant transition and delivery support and assistance to achieve separation under several agreements between the Co-operative Group and the Bank and relevant affiliates (for example, ITSA, the PSMSA, the Transitional Services Agreement and the Reverse Shadowing Letter (each as defined in Part 20 of this Circular)). If the Co-operative Group does not provide this support and assistance, the Bank will not be able to deliver its programme of change, achieve its anticipated business outcomes, and complete its separation from the Co-operative Group;

- *Complexity of IT operating model* – the complexity of the current transitional IT service arrangements across the Co-operative Group and the Bank's replacement suppliers creates risks that the Bank will experience a greater number of service interruptions. Furthermore, the time required to address these interruptions may be greater than the time typically needed given the complex interim service model and the possibility of multiple parties needing to be involved in remedying issues, resulting in additional costs and expenses to the Bank not contemplated by the Plan;

- *Supporting the Separation Cost Share Agreement* – the Bank and the Co-operative Group agreed governance arrangements and funding levels to support IT separation in the Separation Cost Share Agreement. If the approach to separation, overall timetables or activities assumed within the Agreement are not followed, there is a risk that the Separation Cost Share Agreement is no longer appropriate or is breached, giving rise to unplanned liabilities and expenditure;

- *Property occupation and estates issues* – there are formal leases in place for St Paul's House and Miller Street, where the Bank is tenant and the Co-operative Group is the Bank's landlord, along with Balloon Street and Olympic House, where the Co-operative Group is tenant and the Bank is landlord. However, the Co-operative Group does not have formal rights of access to the shared data centres leased or owned by the Bank (in the Olympic House, Tytherington and Delf House premises), raising uncertainties and potential disagreements on responsibilities and liabilities. Discussions are ongoing between the Bank and the Co-operative Group to seek to address this issue of rights of occupation, although as of the date of this Circular no agreement has been concluded. There is also a risk that the Co-operative Group's activities in those data centres may adversely disrupt or impact the Bank's operations until those properties may be disposed of;

- *IT software licensing* – the Bank currently benefits from a number of IT licences procured by the Co-operative Group for its own and the Bank's benefit. The Bank will need to ensure that it procures all the IT licences required to support and run the Bank's IT systems independently from the Co-operative Group, and that those licenses adequately address the Bank's needs. Due to the complexity of separation and the legacy of the Bank's IT estate, there is a risk that a number of additional licences will need to be acquired to ensure licensing compliance. Furthermore, where suppliers to the Bank identify that their products may no longer be required post-separation, they may attempt to levy additional or penal licence fees on the Bank; and

- *Separation governance* – although the majority of planned separation activities are part of broader formally managed change programmes governed by steering committees, there is no overall Bank governance committee overseeing separation. Further, separation is not managed by a central separation team in the Bank and some separation work is being delivered by personnel that are not subject to Bank project change governance. There is a risk that separation costs may not be managed or reported on in a timely manner or may continue to be greater than targeted in the Plan and, where applicable, the May 2017 Outlook on the Plan, particularly if completion of separation is delayed, or does not occur.

49. ***Reputational risk could cause harm to the Bank, its business, operating results, capital position, financial condition, prospects and ability to meet targets, including a return to profitability, and question the Bank's commitment to co-operative values and ethics.***

The Bank's reputation is one of its most important assets. Its ability to attract and retain customers and deposits and to conduct business with its counterparties could be adversely affected to the extent that its reputation or its brand is damaged. The act of addressing or failing to address, or appearing to fail to address, issues that could give rise to reputational risk is likely to cause harm to the Bank, its business and its prospects. The Bank's reputation could be impacted by both known issues and issues not yet identified (some of which could only have an ancillary connection to the Bank). For example, litigation, or the misconduct of employees or other persons (including criminal activity) at any time associated with the Co-operative brand or the "The Co-operative Bank" brand, operational failures, accidents, the outcome of regulatory investigations, media speculation and negative publicity, breaches of data protection or other laws, products considered to be inappropriate and sub-standard customer service, amongst other factors, could impact the Bank's reputation. Reputational damage could arise from, without limitation, any of the following (along with media speculation regarding the same where relevant):

- the reputational damage arising from downgrades to the Bank's credit ratings and the implementation of the Bank's strategy, including the Restructuring and Recapitalisation;
- litigation or objections, including from creditors in connection with the Restructuring and Recapitalisation and interest groups and associated media coverage;
- a requirement to raise further capital in the future, which could affect, or be perceived to affect, confidence in the Bank;
- a failure to implement and execute the Bank's strategy, the Plan and/or the May 2017 Outlook on the Plan in whole or in part;
- any perception that the Bank is vulnerable to market conditions and other factors over which the Bank has limited or no control, such as the interest rate environment;
- a perception that the Bank has moved away from its co-operative Values & Ethics or that there are breaches of the Bank's Values & Ethics policy by the Bank or its employees;
- a reduction in the Bank's customer service levels mainly as a result of cost reductions and outsourcing;
- a conflict between the mutual and ethical reputation of the Co-operative brand with the value maximisation objective of other Shareholders of the Bank and the duties of the Board to such Shareholders, and more generally the Bank's association with the Co-operative brand, including any actions or omissions or speculation by or about the Co-operative Group. See the risk factor entitled "*The Bank's differentiated customer proposition depends in part on its continued use of the "Co-operative" name.*" for further information;
- any potential impact to the Bank's brand or reputation as result of the reduction in the shareholding of the Co-operative Group upon Completion;
- a material or major failure of or inability to promptly recover key services, recover IT capability, or other infrastructure, particularly where this disrupts the Bank's ability to service customer transactions for a prolonged period;
- the risk that The Secretary of State for Business, Energy and Industrial Strategy may direct the Bank to change its registered name, or that the FCA or a third-party may prevent the use of the "Co-operative" name, or take other action regarding the Bank's branding;

- matters relating to the Co-operative Group or its governance or to its current or former officers, employees or management, including their professional or personal misconduct, which adversely impact the Bank's brand;
- adverse findings following from any legal or regulatory investigation into the Bank's conduct or investigations connected to the Bank; see the risk factor entitled "*In common with other banks and financial institutions, the Bank is under intense regulatory scrutiny and expects that environment to continue. The Bank may be the subject of regulatory and other investigations and subject to legal and/or regulatory proceedings*.";
- failing appropriately to address potential conflicts of interest;
- breaching or facing allegations of having breached legal and regulatory requirements, including those relating to AML sanctions, anti-bribery and corruption requirements and a subsequent enforcement action or regulatory investigation;
- acting or facing allegations of having acted unethically (including having adopted inappropriate sales and trading practices);
- failing or facing allegations of having failed to maintain appropriate standards of customer privacy, customer service and record-keeping;
- internal or external fraud;
- failing properly to identify legal, regulatory, reputational, credit, liquidity and market risks inherent in products offered;
- failure to adhere to the Bank's Values & Ethics or ethical policies;
- cyber or denial of service attacks; and
- resignation of the Bank's auditors.

A failure to address these or any other relevant issues appropriately could make significant numbers of customers, depositors and investors unwilling to do business with the Bank. For example, if the negative news flow continues for a significant period of time, there is the risk that the Bank will lose a material number of customers and liability/asset balances to competitors. This could materially adversely affect the Bank's business, operating results, financial condition and prospects and could damage its relationships with its regulators. The Bank cannot provide any assurance that it will be successful in avoiding damage to its business from reputational risk.

50. ***The Bank's policies and processes for risk management may prove inadequate for the risks faced by its business and could lead to exposures outside the Bank's risk appetite, and unforeseen losses. Any failure properly to manage the risks which it faces could cause harm to the Bank and its business prospects.***

Historically, the Bank's risk-management framework ("**RMF**") has been weak and there have been failings in a number of areas in the past.

Whilst the Bank has taken steps to enhance its RMF, further work is required to fully embed the RMF to a consistent standard across the Bank, which may lead to the identification of further risks and control failings which could potentially impact the business, operating results, financial condition and prospects of the Bank.

The Authorities will continue closely to review the Bank's progress throughout 2017 and on an ongoing basis. A failure to implement an RMF that addresses any remaining material deficiencies could potentially result in the Authorities taking further action and operational risks arising from any continuing deficiencies that may have a material adverse effect on the Bank's ability to implement its strategy.

The Bank has a range of tools designed to measure and manage the various risks which it faces. These methods may prove to be inadequate for predicting risk exposure, which may prove to be significantly greater than is predicted. Methods for risk management are based on evaluation of information regarding markets or customers or other information that is publicly known or otherwise available to the Bank. Such information may not always be correct, updated or correctly evaluated. In addition, even though the Bank constantly measures and monitors its exposures, there is a risk that its risk management methods will be ineffective, particularly in unusual or extreme market conditions. It is difficult to predict with accuracy changes in economic or market conditions and to anticipate the effects that such changes could have on the Bank's financial performance and business operations.

51. ***Many of the Bank's business, operational, reporting and financial processes rely on significant manual processes and intervention, which is inefficient and significantly increases the risk of errors in the Bank's operational processes, including customer-facing processes, data and financial reporting, by comparison with automated processes.***

The Bank's auditors have classified the weaknesses in the Bank's control environment as a "pervasive risk to the audit" and "in excess of what would be considered normal in the banking industry".

Key business and operational processes, including processes supporting payments and financial reporting (including, *inter alia*, statutory, regulatory and management reporting, which incorporates management reporting of actual results, planning, forecasting and stress testing reporting), rely on manual process steps and on manipulation of data using spreadsheets and other end-user tools, some of which are not subject to the same controls as the Bank's core systems. Data validation in some cases relies on manual checks where automated checks might be expected, leading to a heightened risk of processing errors and hence to the possibility of financial loss, adverse customer impact, compliance breaches and reputational harm to the Bank. The Bank periodically experiences actual and near-miss risk events, including where manual errors cause incorrect payments to be made or nearly made. Where such payment is retrieved from a customer, this is termed a "near-miss". Where such payment is not recovered, this constitutes an actual operational loss event.

The Bank's financial reporting processes are complex, reflecting reliance on legacy systems which have not been fully integrated following the merger of the Bank and Britannia. The Bank relies on manual processes to consolidate the Bank's financial results and other data, and there is a significant use of spreadsheets, manual controls and adjustments and other end user computing systems, as opposed to fully automated consolidation and reporting processes. The retained evidence supporting the operation and review of these manual controls and substantiation of balances is frequently inadequate and is the subject of controls remediation. The manual nature of the processes increases the risk of a material misstatement in financial reporting.

There is a significant risk that the Bank's financial statements or related financial disclosures and other reporting or financial planning, including the accuracy of the Bank's targets and assumptions, may contain material errors or need to be restated which could lead to actual exposures outside the Bank's risk appetite, unanticipated losses and regulatory censure.

As a result of the Restructuring and Recapitalisation, the Bank's legal entity structure and financial reporting will increase in complexity, with amongst other things, the introduction of Holdco as the ultimate parent company of the Bank, resulting in the requirement for consolidated financial and regulatory group reporting for Holdco and Issuerco (if and when it is interposed between Bank and Holdco). The increased volume of reporting that will be required as a result of the Restructuring and Recapitalisation will, in addition to the existing complex and manual processes described above, further increase such risks. Should any of these risks materialise, they could have a material adverse effect on the Bank's business, operating results, financial condition and ability to achieve its targets.

52. ***The Bank and its customers are exposed to risks associated with cyber crime and fraud.***

As with other financial institutions, reflecting the increased use of technology in financial services, the Bank and its customers are at risk of actual or attempted cyber attacks from parties with criminal or malicious intent, including attacks designed to overload the Bank's systems. These risks are accentuated as the Bank increasingly digitalises its products, services, key functions and distribution channels and as cyber attacks become more sophisticated and prevalent. The Bank is subject to the risk that any cyber attack may result in temporary loss of operational availability of the Bank's systems to its employees and/or customers which could have a material adverse effect on the Bank's business, financial condition, operating results and prospects.

There is a risk that the Bank may not continue to invest sufficiently in its information security controls in response to emerging threats, such as cyber crime and fraud, and to seek to ensure that controls for known threats remain robust. The risks associated with cyber attacks, where an individual or group seeks to exploit vulnerabilities in IT systems for financial gain or to disrupt services, are a material risk to the Bank and the UK financial system, which has a high degree of interconnectedness between market participants, centralised market infrastructure and in some cases complex legacy IT systems. There is a known vulnerability to cyber-attacks inherent in older technologies, especially with older operating systems. The Bank has some exposure to such systems. There is a risk that the Bank's infrastructure and controls may be seen to be ineffective or have material weaknesses or significant deficiencies and any failure of the controls to anticipate, prevent or mitigate a network failure or disruption could entail a temporary loss of operational availability to employees and/or customers and could result in significant financial losses and a material adverse effect on the Bank's operational performance and reputation.

Furthermore, any breach in security of the Bank's systems, for example from increasingly sophisticated attacks by cyber crime groups or fraudulent activity in connection with customer accounts, could disrupt its business, result in the disclosure of confidential information, create significant financial and/or legal exposure and damage the Bank's reputation and/or brand.

Additionally, the Bank and its customers are exposed to increased levels of card, account, identity, internal and other frauds, some of which are more sophisticated, organised and technology-led. This growth and increased sophistication increases the fraud risks to which the Bank is exposed and the Bank's systems based preventative measures may be less developed than those of other banks, may not prove effective in all circumstances to prevent fraud and, without further investment, may be increasingly exposed to fraud risk from increasingly sophisticated attacks by cyber crime groups or fraudulent activity. This may mean that the Bank is potentially exposed to greater levels of attack and resultant losses than other institutions. There is increased focus by Government, regulatory bodies, law enforcement and consumer protection groups in respect of bank-related fraud. This could result in changes to regulation or regulatory expectations in terms of the level of fraud for which the Bank, as opposed to its customers, is held liable, thus increasing the impact of even the present levels of fraud on the Bank's losses.

Any of these activities may be difficult to prevent or detect, and the Bank's internal policies to mitigate these risks may be inadequate or ineffective. The Bank may not be able to recover the losses caused by these activities or events, and it could suffer reputational harm as a result of them, either of which could have a material adverse effect on its business, financial condition, operating results or prospects.

53. ***The Bank may suffer loss as a result of fraud or theft.***

As a financial institution, the Bank is subject to a heightened risk that it will be the target of criminal activity, including fraud or theft. Due to the nature of the Bank's business, it has exposure to many different customers and third-party service providers. The Bank's selection and screening processes with respect to its third-party service providers and lending customers, as well as its internal relationship management processes, may be ineffective if the Bank's customers or third-party service providers engage in fraudulent activity.

For example, the Bank is exposed to potential losses resulting from customers or third-party service providers providing the Bank with falsified or fictitious information in order to secure financing or receive sales commissions. Such fraudulent activity could have a material adverse effect on the Bank's business, financial condition, operating results or prospects. The Bank is also reliant on the accuracy and completeness of information it receives from its third-party service providers, credit reference agencies and customers. If the Bank receives inaccurate or misleading financial statements, credit reports or other financial information relating to its borrowers, such borrowers may be more likely to default on their obligations to the Bank, which could have a material adverse effect on the Bank's business, financial condition, operating results or prospects.

In addition, losses arising from staff misconduct may result from, amongst other things, failure to document transactions properly or obtain proper internal authorisation in an attempt to defraud the Bank, or from theft by staff of customer data or physical theft at the Bank's premises. Such behaviour may be difficult to prevent or detect, and the Bank's internal policies to mitigate these risks may be inadequate or ineffective. The Bank may not be able to recover the losses caused by these activities, and it could suffer reputational harm as a result, each of which could have a material adverse effect on its business, financial condition, operating results or prospects.

54. ***Anti-money laundering ("AML"), anti-bribery, sanctions and other compliance risks.***

Combating money laundering, bribery and terrorist financing and compliance with economic sanctions has been a major focus of government policy relating to financial institutions in recent years (most notably in the UK and the EU). UK and EU law and regulations impose obligations on the Bank to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing. Failure by the Bank to implement and maintain adequate policies, procedures and controls to combat money laundering, bribery and terrorist financing or to ensure economic sanction compliance could have serious legal and reputational consequences for the institution, including exposure to fines, public censure, penalties and damages. In 2013 and 2014, the Bank identified a number of significant control weaknesses with respect to its AML sanctions and terrorist financing controls and consequently there may be instances in which obligations imposed by UK and EU law with respect to AML, sanctions and terrorist financing controls have not been met. There is a risk of the FCA exercising its powers over the Bank (including imposing fines) in respect of any remaining control weaknesses that are in the process of being remediated. The Bank has remediated the majority of its high-risk customers for AML regulations and attestation was submitted to the FCA in Q1 2017 confirming the remediation actions taken in relation to such customers. However, any weaknesses in the Bank's AML, sanctions and terrorist financing controls and/or failure to remediate them could have a significant adverse effect on the Bank's business, operating results, financial condition and/or prospects.

55. ***There are weaknesses in the Bank's framework for managing data, including adequate business and IT infrastructure, documented standards on ownership and quality of data (relating to Bank customers and employees as well as Bank proprietary data), as well as clear, documented standards and policies about the use of data. Failure to adequately maintain corporate records or to adequately maintain and protect customer and employee information could have a material adverse effect on the Bank.***

Weaknesses in the Bank's data governance and data ownership framework have led to sub-optimal data management practices being adopted. These practices have resulted in difficulties in verifying the quality and usage of data across the Bank. As a result, there are risks of inaccurate or incomplete financial and other reporting as well as the risk of inappropriate decision-making due to errors in underlying data.

There is a risk that the retained records may not be adequate for the current purposes of the Bank and the Bank may not have adequate accessibility to required records. This may lead to, amongst other things, the Bank being unable to access sufficient information to ascertain the sequence of past events and defend itself against litigation or, in the course of regulatory or other enquiries, may potentially lead to adverse reputational impact, financial costs, regulatory censure and fines.

The Bank processes personal data (including name, address, date of birth, bank and credit card details and other personal data) of its customers, third-party claimants, business contacts and employees as part of the operation of its business. It must, therefore, comply with data protection and privacy laws and industry standards in the UK and the EU. Such compliance may also be contractually required. Those laws and standards impose certain requirements on the Bank in respect of the collection, use, storage and destruction of such personal data. For example, under UK and EU data protection laws, when processing personal data, certain information must be provided to the individual whose data is being processed. This information includes the identity of the data controller, the purposes for which the data is being processed and any other relevant information relating to the processing. There is a risk that the processing of data by the Bank and its appointed third parties is not conducted in accordance with notifications made to, or obligations imposed by, regulators, the rights of data subjects, or applicable law. Failure to operate effective data protection controls could potentially lead to regulatory censure, fines, reputational and financial costs, increased card handling fees, on the withdrawal of payment processing services in the future, as well as result in potentially inaccurate rating of risks or overpayment of claims.

The GDPR was published in the Official Journal of the EU on 4 May 2016 and is due to come into force on 25 May 2018. The GDPR is likely to increase the regulatory burden on the Bank in processing personal customer, employee and other data in the conduct of its business and acting as data processor in respect of the Co-operative Group's data. The GDPR includes significant financial penalties of up to 4 per cent. of the annual worldwide turnover of company groups. The Bank has a funded plan for GDPR compliance; however, there is a risk that this will not be sufficient, that completion of such plan is delayed or that the final requirements will differ from those for which the Bank has planned.

There is a risk that certain types of data governance breaches could subject the Bank to liability and/or damage the Bank's brands and reputation. For example, the Bank's systems, processes and controls with respect to the use of marketing data present certain deficiencies, including with respect to recording and applying customer marketing preferences. Such weaknesses could lead to the Bank contacting customers or sharing customer details where customers had not provided the relevant permissions. This could result in the Bank losing customers and liability/asset balances to competitors, which may have an adverse impact on cross sales.

The Bank is exposed to the risk that the personal data processed for its purposes could be accessed and/or used without authorisation, whether by employees or other third parties, or otherwise lost or disclosed in breach of data protection laws. If the Bank or any of the third-party service providers on which it relies (including the Co-operative Group) fail to process such personal data in a secure manner or if any such theft or loss of personal data were otherwise to occur, the Bank could face action under data protection laws. This could also result in damage to the Bank's brands and reputation, as well as the loss of new or repeat business, any of which could have a material adverse effect on the Bank's business, operating results, financial condition and/or prospects.

Capita staff who administer Bank mortgage business do so via IT platforms shared with some of the Bank's savings business, which provides them with access to data that does not relate directly to their business activities. If Capita or other third-party staff do not act in accordance with established controls and procedures, there is a risk personal data could be accessed and/or used without authorisation, or otherwise lost or disclosed in breach of data protection laws.

In certain circumstances, the Bank's systems testing activities make use of copies of real customer data. Although these activities are controlled, there remains the possibility that failure of these controls could lead to personal data being accessed and/or used without authorisation, or otherwise lost or disclosed in breach of data protection laws.

56. ***The Bank and the Co-operative Group continue to share and co-mingle data and access to data, creating an increased risk of breaches of data protection and privacy laws sanctions and/or fines from regulators.***

The Bank and the Co-operative Group continue to share physical and digital information assets and access to them, notwithstanding that they are no longer part of the same group, thereby creating an increased risk of breaches of data protection and privacy laws and/or industry standards, entailing sanctions and/or fines from regulators in relation to personal data). An adverse finding from a regulator could have an adverse effect on the Bank's reputation and on the Bank's business, operations, financial condition or ability to achieve its targets.

As the Bank has not completed the separation of its systems from the Co-operative Group, the Co-operative Group has the ability to access the Bank's customer and employee information. The Bank is unable, therefore, to comply across its entire operation with the seventh principle of the Data Protection Act 1998, which requires that personal data must be kept secure against loss or disclosure, as certain personal data will be held on shared assets. The Bank has advised the relevant authority of this fact and of the data risks associated with the separation process and the relevant authority has noted that it is comfortable with the measures which the Bank is putting in place to reduce the risk. There is a risk that the relevant authority will change its approach to the Bank's breach or any other potential or actual breach of data protection and privacy laws and industry standards and the Bank remains at risk of potential enforcement action by the relevant authority.

The Bank is seeking to mitigate the risks of breach of data protection and privacy laws and industry standards by seeking to implement certain separation projects (including separation of digital information assets stored in shared technologies and separation of physical information assets) and has put in place a data processing agreement and manual data exporting agreements with the Co-operative Group for the separation period. An enduring data agreement to govern treatment of co-mingled data was entered into on 3 July 2017. However, there are risks to the successful implementation of these separation projects as these projects are highly complex and face significant challenges This could, for example, mean that during separation the Bank is exposed to poor control by the Co-operative Group of the Bank's data, that the Bank has no audit rights over the Co-operative Group and that the Bank may not be able to share the cost of data separation; the Bank is relying on the Co-operative Group's resources to provide access to those assets which the Bank uses in a timely manner; the separation projects could encounter delays during negotiations and planning, including, due to the Co-operative Group's complex governance arrangements, different working practices and absence of understanding of the Bank's regulated environment; information could be lost during the separation process; lack of an information asset register within the business could impact the ability to separate such assets; there is a risk of increased key person dependencies and the possibility of increased staff turnover owing to the increased workload arising from separation; the technology environment relies in part on archaic technology that increases the degree of difficulty required in separating the data environments (potentially increasing the time and cost of data separation); physical records may not be adequately stored or able to be reached easily, requiring extra time and investment to appropriately separate; and the Bank may not be legally compliant in its business with respect to data processing arrangements. Post-separation, the Bank will have a copy of all Bank data and previously co-mingled Co-operative Group data, and accordingly will not be reliant on the Co-operative Group providing access to Bank data in a timely manner.

Further, there is an increased risk of loss, theft or disclosure of the Bank's commercial information (or a third-party's confidential information) as a result of historical sharing of systems, including data storage systems, between the Bank and the Co-operative Group. Upon eventual completion of systems separation between the Bank and the Co-operative Group each party will retain historical copies of certain data related to the other party that is uneconomical to separate. Areas of concern include legacy IT infrastructure (e.g. shared network drives and/or email systems and voice data recordings), finance systems and marketing systems. The Bank and the Co-operative Group entered into an enduring data sharing agreement dated 3 July 2017 to govern this data. If either party fails to hold the other party's data in accordance with this agreement, this could give rise to data access and/or use without authorisation, whether by employees or other third parties, and/or data loss or disclosure in breach of data protection laws. This in turn could give rise to litigation, regulatory action, fines, censures, claims for redress and reputational damage, and could have a material adverse effect on the Bank's business, financial condition, operating results and prospects.

57. ***The Bank's accounting policies and methods are critical to how it reports its financial condition and operating results. They require the Bank to make estimates about matters that are uncertain.***

The preparation of financial statements in accordance with the international financial reporting standards issued by the International Accounting Standards Board (the "**IASB**") as adopted by the European Commission for use in the EU ("**IFRS**") requires the use of estimates. It also requires management to exercise significant judgment in applying relevant accounting policies so that they comply with IFRS.

In the Bank's financial statements, the basis of preparation and accounting policies disclosures have identified certain accounting policies in respect of which significant judgment is required in determining appropriate assumptions and estimates when valuing assets, liabilities, commitments, provisions and contingencies. Significant judgement is also used in developing targets, forecasts and assumptions and, accordingly, there is a risk that if the judgement exercised or the estimates or assumptions used subsequently turn out to be incorrect, then this could result in significant loss to the Bank, beyond that anticipated or provided for, which could have an adverse impact on the Bank's financial condition, operating results and prospects.

These critical judgements and estimates relate to, *inter alia*, the assumptions used in the determination of loan impairment provisions, conduct risk and legal provisions, group relief receivable from the Co-operative Group, deferred tax, pension schemes, the provision relating to the Bank's separation from the Co-operative Group and effective interest rate and fair value adjustments and the accounting treatment of the Restructuring and Recapitalisation, particularly the determination that the Restructuring and Recapitalisation is not a business combination under IFRS 3 (Business Combinations).

The Bank has established policies and control procedures that are intended to ensure that these judgements (and the associated assumptions and estimates) that are applied in its financial statements are well controlled and applied consistently. In addition, the policies and procedures are intended to ensure that the process for changing accounting policies and methodologies moves forward in an appropriate manner. The Bank cannot guarantee that it will not be required to make (potentially material) changes in accounting policies, methodologies or estimates or restate prior period financial statements in the future.

There is also a risk the Bank's accounting policies and related judgements, estimates and determinations are challenged by regulatory bodies, including the Financial Reporting Council. This or any of the above potential challenges to the Bank's accounting policies or managements' judgements estimates and determinations, and any associated restatements of previously published financial statements and any related litigation against the Bank arising from any such restatements could have a material adverse effect on the Bank's financial condition, operating results or prospects.

58. ***Changes in the Bank's accounting policies or in accounting standards could materially affect how it reports its financial condition and operating results.***

From time to time, the IASB and/or the EU change the IFRS, which govern the preparation of the Bank's financial statements. These changes can be difficult to predict and could materially impact how the Bank records and reports its financial condition and operating results. In some cases, the Bank could be required to apply a new or revised standard retrospectively, resulting in restating prior period financial statements.

For example, International Financial Reporting Standard 9 (Financial Instruments: Recognition and Measurement) ("**IFRS 9**"), which is due to become effective in relation to the Bank's financial reporting after 1 January 2018, includes new requirements for the classification and measurement of financial assets and liabilities, hedge accounting and the implementation of an expected credit loss (rather than incurred loss) basis for measuring impairment of financial assets. The parallel run of the requirements of IFRS 9, which is planned to take place in the second half of 2017, is expected to provide reliable quantitative impact information which will be disclosed in the Bank's 2017 annual report and accounts. Until such a reliable estimate is available, there is a risk that IFRS 9 could have a material adverse effect on the Bank's financial condition, operating results and prospects.

Other new accounting standards that have been issued by the IASB that do not yet need to be applied by the Bank include IFRS 15 (Revenue from Contracts with Customers (2014)), amendments to IFRS 10 (Consolidated financial statements) and IAS 28 (Investments in associates and joint ventures (2014)), amendments to IAS 7 (Statement of Cash Flows), IFRS 16 (Leases), amendments to IAS 12 (Income taxes) and amendments to IFRS 2 (Share based payments). The Bank has not yet finalised its estimation of the financial impact of all of these new accounting standards and there is therefore a risk that any of these new standards could materially affect the Bank's current and future financial condition and results of operations. The IASB may make other changes to financial accounting and reporting standards that govern the preparation of the Bank's financial statements, which the Bank may adopt, or which the Bank may adopt prior to the date on which such changes become mandatory if determined to be appropriate by the Bank, or which the Bank may be required to adopt. Any such change in the Bank's accounting policies or accounting standards could materially affect its reported financial condition and operating results.

59. ***Following implementation of the Restructuring and Recapitalisation, there is a risk that the analysis undertaken in relation to accounting, regulatory or taxation treatments may have to be revised.***

The Bank has undertaken a detailed accounting, taxation and regulatory capital analysis to determine, amongst other things, the accounting, regulatory and taxation treatments which will be required following the changes to the Bank Group's organisational structure as a result of the Restructuring and Recapitalisation.

In the preparation of such analysis, significant judgement is required in various instances (for examples of the judgement required, albeit specifically with regards to accounting policies, see the risk factors entitled "*The Bank's accounting policies and methods are critical to how it reports its financial condition and operating results. They require the Bank to make estimates about matters that are uncertain*" and "*Changes in the Bank's accounting policies or in accounting standards could materially affect how it reports its financial condition and operating results.*"). Should the judgment exercised or the estimates or assumptions used by the Bank subsequently turn out to be incorrect or external auditor, adviser or statutory authority opinions change following the Restructuring and Recapitalisation, there is a risk that the pro forma financial information set out in Part 8 of this Circular may not be appropriately stated and, accordingly, may require negative adjustments to regulatory capital, accounting valuations and/or the value of tax losses available to the Bank in the future; each of which could have a material adverse effect on the Bank's financial condition, operating results or prospects.

60. ***The Bank is exposed to a number of tax risks including risk of changes in tax legislation and its interpretation and a change in the rate of corporate and other taxes.***

The Bank's activities are conducted principally in the UK and it is, therefore, subject to a range of UK taxes at various rates. Future actions by the Government to change tax rates or to impose additional taxes could reduce the Bank's profitability. Additional or revised tax legislation or changes to its interpretation might also affect the Bank's financial condition in the future, including an impact on the Bank's tax costs and the utilisation of tax losses. In addition, the Bank is subject to tax audits and enquiries by HMRC which could result in additional tax charges, including interest and penalties relating to past periods of up to six years. Any such charges could be material, which might also affect the Bank's financial condition in the future.

There is risk that the Bank could suffer losses due to additional tax charges (including interest and penalties), other financial costs or reputational damage due to: failure to comply with, or correctly assess the application of, relevant tax laws; failure to deal with tax authorities in a timely, transparent and effective manner (including in relation to historical transactions); incorrect calculation of tax estimates for reported and forecast tax numbers; or provision of incorrect tax advice. Such charges, or conducting any challenge to a relevant tax authority, could lead to adverse publicity, reputational damage and costs materially exceeding current provisions, in each case to an extent which could have an adverse effect on the Bank's operations, financial condition and prospects.

The May 2017 Outlook on the Plan assumes recognition of deferred tax assets during the life of the Plan based on a certain set of criteria (as set out in paragraph 9.2(e) in Part 7 of this Circular). There is a risk that one or more of these criteria will not be satisfied and that the Bank will be unable to recognise its deferred tax assets in the quantum expected or at all, which would increase the risk of a delay as to when the Bank expects to generate a post-tax profit in the future.

61. ***There is a risk that the Bank's insurance cover may be inadequate, that it will be difficult for the Bank to obtain insurance and that those insurance policies which the Bank has in place might become void or voidable.***

The Bank has a number of insurance policies in place with respect to its business, assets and liabilities. Any insurance that the Bank may obtain may be subject to exclusions, limitations, minimum claim amounts and excess amounts and other terms that mean that the Bank may have uninsured claims and losses. There is a risk that the terms of the Bank's insurance policies will not cover the Bank's liabilities in all situations and that the Bank may therefore have uninsured exposure. There is also a risk that the level of premium payable by the Bank may rise, to reflect the insurance market's view of the Bank's financial condition.

Any insurance cover that the Bank has in place could become void or voidable in the event of a fundamental non-disclosure of information by the Bank.

As part of the process of separating from the Co-operative Group, the Bank has prepared a list of property assets and valuations. There remain certain property assets for which ownership is unclear and no further work is being undertaken by the Bank to identify ownership of such property assets. Accordingly, there is a risk that the insured values do not fully match the rebuild/reinstatement values of the Bank's assets and therefore do not comply with certain provisions in its property insurance policies.

Any failure of the Bank to retain adequate insurance coverage in respect of any liabilities could have a material adverse effect on the Bank's business, financial condition, results of operations and prospects.

62. ***Risks relating to the Bank's freehold and leasehold interests.***

As at 31 December 2016, the Bank operated 105 branches (which the Bank is aiming to reduce to 95 by the end of July 2017) and the Bank operates 10 major sites (being head office, call centre and data centre locations utilised for banking operations) and holds 108 onerous interests (being former branch and corporate banking centres not utilised by the Bank for its operations but to which it still retains liability through title ownership). These are held on a mixture of leasehold and freehold interests and, whilst the majority relate to property which is registered at the Land Registry, there are some properties (in respect of which the Bank's interest has been held for a number of years) which comprise unregistered land. Accordingly, there is a risk this lack of registration could result in potential disputes or challenges to ownership or title.

The Bank also owns personal property and there is a risk that any real or personal property is not held with title absolute (for example, some real property leases may comprise good leasehold title) or that they are not, without a full title investigation, free and clear of all liens, encumbrances, restrictions, cautions, notices or inhibitions and defects such that they do not individually or in aggregate materially affect the value of, or interfere with the use made (or proposed to be made) by the Bank or any of its subsidiaries.

Additionally there is a risk, in the absence of a current investigation, that leases to any real property and buildings are not subsisting and enforceable and contain exceptions which could materially interfere with the use made and/or proposed to be made of such property and buildings or would individually, or in aggregate, result in a material change to the day to day business operations of the Bank, which could have an adverse impact on the Bank's operations, financial results and condition.

63. ***Risks relating to health and safety.***

The Bank has historically failed to manage many aspects of its health and safety obligations effectively, and as a result is in breach of a number of technical areas of health and safety, and fire safety legislation, with further improvements needed (for example, in respect of fire risk assessments and proactive asbestos management plans). Although the risk of personal injury or illness to employees, customers and those who visit the Bank's premises is considered by the Bank to be low given the hazard profile of the environment in which the Bank operates, until these known shortcomings in health and safety management are remediated, there is a higher risk of the Bank being unable to successfully defend an action should an incident arise. Furthermore, until such remediation is complete the Bank may have some exposure to risk of enforcement action from the Health and Safety Executive, Fire and Rescue Service(s), which could have an adverse effect on the Bank's business, financial condition, operating results and prospects.

Risks relating to the A Shares and the B Shares

64. ***The A Shares will not carry any voting rights save where there are no B Shares in issue and in certain other limited circumstances. Consequently, following completion of the Restructuring and Recapitalisation, unless a holder of A Shares, together with its affiliates, holds 10 per cent. or more of the A Shares (and fulfils other criteria) entitling such holder to receive B Shares (which carry voting rights and other benefits and rights) in proportion to their respective holding of A Shares, A Shareholders will not have any voting interests in Holdco and Holdco will be controlled by the B Shareholders. Furthermore, the B Shares will entitle their holders to different rights than those conferred by ownership of the A Shares and the interests of the B Shareholders may conflict with those of A Shareholders.***

The share capital of Holdco will comprise two classes: (i) A Shares; and (ii) B Shares. The A Shares bear the primary economic interest in Holdco. The A Shares entitle holders to participate in distributions but do not carry any voting rights except on matters at a general meeting affecting the rights of A Shareholders as a class and certain other matters (as further described in paragraph 4.3 of Part 15 of this Circular). Furthermore, if at any time: (a) there are no B Shares in issue or all B Shares in issue are subject to a notice from the Holdco Board that they will be redeemed or bought back; or (b) Holdco ceases to own (directly or indirectly) more than 50 per cent. of the shares of the Bank as a result of a mandatory write-down or bail-in or the automatic conversion of securities by reason of the Bank failing to meet certain regulatory thresholds in respect of any security issued by Issuerco or the Bank, the voting rights provided under the B Shares will vest in the A Shares (save that in circumstances where an A Shareholder owns 10 per cent. or more of the A Shares, such A Shareholder will only be able to exercise the votes attaching to those A Shares if it has been approved by the PRA and the FCA as a "controller" for the purposes of Part 12 of FSMA).

The B Shares carry all of the voting rights at a general meeting of Holdco and also provide certain governance, notification and approval rights with respect to the Holdco Group, but do not entitle holders to participate in distributions. Furthermore, B Shareholders are entitled to the Exit Premium, as further described in paragraph 4.4 of Part 15 of this Circular.

Holders of A Shares are only eligible to receive B Shares if they hold (together with their affiliates) at least 10 per cent. of the A Shares (and fulfil certain other criteria). Consequently, save in the limited circumstances described above, holders of less than 10 per cent. of the A Shares will not have any voting interests in Holdco. As a result of the dilution that holders of Ordinary Shares will suffer under the Share Transfer upon implementation of the Members' Scheme, a holder of Ordinary Shares will not, unless such holder is also a Subordinated Noteholder who receives A Shares pursuant to the Notes Exchange and/or subscribes for additional A Shares pursuant to the Scheme Creditors' Equity Subscription or the Backstop Arrangements in such numbers as are sufficient to result in that holder holding 10 per cent. or more of the A Shares, and will not, therefore, have any voting rights in Holdco (and accordingly no indirect voting interests in the Bank).

See paragraphs 4.3 and 4.4 of Part 15 for further details on the rights attaching to each of the A Shares and the B Shares.

As the B Shares, save in the limited circumstances described above, hold all the voting rights, the B Shareholders collectively will have the ability to control the outcome of all matters requiring Holdco shareholder approval, including: (a) the election of directors; (b) the approval of certain business decisions, including significant corporate transactions; (c) amending the Holdco Articles of Association; (d) disapplying pre-emption rights; and (e) requesting court approved capital reductions. They will also be able to, among other things, prevent, delay or deter any future change of control of Holdco, which could deprive Shareholders of an opportunity to earn a premium for the resale of their A Shares over the then prevailing market price.

The Bank has been informed that, based on their commitments under the Lock-Up Agreement, their holdings of Ordinary Shares and Subordinated Notes, as applicable, as at 25 July 2017 (being the latest practicable date prior to the date of this Circular), and assuming each of them have been issued and subscribes for (as the case may be) their full entitlement of (where applicable): (i) A Shares pursuant to the Share Transfer (including the Early Bird Members' Premium); (ii) A Shares pursuant to the Notes Exchange; (iii) A Shares pursuant to the Equity Subscriptions; and (iv) their pro rata share of the Backstop Consideration Shares, and taking into account their holdings of Incorporation Shares (where applicable), and further assuming that: (a) no other Qualifying Scheme Creditors have acceded to the Backstop Arrangements following 25 July 2017 (being the latest practicable date prior to the date of this Circular); (b) no other Shareholder has become entitled to share in the Early Bird Members' Premium following 25 July 2017 (being the latest practicable date prior to the date of this Circular); (c) the Subscription Shares have been subscribed for in full by the Qualifying Shareholders and Qualifying Scheme Creditors, as applicable; and (d) £30 million in principal amount of 2023 Notes are subject to the Mandatory Cancellation, upon Completion:

- Silver Point Capital will hold approximately 28 per cent. of the expected initial issued B Shares;
- GoldenTree will hold approximately 25 per cent. of the expected initial issued B Shares;
- Anchorage Capital Group will hold approximately 16 per cent. of the expected initial issued B Shares;
- Invesco will hold approximately 16 per cent. of the expected initial issued B Shares; and
- Cyrus Capital Partners will hold approximately 15 per cent. of the expected initial issued B Shares.

Consequently, by virtue of the level of their voting power described above, each of Silver Point Capital, GoldenTree, Anchorage Capital Group, Invesco and Cyrus Capital Partners will possess sufficient voting power to have a significant influence over all matters requiring B Shareholder approval. In particular, Silver Point Capital will have, and in practice GoldenTree is expected to have, sufficient voting power to: (a) block matters requiring the approval of B Shareholders by special resolution without the support of any other B Shareholders, such as amending the Holdco Articles of Association, disapplying pre-emption rights, and requesting court approved capital reductions, the election of directors and approval of certain business decisions, including significant corporate transactions; and (b) influence significantly the outcome of certain matters requiring the approval of B Shareholders by ordinary resolution either by blocking (with the need for the support of other B Shareholders) or by exercising substantial influence over any such ordinary resolutions, such as those relating to the election of directors and approval of certain business decisions, including significant corporate transactions.

In addition to having voting control, the B Shareholders together also have the right to nominate up to two Holdco Directors to the Holdco Board and, via Holdco's ownership of the Bank, the Board (the "**B Shareholder Nominee Directors**"). To the extent that such B Shareholder Nominee Directors are executive directors, such B Shareholder Nominee Directors will be involved in the day-to-day management of the Holdco Group, including at the Bank, and consequently in such circumstances, through their entitlement to appoint the B Shareholder Nominee Directors, the B Shareholders would be able to exert significant influence (notwithstanding that the B Shareholder Nominee Directors will owe a fiduciary duty to Holdco and the Bank, as the case may be, and must act in good faith in a manner they reasonably believe to be in the best interests of Holdco or the Bank, as the case may be, as a whole) on the day-to-day operations of the Holdco Group, including at the Bank, which could include, among other things, shaping the strategic direction of the Bank and the Holdco Group. It is possible that the interests of Holdco will differ from those of its shareholders, or any class of them.

It is possible that the interests of the A Shareholders and the B Shareholders will differ, whether as a result of the differing class rights or otherwise. For example, the B Shareholders have preferred rights on the return of capital on a winding-up of Holdco and the A Shareholders may not transfer their A Shares to a Commercial Competitor of the Bank without the sanction of a special resolution of Holdco. There could also be a conflict between the interests of the B Shareholders, or those of the Principal Investors, and the interests of Holdco's other shareholders with respect to, for instance, any future dividend policy that Holdco may propose. There can be no assurance that the interests of the B Shareholders, or those of the Principal Investors, will coincide with the interests of Holdco's other shareholders or that the B Shareholders, including the Principal Investors, will act in a manner that is in the best interests of Holdco.

Furthermore, pursuant to the terms of the Holdco Articles of Association, if any person (or group) acquires more than 75 per cent. of the A Shares, then they shall be entitled to require the remaining A Shareholders to sell them their A Shares on the best terms given by the acquirer in the previous 12 months provided they make a payment to each B shareholder equal to that it would have triggered if such transaction were an exit for the purposes of triggering an Exit Premium by Holdco (the "**Drag Along Rights**"). Consequently, any A Shareholder whose A Shares are acquired pursuant to the exercise of the Drag Along Rights may not receive the value for their A Shares that they had ascribed to them and, provided such acquirer complies with the terms of the Drag Along Rights, will otherwise be unable to prevent the sale of such A Shares to such acquirer.

65. ***Shareholders will experience significant dilution to their ownership interests following completion of the Restructuring and Recapitalisation.***

Pursuant to the Share Transfer under the terms of the Members' Scheme, Shareholders will transfer their Ordinary Shares to Holdco in exchange for A Shares representing in aggregate approximately 5 per cent. of the total number of fully-diluted issued A Shares of Holdco immediately following Completion (including the Early Bird Members' Premium). Consequently, upon implementation of the Members' Scheme, a holder of Ordinary Shares will experience significant dilution with respect to its relative ownership interests in the Bank prior to completion of the Restructuring and Recapitalisation as compared to their ownership interests in Holdco following completion of implementation of the Restructuring and Recapitalisation.

The precise level of absolute dilution a holder of Ordinary Shares will suffer (assuming that such Shareholder is not also a Subordinated Noteholder who receives A Shares pursuant to the Notes Exchange and/or subscribes for additional A Shares pursuant to the Scheme Creditors' Equity Subscription or the Backstop Arrangements) as a consequence of the Restructuring and Recapitalisation will depend upon the precise number of A Shares that are issued upon completion of the Restructuring and Recapitalisation and whether such holder of Ordinary Shares is a Qualifying Shareholder who subscribes for additional A Shares under the terms of the Members' Equity Subscription and whether such holder of Ordinary Shares is entitled to receive the Early Bird Members' Premium.

Upon completion of the Restructuring and Recapitalisation, assuming that a holder of Ordinary Shares:

(a) does not, or is not permitted under the terms and conditions of the Members' Equity Subscription to, subscribe for additional A Shares pursuant to the Members' Equity Subscription and is not entitled to receive the Early Bird Members' Premium, such Shareholder will suffer a dilution of 95.25 per cent. to their existing interests; and

(b) is permitted under the terms and conditions of the Members' Equity Subscription to subscribe for additional A Shares pursuant to the Members' Equity Subscription and elects to subscribe for the maximum number of additional A Shares such Shareholder is entitled to subscribe for under the terms of the Members' Equity Subscription and is entitled to receive the Early Bird Members' Premium, such Shareholder will suffer a dilution of 91.6 per cent. to their existing interests assuming all Shareholders under the Members' Scheme receive the Early Bird Premium;

in each case assuming that such Shareholder is otherwise not also a Subordinated Noteholder who receives A Shares pursuant to the Notes Exchange and/or subscribes for additional A Shares pursuant to the Scheme Creditors' Equity Subscription or the Backstop Arrangements.

For further information, see paragraph 14 of Section A of Part 1 of this Circular, which sets out the dilutive impact of the components of the Restructuring and Recapitalisation.

66. ***No dividends to be paid in respect of the A Shares in the near future.***

Following completion of the Restructuring and Recapitalisation, Holdco will be the holding company of the Bank and will be dependent on the payment of dividends, distributions, loans or advances by its subsidiaries, including the Bank, to produce distributable reserves. Holdco's ability to pay dividends on the A Shares and effect certain returns of capital will be dependent upon, amongst other things, it having sufficient cash resources and, where necessary, sufficient distributable reserves out of which any proposed dividend may be paid. Any payment of dividends, distributions, loans or advances to Holdco by its subsidiaries, including the Bank, will be dependent upon the business and financial condition, earnings and cash flow position and other factors affecting such subsidiaries, including in particular those matters described below affecting the ability and timing of any dividend to be paid by the Bank.

Furthermore, the Bank does not expect to pay dividends in the near future, and is only targeting potential dividends from 2021 in the May 2017 Outlook on the Plan. The Bank's ability to pay any dividends at any time in the future is subject to the Bank's compliance with regulatory capital and loss-absorbing capacity requirements, including the Combined Buffer (currently comprised only of its capital conservation buffer and set at 1.25 per cent. of total RWAs met entirely by CET1 capital. The capital conservation buffer is set to rise to 2.5 per cent. of total RWAs met entirely by CET1 capital in 2019 with a rise of 0.625 per cent. in both 2018 and 2019. In addition to the capital conservation buffer, the counter-cyclical capital buffer will rise from the current requirement of zero per cent. to 0.5 per cent. of total RWAs in June 2018 and is expected to rise to 1 per cent. of total RWAs by the end of 2018, which would result in an aggregate Combined Buffer requirement of 3.5 per cent. of total RWAs in 2019), which dictates the Maximum Distributable Amount available for distribution by way of dividends pursuant to the restrictions imposed under CRD. Furthermore, distribution by way of dividend will be dependent on the availability of distributable reserves, PRA approval and compliance by the Bank with provisions concerning dividends contained in its Articles of Association (for further information see paragraph 4 of Part 16 of this Circular). In addition, the availability of distributable reserves is expected to be reliant on a shareholder and court-approved reduction of share capital. There is no certainty that any such approvals will be forthcoming if and when such approvals are sought in the future.

The Bank can give no assurance that neither it nor, following completion of the Restructuring and Recapitalisation, Holdco, will pay any dividends in the future, nor, if a dividend is paid, what the amount of such dividend will be. Furthermore, until the Bank meets full ICG and compliance with its Combined Buffer and its MREL, the Bank may be prevented from making discretionary payments, including dividends to Holdco.

67. ***A Shareholders may not be able to realise returns on their investment in A Shares.***

The A Shares are not listed on the Official List, nor are they admitted to the London Stock Exchange. They are, therefore, expected to be illiquid, as there will be a limited number of A Shareholders and there is no public market for the A Shares. It is likely that a liquid market in the shares will never develop and, consequently, A Shareholders may not be able to realise their investment in the A Shares. In addition, A Shares will lack voting rights (save for in limited circumstances) which may impact their value. Furthermore, upon completion of the Restructuring and Recapitalisation, there will be a number of new shareholders in Holdco who were formerly Subordinated Noteholders. Such new shareholders may ascribe a different value to the A Shares than the current Shareholders, which could exacerbate the risk of such Shareholders not being able to realise their investment in the A Shares.

68. ***The ability of Overseas Shareholders to bring actions or enforce judgments against the Bank, Holdco or the Bank's and/or Holdco's directors may be limited.***

The ability of an Overseas Shareholder to bring an action against the Bank or Holdco may be limited under relevant laws. The Bank is a public limited company incorporated in England and Holdco is a limited liability company incorporated in England. The rights of Shareholders are governed by the laws of England and Wales and by the Articles of Association of the Bank. The rights of shareholders in Holdco will be governed by the laws of England and Wales and by the Holdco Articles of Association and the B Shareholders' Agreement. These rights differ from the rights of shareholders in typical U.S. corporations and some other non-UK corporations. In particular, the laws of England and Wales significantly limit the circumstances under which shareholders of companies may bring derivative actions. Under such laws, generally only a company can be the proper claimant in proceedings in respect of wrongful acts committed against it. In addition, it may be difficult for an Overseas Shareholder to prevail in a claim against the Bank or Holdco under, or to enforce liabilities predicated upon, non-UK securities laws.

Furthermore, pursuant to paragraph 10 of Part 12 of this Circular, it is a term and condition of the Members' Equity Subscription that any subscriber irrevocably and unconditionally assents to and sanctions, to the fullest extent permitted by law, the waiver of all rights and entitlements that it has or acquires to bring, participate in or enforce legal proceedings of any nature against the Bank and/or Holdco in connection with the Subscription Shares and/or the Members' Equity Subscription other than in the English and Welsh courts.

An Overseas Shareholder may not be able to enforce a judgment against some or all of the directors of the Bank and/or Holdco. It may not be possible for an Overseas Shareholder to effect service of process upon the Bank's and/or Holdco's directors and executive officers within the Overseas Shareholder's country of residence or to enforce against the Bank's and/or Holdco's directors and executive officers judgments of courts of the Overseas Shareholder's country of residence based on civil liabilities under that country's securities laws. There is a risk that an Overseas Shareholder will not be able to enforce any judgments in civil and commercial matters or any judgments under the securities laws of countries other than the UK against the Bank's and/or Holdco's directors or executive officers who are residents of the UK or countries other than those in which judgment is made. In addition, English or other courts may not impose civil liabilities on the Bank's and/or Holdco's directors or executive officers in any original action based solely on foreign securities laws brought against the Bank or Holdco or the Bank's and/or Holdco's directors in a court of competent jurisdiction in England or other countries.

69. ***Shareholders outside the UK may be subject to exchange rate risk.***

The A Shares and any dividends to be paid in respect of them, will be, denominated in pounds sterling. A holding of A Shares by an investor whose principal currency is not sterling exposes that investor to foreign currency exchange rate risk. Any depreciation of sterling in relation to such foreign currency will reduce the value of the investment in the A Shares or any dividends in foreign currency terms, and any appreciation of sterling will increase the value in foreign currency terms. Government and monetary authorities may impose (as some have done in the past) exchange rate controls that could adversely affect an applicable exchange rate.

70. ***The Bank may apply the proceeds of the Holdco Subscriptions to uses that Shareholders may not agree with or in ways that do not increase the Bank's and/or Holdco's profits or share value.***

The Bank will have considerable discretion in the application of the net proceeds of the Holdco Subscriptions received by the Bank and potential investors must rely on the judgment of the Directors regarding the application of such proceeds. The net proceeds may be used for corporate purposes that do not increase the Bank's and/or Holdco's profitability or increase Holdco's share value. Furthermore, they may be placed in investments that fail to produce income or that lose value.

71. ***The ability to participate in the Members' Equity Subscription will not be available to any person: (i) with a registered address in the United States (save for Shareholders who the Bank reasonably believes are either QIBs or Accredited Investors); (ii) in the EEA who is not a Qualified Investor; or (iii) in any of the other Excluded Territories, and as a result Shareholders who are not permitted to participate will experience significant dilution of ownership in the Bank.***

The ability to participate in the Members' Equity Subscription will not be available to any person with a registered address in, or who is resident or located in, the United States (save for Shareholders who the Bank reasonably believes are either QIBs or Accredited Investors), in the EEA who are not Qualified Investors or any of the Excluded Territories and possibly other overseas jurisdictions, unless an exemption is available. Accordingly, subject to certain exemptions, Shareholders with a registered address in the United States (save for Shareholders who the Bank reasonably believes are either QIBs or Accredited Investors) or any of the Excluded Territories or any other such overseas jurisdictions will be unable to take up their Members' Equity Subscription Entitlement. The proportionate economic and voting interests of such Shareholders will, therefore, be diluted (in addition to the dilution that they will suffer as consequence of the implementation of the Notes Exchange, the Members' Scheme and the Scheme Creditors' Equity Subscription).

72. ***Failure to comply with the procedures of the Members' Equity Subscription may result in Shareholders being unable to participate successfully in the Members' Equity Subscription. Shareholders are responsible for complying with all of the procedures for participating in the Members' Equity Subscription which are set out in the relevant paragraphs of Part 13 of this Circular.***

There are certain restrictions imposed on the participants in the Members' Equity Subscription (including as to their status as QIB or Accredited Investor, or as a Qualified Investor, if they are resident or located in the U.S. or the EEA, respectively). Furthermore, Shareholders will be deemed to make a number of acknowledgements, representations, warranties and undertakings on submission of an Application Form or CREST acceptance. Failure to comply with such restrictions or any such acknowledgements, representations, warranties and undertakings could result in, among other things, such Shareholder not being permitted to participate in the Members' Equity Subscription.

ANNEX

DEFINITIONS

“10-13 LR”	*Chapter 10: (Significant Transactions), Chapter 11: (Related Party Transactions), Chapter 12: (Dealing in own securities and treasury shares)* and Chapter 13: *(Contents of Circulars) o*f the Listing Rules
“2006 Agreement”	the agreement dated 16 February 2006 entered into by the Bank and CFSMS in relation to the provision of shared IT assets and the on-supply of certain third-party services by CFSMS
“2010 PD Amending Directive”	Directive 2010/73/EU
“2013 Liability Management Exercise”	the consent solicitation and scheme of arrangement of the Bank and the Co-operative Group to raise £1.2 billion of capital in 2013, announced on 4 November 2013 and completed on 20 December 2013 consisting of the transfer of certain preference shares and the extinguishment of multiple subordinated liabilities, followed by the recognition of a single tranche of subordinated debt, undertaken as part of the 2013 Recapitalisation Plan
“2013 Recapitalisation Plan”	the Co-operative Group and the Bank completed a recapitalisation plan, originally announced on 17 June 2013, to meet a £1.5 billion CET1 capital shortfall in 2013 which included: the 2013 Liability Management Exercise; CET1 capital contributions from CBG; and interest savings on securities surrendered in the 2013 Liability Management Exercise
“2014 Institutional Shareholder(s)”	each of Silver Point Capital, Perry Capital, Invesco Asset Management Limited and York Capital Management Europe (UK) Advisers LLP
“2014 Plan”	has the meaning given to it in Part 3 of this Circular
“2014 Shareholder Rights Agreement”	the agreement between the Co-operative Group, CBG, the 2014 Institutional Shareholders and the Bank dated 9 May 2014, as described in paragraph 17.5 of Part 16 of this Circular
“2023 Noteholder Extraordinary Resolutions”	the 2023 Notes First Extraordinary Resolution and 2023 Notes Second Extraordinary Resolution, individually or taken together, as the context requires, in each case to be proposed at the 2023 Noteholder Meeting as set out in the relevant notice convening each 2023 Noteholder Meeting, The 2023 Notes Second Extraordinary Resolution shall be conditional on the passing and implementation of the 2023 Notes First Extraordinary Resolution
“2023 Noteholders”	the holders of the 2023 Notes
“2023 Noteholder Meeting”	the meeting convened, in connection with the Consent Solicitation, for the holders of the 2023 Notes to vote on the 2023 Noteholder Extraordinary Resolutions proposed at such meeting (and if such meeting is adjourned, shall include the adjourned meeting)
“2023 Notes”	the Bank’s £206,000,000 11% Subordinated Notes due 2023 (ISIN: GB00BFXW0853)

“**2023 Notes First Extraordinary Resolution**”..	the first extraordinary resolution proposed at the 2023 Noteholder Meeting, as set out in the notice to such meeting
“**2023 Notes Retail Confirmation Deadline**”...	10.1 a.m. on the third Business Day following, but not including, the Members’ Scheme Effective Date
“**2023 Notes Second Extraordinary Resolution**”..	the second extraordinary resolution proposed at the 2023 Noteholder Meeting, as set out in the notice of such meeting
“**2023 Trust Deed**”.............................	the trust deed constituting the 2023 Notes dated 20 December 2013 made between the Bank and Law Debenture Trustees Limited
“**2025 Notes**”......................................	the £250,000,000 Fixed Rate Reset Callable Subordinated Tier 2 Notes due 2025 (ISIN: XS1249403541)
“**A Share**”...	a class A ordinary share of £0.0001 in the capital of Holdco
“**A Shareholders**”..............................	the holders of A Shares from time to time
“**A Share Governance Event**”..........	has the meaning given to it in paragraph 4.3 of Part 15 of this Circular
“**Acceptable Security Asset**”............	an acceptable security asset being either: (i) gilt-edged securities issued by the government of the United Kingdom; (ii) any debt or equity security that is listed and freely tradable and is rated either: (a) AAA by Standard & Poor’s Ratings Services, a division of The McGraw Hill Companies, Inc.; (b) AAA by Fitch Ratings Ltd.; or (c) Aaa by Moody’s Investors Service Limited, or, in each case, any successor to or transferee of the ratings business of such party; or (iii) cash denominated in pounds sterling.
“**Accredited Investor**”.......................	an “accredited investor” (as defined in Regulation D of the U.S. Securities Act of 1933)
“**Additional Backstop Provider**”.....	has the meaning given to it in paragraph 6 of Section A of Part 1 of this Circular
“**Additional Tier 1**” or “**AT1**”...........	means Additional Tier 1 capital as defined in the CRR
“**Ad-Hoc Committee**”.......................	the informal committee of Subordinated Noteholders formed for the purpose of negotiating the terms of the Restructuring and Recapitalisation with the Bank.
“**Adjusted Loss Forecast**”................	has the meaning given to it in paragraph 6.1 of Part 7 of this Circular
“**Advanced Internal Ratings Based Approach**” or “**IRB Approach**”.......	advanced internal ratings based approach stipulated within CRR allows a more sophisticated and risk sensitive approach to calculate credit risk. It is more advanced than Foundation Internal Ratings Based approach as probability of default, loss given default and exposure at default parameters are derived by the Bank

"**Advisers**"	(a) Clifford Chance LLP; (b) Paul Hastings (Europe) LLP and any other adviser retained to advise the Principal Investors via Paul Hastings (Europe) LLP; (c) Houlihan Lokey EMEA, LLP; (d) PJT Partners Inc; (e) UBS Limited; (f) Merrill Lynch International; (g) Linklaters LLP; (h) Lansons Communications LLP; and (i) Grant Thornton UK LLP, and any of their directors, partners, employees and Affiliates;
"**Affiliates**"	in respect of a person or entity: (a) a subsidiary of that person or entity or a holding company of that person or entity or any other subsidiary of such a holding company; and (b) any Affiliated Entities of any of the persons or entities referred to in sub-paragraph (a) above
"**Affiliated Entities**"	means (a) in relation to a fund (the "**first fund**"), (i) a fund which is managed or advised by the same investment manager or investment adviser as the first fund or, (ii) if it is managed by a different investment manager or investment adviser, a fund whose investment manager or investment adviser is an associate of the investment manager or investment adviser of the first fund or which is a coinvestment vehicle under common control with the first fund; and (b) in relation to any other person, a fund which is managed or advised by such person or any of its associates
"**AGM**"	an annual general meeting of the Bank
"**Alternative Performance Measures**" or "**APMS**"	alternative performance measures (as defined in the ESMA Guidelines on Alternative Performance Measures)
"**AML**"	anti-money laundering
"**Anchorage Capital Group**"	funds managed and/or advised by Anchorage Capital Group, LLC
"**Annual Allowance**"	the "annual allowance" as defined in section 228 of the Finance Act 2004
"**API**"	application programming interface
"**applicant**"	has the meaning given to it in paragraph 3.3 of Part 12 of this Circular
"**Application Form**"	the personalised application form on the basis of which Provisional Qualifying Non-CREST Shareholders may apply for their pro rata share of the Subscription Shares under the Members' Equity Subscription

"**Articles of Association**"	the articles of association of the Bank adopted on 15 November 2013
"**Audit Committee**"	the audit committee of the Board
"**Authorities**"....................................	HM Treasury, the Bank of England, the FCA and/or the PRA
"**B Share**"	a class B redeemable preference share of £0.01 in the capital of Holdco
"**B Shareholder Nominee Directors**"	has the meaning given to it in paragraph 10 of Part 2 of this Circular
"**B Shareholders**"	the holders of B Shares from time to time
"**B Shareholders' Agreement**"	means the shareholders' agreement to be entered into between the B Shareholders and Holdco on or around the Settlement Date
"**B Shares Subscription**"	has the meaning given to it in paragraph 5 of Section A of Part 1 of this Circular
"**BaCB**"	business and commercial banking
"**Backstop Accession right**".............	has the meaning given to it in paragraph 6 of Section A of Part 1 of this Circular
"**Backstop Agreement**".....................	a backstop agreement between the Principal Investors, the Bank, Holdco and the Information Agent dated 14 July 2017 in respect of the Backstop Arrangements
"**Backstop Arrangements**"	has the meaning given to it in paragraph 6 of Section A of Part 1 of this Circular
"**Backstop Commitment**"................	has the meaning given to it in paragraph 6 of Part 2 of this Circular
"**Backstop Consideration Shares**"...	has the meaning given to it in paragraph 5 of Section A of Part 1 of this Circular
"**Backstop Providers**"	has the meaning given to it in paragraph 6 of Section A of Part 1 of this Circular
"**Bank**"...	The Co-operative Bank p.l.c., a company incorporated in England and Wales (registered number 00990937), whose registered office is at P.O. Box 101, 1 Balloon Street, Manchester M60 4EP
"**Bank Incentive Plans**"	means the LTIP, the DBP and TDAP
"**Bank Exit**"	has the meaning given to it in Part 16 of this Circular
"**Bank Group**"	the Bank and its subsidiaries and subsidiary undertakings from time to time
"**Bank Section**".................................	the section of Pace for which the Bank is responsible
"**Banking Act**"	the Banking Act 2009, as amended
"**Bank's Historical Business Classification**"	the historical "Core Business"/"Non-core Business" classification as further described in Part 4 of this Circular
"**Basel 2.5**"	the first stage of the strengthening of requirements laid out in Basel II, with changes focusing on trading book and securitisations. Basel 2.5 was implemented in the UK via the FSA Handbook

"**Basel II**"	a statement of best practice issued by the Basel Committee, that defines the methods by which firms should calculate their regulatory capital requirements to retain enough capital to protect the financial system against unexpected losses. Basel II became law in the EU Capital Requirements Directive, and was implemented in the UK via the FSA Handbook. References to Basel II in this Circular are made in accordance with Basel 2.5
"**Basel III**"	the second stage of the strengthening of, and a supplement to, the requirements laid out in Basel II. Basel III is a broader review of every aspect of the international prudential framework for capital requirements, developed by the Basel Committee on Banking Supervision
"**Basel IV**"	the Basel III framework
"**Basel Committee**"	Basel Committee on Banking Supervision
"**BBA**"	the British Banker's Association
"**Beneficial Owner**"	a person who is the owner of (i) an interest in a particular principal or principal amount of 2023 Notes held in a Clearing System, as shown in the records of the relevant Clearing System or its Direct Participants, or (ii) a Note in certificated form held outside the Clearing Systems.
"**Blocking Instructions**"	(a) with respect to non-CREST Notes, custody instructions delivered to the relevant clearing system, which will block such non-CREST Notes from trading, and pursuant to which non-CREST Scheme Creditors may (among other things) issue electronic instructions to participate in the Creditors' Equity Subscription and the Backstop Arrangements; and (b) with respect to CREST Notes, a TTE Instruction
"**Bluemountain Capital Management**"	funds managed and/or advised by Bluemountain Capital Management LLC
"**Board**"	the Board of directors from time to time of the Bank
"**Board Committee**"	a committee of the Board
"**Britannia**"	Britannia Building Society
"**Britannia Scheme**"	the Britannia pension scheme
"**Britannia Trustee**"	the trustee of the Britannia Scheme
"**BRRD**"	the EU Bank Recovery and Resolution Directive (2014/59/EU)
"**Business Banking**"	the business banking sub-segment of the BaCB
"**Business Day**"	a day other than a Saturday or Sunday or public holiday in England and Wales
"**Calico**"	Calico Finance Number One Limited
"**Capita**"	Western Mortgage Services Limited (a subsidiary of Capita PLC)

“**Capita Agreement**”	the agreement between the Bank and Capita entered into on 1 August 2015, as described in paragraph 17.6 of Part 16 of this Circular
“**capital conservation buffer**”	CET1 capital equal to 2.5 per cent. of an institution’s total risk exposure amount (subject to transitional provisions to 2019)
“**Capital Raising**”	(a) the Equity Subscriptions; and (b) the Notes Exchange
“**CASS**”	current account switching service
“**CBG**”	the Co-operative Banking Group Limited
“**CCA**”	Consumer Credit Act 1974, as amended
“**Certificated Holding Consent Instruction**”	the form of Consent Instruction to be submitted by Eligible 2023 Noteholders who hold 2023 Notes in certificated form outside the Clearing Systems and who wish to vote in favour of the Proposals
“**CFSMS**”	CFS Management Services Limited
“**CFSMS Agreement**”	the agreement between the Bank and CFSMS entered into on 30 March 2007, as described in paragraph 17.7 of Part 16 of this Circular
“**CFSMS-Bank 2006 Agreement**”	the agreement dated 16 February 2006 in relation to the provision of assets and personnel to the Bank by CFSMS
“**Chairman**”	the chairman of the Board from time to time
“**Chief Executive Officer**”	the chief executive officer of the Bank from time to time
“**Chief Financial Officer**”	the chief financial officer of the Bank from time to time
“**Chief Risk Officer**”	the chief risk officer of the Bank from time to time
“**Circular**”	this document
“**Circular Date**”	the date on which this Circular is posted to Shareholders
“**CISGIL**”	CIS General Insurance Limited
“**CMA**”	Competition and Markets Authority
“**Co-existence Principles**”	the co-existence principles agreed in 2013 between the Bank and the Co-operative Group
“**CoAM**”	Co-operative Asset Management
“**Code**”	the City Code on Takeovers and Mergers
“**Combined Buffer**”	means, broadly, the combination of the capital conservation buffer, the institution-specific counter-cyclical buffer and the higher of (depending on the institution) the systemic risk buffer, the global systemically important institutions buffer and the other systemically important institution buffer, in each case as applicable to the institution. The system risk buffer does not currently apply to the Bank and is not expected to apply over the life of the Plan. The capital conservation buffer will increase by 0.625 per cent. of RWAs each year until it reaches the applicable limit of 2.5 per cent. (which will be reached in 2019). The counter-cyclical capital buffer is currently set at zero but will increase to 0.5 per cent. of RWAs in

	June 2018 and is expected to rise to 1.0 per cent. of RWAs by the end of 2018
"**Commercial Competitor**"	has the meaning given to it in paragraph 4.3(d) of Part 5 of this Circular
"**Common Equity Tier 1**" or "**CET1**"	as defined in accordance with the CRR
"**Companies Act**"	the Companies Act 2006, including any statutory modification or re-enactment thereof
"**Completion**"	the completion of the Restructuring and Recapitalisation in accordance with the terms of the Restructuring Deed
"**Completion Time**"	has the meaning given to it in the Restructuring Deed set out in Annex 1 to Part 13 of this Circular
"**Compliance Statement**"	the non-legally binding agreement between the Bank and Co-operatives UK
"**Consent Instructions**"	an instruction by which a Noteholder may participate in the Consent Solicitation in accordance with its terms
"**Consent Solicitation**"	the invitation by the Bank to Eligible 2023 Noteholders to consent to the approval of the 2023 Noteholder Extraordinary Resolutions in respect of the Proposals on the terms described in the Consent Solicitation Memorandum
"**Consent Solicitation Conditions**"	the following conditions which must be satisfied in order for the Mandatory Cancellation of the 2023 Notes to occur: (i) the passing of both of the 2023 Notes First Extraordinary Resolution and the 2023 Notes Second Extraordinary Resolution in respect of the 2023 Notes by the relevant Noteholders, and the satisfaction of the Eligibility Condition relating to the 2023 Notes Second Extraordinary Resolution; (ii) (A) the Creditors' Scheme being approved by the requisite majority of the Scheme Creditors at the Creditors' Scheme Court Meeting and sanctioned by the Court; (B) an office copy of the sanction order must be delivered to the Registrar of Companies at Companies House; and (C) the Creditors' Scheme becoming unconditional in accordance with its terms; (iii) (A) the Members' Scheme being approved by the requisite majority of the Scheme Shareholders at the Members' Scheme Court Meeting and sanctioned by the Court; (B) an office copy of the sanction order must be delivered to the Registrar of Companies at Companies House; and (C) the Members' Scheme becoming unconditional in accordance with its terms: (iv) the successful completion of the Equity Subscriptions; and (v) the passing of the Resolutions at the General Meeting
"**Consent Solicitation Expiration Deadline**"	10.1 a.m. on 18 August 2017 (subject to the right of the Bank to amend such date upon notice to Subordinated Noteholders)

“**Consent Solicitation Memorandum**”.................................	the consent solicitation memorandum dated the date of this Circular circulated to 2023 Noteholders with respect to the Consent Solicitation
“**Consenting Holders**”......................	has the meaning given to it in paragraph 6 of Section A of Part 1 of this Circular
“**Co-operative Group**”	Co-operative Group Limited or Co-operative Group Limited and its subsidiary undertakings, as the context requires
“**Co-operative Group Nominee Director**”...	a director appointed by the Co-operative Group to the Board, as described in paragraph 4.17 of Part 16 of this Circular
“**Co-operative Group Section**”.........	the section of Pace for which the Co-operative Group is responsible
“**Co-operatives UK**”.........................	Co-operatives UK Limited
“**Core Business**”................................	lines of business that are consistent with the Bank’s strategy and risk appetite. This historical classification is no longer used by the Bank following 31 December 2016
“**Counter-cyclical capital buffer**”	CET1 capital equal to the weighted average of the buffers in effect in the jurisdictions to which an institution has a credit exposure relative to an institution’s total risk exposure amount. The UK rate is currently set by the Bank of England’s Financial Policy Committee at zero per cent. On 27 June 2017, the FPC announced an increase of the counter-cyclical capital buffer to 0.5 per cent. of RWAs (effective from June 2018). Absent a material change in the FPC’s outlook, and consistent with its stated policy for a standard risk environment, the FPC also announced that it expects to further increase the rate to 1 per cent. of RWAs at its November 2017 meeting (with such requirement taking effect 12 months later).
“**Court**”	the High Court of Justice of England and Wales
“**CPI**”...	consumer price index
“**CRA**”..	Consumer Rights Act 2015
“**CRD**”..	the EU Capital Requirements Directive (Directive 2013/36/EU)
“**CRD IV**”	means the legislative package consisting of CRD and CRR
“**CRD V**”	the proposed CRD V Directive (proposed by the European Commission in November 2016), which will amend CRD IV
“**CRE**”	commercial real estate
“**Credit Risk RWAs**”........................	the amount of exposure deemed “at risk” according to PRA prescribed calculations for Pillar 1 capital requirements that relates to earnings and capital arising from a borrower's failure to meet the terms of any contract with the Bank or their failure to perform as agreed
“**Creditors’ Scheme**”........................	the scheme of arrangement pursuant to Part 26 of the Companies Act and to be made between the Bank and the Scheme Creditors in connection with the Restructuring and Recapitalisation, and with any modification or addition or condition made or introduced in accordance with its terms

"**Creditors' Scheme Circular**"	the circular relating to the Creditors' Scheme required to be provided to the Scheme Creditors pursuant to Part 26 of the Companies Act and dated the same date as this Circular
"**Creditors' Scheme Court Meeting**"	the meeting of Scheme Creditors to be held at 9.45 a.m. on 21 August 2017 at 10 Upper Bank Street, Canary Wharf, London E14 5JJ (and any adjournment thereof) convened at the direction of the Court pursuant to Part 26 of the Companies Act at which a resolution will be proposed to approve the Creditors' Scheme
"**Creditors' Scheme Sanction Order**"	has the meaning given to it in paragraph 5 of Section A of Part 1 of this Circular
"**CREST**"	the relevant system, as defined in the Uncertificated Securities Regulations 2001 (SI 2001 No. 2001/3755) in respect of which Euroclear UK & Ireland Limited (previously CREST Co Limited) is the operator (as defined in the CREST Regulations)
"**CREST Courier and Sorting Service**"	the courier and sorting service offered by CREST
"**CREST Manual**"	the rules governing the operation of CREST, consisting of the CREST Reference Manual, CREST International Manual, CREST Central Counterparty Service Manual, CREST Rules, Registrars Service Standards, Settlement Discipline Rules, CCSS Operations Manual, Daily Timetable, CREST Application Procedure and CREST Glossary of Terms (all as defined in the CREST Glossary of Terms)
"**CREST Regulations**"	the Companies Act 1996 (Uncertificated Securities), Regulations 1996 (S.I. No. 68/1996) and the UK Uncertificated Securities Regulations 2001 (SI 2001 No. 2001/3755), including any modifications thereof or any regulations in substitution therefore and for the time being in force
"**CRR**"	the Capital Requirements Regulation (Regulation (EU) 575/2013)
"**CRR II**"	the proposed CRR II Regulation (proposed by the European Commission in November 2016), which will amend CRR
"**CTF**"	counter terrorist financing
"**Customer**"	has the meaning set out in the regulatory rules of the U.S. Commodities Futures and Trading Commission as in force from time to time
"**CWS**"	the Co-operative Bank Wholesale Society Limited
"**Cyrus Capital Partners**"	funds managed and/or advised by Cyrus Capital Partners, L.P.
"**Data Protection Agreement**"	the data processing agreement entered into between the Bank and the Co-operative Group on 13 April 2015
"**DBP**"	means the Co-operative Bank p.l.c. Deferred Bonus Plan
"**DGS**"	Deposit Guarantee Scheme
"**DGSD**"	Directive 2009/14/EC
"**Director**"	a director of the Bank from time to time

"**Direct Participant**"..........................	has the meaning given to it in the Restructuring Deed set out in Part 13 of this Circular
"**Disclosure Guidance and Transparency Rules**"........................	the disclosure guidance and transparency rules made by the FCA under section 73A of FSMA
"**Downgraded Security Assets**"........	has the meaning given in paragraph 14.1 of Part 16 of this Circular
"**DPA**"...	Data Protection Act 1998
"**DWF**"	the Bank of England's Discount Window Facility
"**Early Bird Members' Arrangements**".................................	refers to the arrangements described in Para 6, Section A, Part 1 of this Circular
"**Early Bird Consenting Members**"..	means a Scheme Shareholder that has signed the Lock-up Agreement, executed an appropriate deed poll as provided at www.co-operativebank.co.uk/investorrelations pursuant to which it has agreed to adhere to and be bound by certain provisions of the Lock-up Agreement or otherwise has undertaken in writing to support the implementation of the Restructuring and Recapitalisation on the terms acceptable to the Bank by 28 July 2017 in respect of some or all of its Scheme Shares
"**Early Bird Members' Premium**"...	has the meaning given in paragraph 6 of Section A of Part 1 of this Circular
"**EEA**"	European Economic Area
"**Eligibility Condition**"......................	the quorum required for, and the requisite majority of votes cast at, the relevant 2023 Noteholder Meeting in respect of the 2023 Notes Second Extraordinary Resolution being reached by 2023 Noteholders eligible to participate in the Consent Solicitation (in accordance with any restrictions thereto), irrespective of any participation at the 2023 Noteholder Meeting by Ineligible 2023 Noteholders (and which would also have been so reached if any Ineligible 2023 Noteholders who provided confirmation of their status as Ineligible 2023 Noteholders and waived their right to attend and vote (or be represented) at the 2023 Noteholder Meeting had actually participated at the 2023 Noteholder Meeting) including (if applicable) the satisfaction of such condition at an adjourned 2023 Noteholder Meeting
"**Eligible 2023 Noteholders**"............	A Subordinated Noteholder that is eligible to participate in the Consent Solicitation on the basis that such Subordinated Noteholder (a) is not a U.S. person or (b) is a person to whom the Consent Solicitation can otherwise be lawfully made and that may lawfully participate in the Consent Solicitation. In its absolute discretion at any time prior to the Expiration Deadline, the Bank may extend the definition of Eligible 2023 Noteholder to also include any U.S. person that (i) is in a category of investors that has been approved to participate by the Bank in its absolute discretion; and (ii) has submitted or will submit a validly executed U.S. Investor Letter prior to the Expiration Deadline; and (iii) is a person to whom the Consent Solicitation can otherwise be made and that may lawfully participate in the Consent Solicitation including under U.S. securities laws

"**EMU**"	Economic and Monetary Union
"**Entitlements Record Date**"	the date of the General Meeting (or, if later, any date to which it is adjourned)
"**Entitlements Record Time**"	6.00 p.m. on the Entitlements Record Date
"**ERC**"	early repayment charges
"**Escrow Agent**"	Lucid Issuer Services Limited
"**Escrow Monies**"	has the meaning given to it in paragraph 17.20 of Part 16 of this Circular
"**ESMA**"	European Securities and Markets Authority has the meaning given to it in paragraph 3 of Section B of Part 1 of this Circular
"**Estimated Outcome Analysis**"	has the meaning given to it in paragraph 3 of Section B of Part 1 of this Circular
"**EU**"	the European Union
"**Euroclear UK**"	Euroclear UK and Ireland Limited, the operator of CREST
"**Eurozone**"	those Member States which have adopted the euro
"**Equity Subscriptions**"	the Members' Equity Subscription and the Scheme Creditors' Equity Subscription
"**Excluded Territories**"	Australia, Canada, Hong Kong, Japan, New Zealand, South Africa, Switzerland and any other jurisdiction where the delivery of the Circular into, or to a Shareholder resident in, such jurisdiction would breach any applicable law or regulation, and "**Excluded Territory**" shall mean any of them
"**Excluded Territories Shareholders**"	Shareholders with a registered address, or who are resident or located in, an Excluded Territory on the Circular Date or the at Entitlements Record Time as the context requires
"**Executive Committee**"	the executive committee of the Bank
"**Exit Premium**"	has the meaning given to it in paragraph 10 of Part 2 of this Circular
"**FCA**"	Financial Conduct Authority
"**FCA cash savings requirements**"	the rules and guidance in the FCA's Banking Conduct of Business Sourcebook introduced following the FCA's market study into competition in the cash savings sector
"**FCA Handbook**"	the FCA's handbook containing detailed rules and prudential standards set by the FCA
"**FEMR**"	the Fair and Effective Markets Review, launched by the Chancellor of the Exchequer and the Governor of the Bank of England in June 2014
"**FG 17/4**"	the finalised guidance issued by the FCA on 24 April 2017 regarding "The fair treatment of mortgage customers in payment shortfall: impact of automatic capitalisations"
"**FICC**"	Fixed Income, Currency and Commodities

"**Final Backstop Commitment**"	has the meaning given to it in paragraph 6 of Section A of Part 1 of this Circular
"**Financial Services Authority**" or "**FSA**"	an independent non-governmental body, given statutory powers by the Financial Services and Markets Act 2000, which regulated the financial services industry. It was replaced as the UK's financial regulator on 1 April 2013 by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA)
"**Financial Services Handbooks**".....	the FCA Handbook and PRA Rulebook
"**First instruction**"............................	has the meaning given to it in paragraph 2.2 of Part 12 of this Circular
"**Fitch**"...	Fitch Ratings Limited
"**Floating rate notes**"	investments with a variable interest rate. The adjustments to the interest rate are usually made every three to six months and are tied (or float) to a certain money market index
"**Forms of Proxy**"	the form of proxy with respect to each of the Members' Scheme Court Meeting and the General Meeting, being in the case of (a) the Members' Scheme Court Meeting, the blue Form of Proxy (b) the General Meeting, the pink Form of Proxy; and
"**FOS**"	Financial Ombudsman Service
"**Foundation Internal Ratings Based**"	Foundation Internal Ratings Based approach uses standard LGD and EAD parameters but PD is estimated by the Bank
"**FPC**"...	the Bank of England's Financial Policy Committee
"**FRC**"	Financial Reporting Council
"**FS Act 2012**"	the Financial Services Act 2012
"**FSCS**"...	the Financial Services Compensation Scheme
"**FSMA**"	the Financial Services and Markets Act 2000, as amended
"**FSP**"...	formal sale process
"**FTE**"...	full time equivalent
"**Funding For Lending Scheme**"	the Bank of England's funding for lending scheme
"**GDP**"	gross domestic product
"**GDPR**"	the General Data Protection Regulation (Regulation (EU) 2016/679)
"**general bail-in tool**"	the general bail-in provision under the Special Resolution Regime which could be imposed on the Bank
"**General Meeting**"...........................	the general meeting of the Bank scheduled to take place at 9.30 a.m. on 21 August 2017 at 10 Upper Bank Street, Canary Wharf, London E14 5JJ (and any adjournment thereof) called by the Bank for the purposes of considering and, if thought fit, passing the Resolutions (set out in Part 18 of this Circular)
"**Group Agreement**".........................	the agreement to implement the Term Sheets dated 28 June 2017 between the Bank and Co-operative Group

"**GoldenTree**"....................................	funds and/or accounts managed and/or advised by GoldenTree Asset Management L.P
"**GoldenTree Related Party Transaction**"......................................	the arrangements with GoldenTree described in paragraph 11 of Section A of Part 1 of this Circular
"**Government**"	the government of the United Kingdom
"**Group Related Party Transaction**"......................................	the arrangements with the Co-operative Group described in paragraph 11 of Section A of Part 1 of this Circular
"**GT**"..	Grant Thornton UK LLP
"**HM Treasury**"	the Government's economic and finance ministry
"**HMRC**"...	HM Revenue & Customs
"**Holdco**"	Balloon Street Holdings Limited, a company incorporated in England and Wales (registered number 10865342), whose registered office is at c/o Paul Hastings (Europe) LLP, 10 Bishops Square, Eighth Floor, London, E1 6EG
"**Holdco Articles of Association**"	the articles of association of Holdco to be adopted on the Settlement Date
"**Holdco Board**"................................	the board of directors of Holdco
"**Holdco Director**"............................	a director of Holdco from time to time
"**Holdco Group**"................................	Holdco and its subsidiaries and subsidiary undertakings from time to time, which, following the Reorganisation and Recapitalisation, will include the Bank
"**Holdco Senior Managers**".............	those persons listed as senior managers in Section A of Part 5 of this Circular
"**Holdco Shares**"................................	A Shares and B Shares
"**Holdco SID**"....................................	Holdco Senior Independent Director
"**Holdco Subscriptions**"....................	has the meaning given to it in paragraph 5 of Section A of Part 1 of this Circular
"**Holding Period Trustee**"................	Lucid Issuer Services Limited
"**Holding Period Trust Deed**"..........	has the meaning given to it in the Restructuring Deed set out in Annex 1 to Part 13 of this Circular
"**HPI**"...	house price index
"**HQLA**"..	high quality liquid assets
"**HR Director**"	human resources director of the Bank from time to time
"**IAS 19**"..	International Accounting Standard 19
"**IAS 24**"..	International Accounting Standard 24
"**IAS 37**"..	International Accounting Standard 37
"**IASB**"	the International Accounting Standards Board

"**IBNI**"	issues incurred but not yet identified by the Bank in relation to conduct
"**ICG**"	individual capital guidance, being the PRA's guidance as to the regulatory capital it expects the Bank to hold
"**IFR**"	Regulation on Interchange Fees for Card-based Payment Transactions ((EU) 2015/751)
"**IFRS**"	the international financial reporting standards issued by the IASB, as adopted by the European Commission for use in the EU
"**IFRS 2**"	International Financial Reporting Standard 2 (Share-based Payments)
"**IFRS 9**"	International Financial Reporting Standard 9 (Financial Instruments: Recognition and Measurement)
"**IGAs**"	intergovernmental agreements between the United States and other jurisdictions to implement FATCA, which modify the way in which FATCA applies in their jurisdictions
"**Incorporation Shares**"	the 451,457 ordinary shares of £0.10 each in the capital of Holdco at incorporation
"**Independent Non-Executive Director**"	each of William Thomas, Laura Carstensen, Maureen Laurie, Derek Weir, Glyn Smith and Aidan Birkett
"**Independent Shareholder**"	all Shareholders with the exception of, GoldenTree in the case of the GoldenTree Related Party Transaction, Silver Point Capital in the case of the Silver Point Capital Related Party Transaction and CBG in the case of the Group Related Party Transaction
"**indexed LTV ratio**"	being the current aggregate mortgage balance divided by the latest property valuation (of the mortgaged property), indexed using the Halifax non-seasonally adjusted regional house price indices dated as at the end of Q3 2016)
"**Ineligible 2023 Noteholders**"	a Subordinated Noteholder that is not eligible to participate in the Consent Solicitation on the basis that such Subordinated Noteholder is not an Eligible 2023 Noteholder
"**Information Agent**"	Lucid Issuer Services Limited
"**Initial Backstop Providers**"	the Principal Investors in the context of the Backstop Arrangements
"**Initial Holdco Shareholders**"	each of Canary SC Master Fund, L.P., Cyrus Opportunities Master Fund II, Ltd., Crescent 1, L.P., CRS Master Fund, L.P., Cyrus Select Opportunities Master Fund, Ltd., Cyrus Special Strategies Master Fund, L.P., Goldentree Asset Management Lux, S.à.r.l., GT NM L.P., The San Bernardino County Employees' Retirement Association, Gold Coast Capital Subsidiary X Limited, Bluemountain Kicking Horse Fund L.P., Bluemountain Montenvers Master Fund SCA SICAV – SIF, Bluemountain Logan Opportunities Master Fund L.P., Bluemountain Foinaven Master Fund L.P., Blue Mountain Credit Alternatives Master Fund L.P., SP Coop Investment, Ltd. and Anchorage Illiquid Opportunities Offshore V.L.P.

"**Internal Capital Adequacy Assessment Process**" or "**ICAAP**"	the Bank's own assessment, as part of Basel II requirements, of the levels of capital that it needs to hold in respect of its regulatory capital requirements (for credit, market and operational risks) and for other risks including stress events
"**Invesco**"	Invesco Asset Management Limited for and on behalf of funds it advises and/or manages
"**Investment Bank**"	each of Merrill Lynch International and UBS Limited and together, the "**Investment Banks**"
"**Investor Presentation**"	the investor presentation given to investors by the Bank on 9 March 2017 and prepared in conjunction with the announcement of the Bank's 2016 results
"**Investor Related Party Transactions**"	the GoldenTree Related Party Transaction and the Silver Point Capital Related Party Transaction
"**IPO**"	initial public offering
"**IRB**"	Internal Ratings Based
"**IRRBB**"	interest rate risk in the banking book
"**IRS**"	U.S. Internal Revenue Service
"**ISA**"	individual savings account
"**ISIN**"	International Securities Identification Number
"**Issuerco**"	an entity to be incorporated as a public limited company and inserted within the Holdco Group between the Bank and Holdco in due course following completion of the Restructuring and Recapitalisation
"**IT**"	information technology
"**IT Separation Costs Agreement**"	the agreement entered into on 22 January 2015, between the Bank and the Co-operative Group, which allowed the Bank to then enter into an IT outsourcing agreement with IBM for enterprise computing services
"**ITSA**"	the agreement, dated 5 July 2012 (as amended and restated from time to time), entered into by the Bank, CFSMS, and the Co-operative Group as further described in paragraph 17.2 of Part 16 of this Circular
"**Latest Practicable Date**"	25 July 2017, being the latest practicable date before the posting of this Circular and the Application Forms
"**Legacy Portfolio**"	portfolio of non-core corporate assets (inconsistent with the Bank's strategy and risk appetite)
"**Legacy Portfolio and Optimum Assets**"	has the meaning given to it in Part 4 of this Circular
"**Liability Management Exercise**"	the Notes Exchange and the Consent Solicitation
"**LIBOR**"	London Interbank Offered Rate – the interest rate participating banks offer to other banks for loans on the London market

"**Lifetime Allowance**"........................	means the "lifetime allowance" as defined in, and calculated in accordance with, section 218 of the Finance Act 2004 as modified by Schedule 26 to the said Act
"**Liquidity Coverage Ratio**" or "**LCR**"..	a liquidity metric that aims to ensure that a bank has an adequate stock of unencumbered high quality liquid assets to meet its liquidity needs for a 30 calendar day liquidity stress scenario
"**Listing Rules**".................................	the listing rules of the FCA relating to admission to the Official List made in accordance with section 73A(2) of FSMA
"**LMS**"..	last-man standing
"**Lock-Up Agreement**"......................	the lock-up and support agreement dated 28 June 2017 between the Bank and the Principal Investors
"**Lock-Up Termination Events**".......	has the meaning given to it in paragraph 17.13 of Part 16 of this Circular
"**Long Stop Date**".............................	the later of: (a) 18 September 2017; (b) such later date falling prior to 31 December 2017 as may be agreed as the "Long Stop Date" for the purposes of the Lock-Up Agreement; and (c) such later date as the Bank and Holdco may agree and the Court may allow
"**Loss Given Default**" or "**LGD**"......	Loss Given Default is a Pillar 1 parameter and represents an estimate of the actual loss that would occur in the event of default expressed as a percentage of the EAD
"**LSA**"..	loss sharing agreement
"**LSB**"..	Lending Standards Board
"**LTI**"..	loan-to-income
"**LTIP**"...	The Co-operative Bank PLC Long Term Incentive Plan as approved by Shareholders on 17 June 2015 and as amended from time to time
"**LTV**"..	loan-to-value
"**Majority Consenting Holders**"......	the Bank and Consenting Holders holding in aggregate greater than 50 per cent. of the aggregate principal amount of the Subordinated Notes held by Consenting Holders at the relevant time
"**Mandatory Cancellation**"...............	the mandatory cancellation of the 2023 Notes of Retail Noteholders pursuant to the new Condition 6.7 to be inserted into the terms and conditions of the 2023 Notes, as set out in the 2023 Notes Second Extraordinary Resolution, in consideration of which the Retail Cash Consideration (up to the Maximum Cash Amount) will be paid to Retail Noteholders
"**mandatory write-down**".................	has the meaning given to it in the risk factor entitled *"The implementation of the Restructuring and Recapitalisation faces a number of significant risks and relies on the Members' Scheme (including the Members' Equity Subscription), the Creditors' Scheme (including the Scheme Creditors' Equity Subscription) and the Consent Solicitation being executed successfully and the Resolutions being passed. If the Restructuring and Recapitalisation does not succeed, the Bank believes the most likely outcome is that the Ordinary Shares and the Subordinated Notes will be subjected to a mandatory write-down, either as a preliminary step to, or in the*

	course of the Bank's entry into, Special Resolution. In such a scenario, the Bank believes that Shareholders will receive no recovery in respect of the Ordinary Shares that they hold, and that Subordinated Noteholders will receive no recovery in respect of the Subordinated Notes that they hold" in Part 3 of this Circular
"**mandatory write-down tool**"..........	the mandatory provision under the Banking Act that requires loss-absorbing capacity instruments are written down or converted before or at the same time as any of the stabilisation options are implemented
"**Market Abuse Regulation**"............	the Market Abuse Regulation (2014/596/EU)
"**Matrix**"...	the matrix drawn up by the Bank as required under the Compliance Statement, as further described in the risk factor entitled "*The Bank's differentiated customer propositions depends in part on its continued use of the "Co-operative" name*" in Part 3 of this Circular
"**MAV**"...	minimum asset value
"**Maximum Cash Amount**"	the cap of £13,500,000 on the aggregate cash amount to be paid in respect of the Retail Cash Consideration to all Retail Noteholders in respect of their 2023 Notes pursuant to the Mandatory Cancellation
"**Maximum Distributable Amount**"	Maximum Distributable Amount is calculated in accordance with Article 141 of CRD. An institution is prohibited from making a distribution in connection with CET1 to an extent that would reduce its CET1 capital to a level where the Combined Buffer requirement is not met. An institution that fails to meet the Combined Buffer shall be prohibited from undertaking any or all of the actions set out below before it has calculated the Maximum Distributable Amount and shall not distribute more than the Maximum Distributable Amount by undertaking any of the actions set out below: (a) make a distribution in connection with CET1 capital; (b) create an obligation to pay variable remuneration or discretionary pension benefits or pay variable remuneration if the obligation to pay was created at a time when the institution failed to meet the Combined Buffer requirements; and (c) make payments on Additional Tier 1 instruments
"**May 2017 Outlook on the Plan**"....	has the meaning given to it in paragraph 2 of Section A of Part 1 of this Circular
"**MCD**"..	the EU Mortgage Credit Directive (2014/17/EU, published on 28 February 2014 and which came into force on 21 March 2014)
"**MCOB**"...	FCA's Mortgages and Home Finance: Conduct of Business sourcebook
"**MDA**"	has the meaning given to it in paragraph 2.7 of Part 11 of this Circular
"**Member State**"	a member state of the EU
"**Members' A Share Entitlement**"...	has the meaning given to it in paragraph 3 of Part 2 of this Circular

"**Members' Equity Subscription**"....	the entitlement of Qualifying Shareholders to subscribe in aggregate for such number of Subscription Shares as represent 3.3785 per cent. of the total number of fully-diluted issued A Shares as at Completion for an aggregate net cash consideration of approximately £12.5 million
"**Members' Equity Subscription Entitlement**"	has the meaning given to it in paragraph 3 of Part 2 of this Circular
"**Members' Scheme**".........................	the scheme of arrangement pursuant to Part 26 of the Companies Act and to be made between the Bank and the Scheme Shareholders in connection with the Restructuring and Recapitalisation, as set out in Part 13 of this Circular with or subject to such modification, addition or condition made or introduced in accordance with its terms
"**Members' Scheme Court Meeting**"	the meeting of Scheme Shareholders to be held at 9.15 a.m. on 21 August 2017 at 10 Upper Bank Street, Canary Wharf, London E14 5JJ (and any adjournment thereof) convened at the direction of the Court pursuant to Part 26 of the Companies Act at which a resolution will be proposed to approve the Members' Scheme
"**Members' Scheme Effective Date**"	the date on which the Members' Scheme becomes effective, which is expected to be 24 August 2017
"**Members' Scheme Sanction Order**"..	has the meaning given to it in paragraph 5 of Section A of Part 1 of this Circular
"**Merger**"...	any combination of two or more business enterprises into a single enterprise. In the Bank, this specifically refers to the merger of the Bank with Britannia Building Society on 1 August 2009
"**MiFID II**"..	Directive 2014/65/EU and associated Regulation 600/2014 adopted on 15 May 2014 by the European Parliament and European Council on markets in financial instruments, which repeal and recast the existing Directive 2004/39/EC on markets in financial instruments
"**MLD3**"	the third EU Money Laundering Directive (2005/60/EC)
"**MLD4**"	the fourth EU Money Laundering Directive (EU 2015/849)
"**MLR**"	the UK Money Laundering Regulations 2007
"**MMR**"	FCA's Mortgage Market Review
"**MMS**"..	the FCA's terms of reference for its mortgage market study (MS16/2) published on 12 December 2016
"**Money Laundering Regulations**" ..	the Money Laundering Regulations 2007 as amended from time to time
"**Moody's**"..	Moody's Investors Service Limited
"**Mortgage Rectification Programme**".....................................	the Mortgage Rectification Programme relates to legacy system issues. This predominantly relates to the incorrect monthly mortgage payment calculation resulting in the under or over payment of interest and capital
"**MREL**"..	minimum requirement for own funds and eligible liabilities as prescribed by BRRD

"**MREL Statement of Policy**"	the Bank of England's statement of policy of November 2016 titled "The Bank of England's approach to setting a minimum requirement for own funds and eligible liabilities (MREL)"
"**Net Stable Funding Ratio**" or "**NSFR**"	Net Stable Funding Ratio is a liquidity ratio introduced under CRD IV, measuring the proportion of long term assets which are funded by long term or stable funding
"**New Direct Agreement**"	the agreement between the Bank and Sopra entered into on 31 March 2017, as described in paragraph 17.7 of Part 16 of this Circular
"**New Ordinary Share**"	a new Ordinary Share to be issued by the Bank to Holdco pursuant to the Holdco Subscriptions
"**No Creditor Worse Off**"	has the meaning given in paragraph 2.8 of Part 11 of this Circular
"**Nomination Committee**"	the nomination committee of the Board
"**Non-core Assets**"	the asset classes of the Non-core Business of the Bank
"**Non-core Business**"	non-core business lines include activities not consistent with the strategy of the Bank, are managed for value and are targeted for run down or exit. These non-core lines contain the majority of the impairment risk for the Bank, and predominantly include the Legacy Portfolio (corporate non-core) and Optimum (the closed book of intermediary and acquired loan book assets). This historical classification is no longer used by the Bank following 31 December 2016
"**Non-Responding Scheme Creditors**"	has the meaning given to it in paragraph 4 of Part 2 of this Circular
"**Note Claims**"	all the rights, title and interest to and claims against the Bank or Law Debentures Trustees Limited arising out of or in connection with the 2023 Notes.
"**Notes Exchange**"	the exchange of all Subordinated Notes held by Subordinated Noteholders (other than the 2023 Notes held by Retail Noteholders which shall be subject to the Mandatory Cancellation), in consideration for A Shares in Holdco (representing in aggregate 17.42999 per cent. of the total number of fully-diluted issued A Shares of Holdco immediately following Completion), to be implemented pursuant to the Creditors' Scheme
"**Notes Exchange Entitlement**"	has the meaning given to it in paragraph 4 of Part 2 of this Circular
"**Notification Matters**"	has the meaning given to it in paragraph 4.4 of Part 15 of this Circular
"**Notification Threshold**"	has the meaning given to it in paragraph 4.4 of Part 15 of this Circular
"**NPS**"	net promoter scores, being an index ranging from -100 to 100 that measures the willingness of customers to recommend the Bank's products or services to others
"**Official List**"	the Official List maintained by the Financial Conduct Authority
"**OFT**"	Office of Fair Trading

"**Operational Projects**"	the category of the Bank's investment expenditure which relates to changes in the regulatory environment and smaller business-led initiatives, including process improvements
"**operational risk**"	the risk of loss resulting from inadequate and failed processes, people or systems within the Bank or from external events. The Bank holds capital for each of the seven Basel categories of operational risk against which a regulated entity has to assess its operational Risk capital requirements, these are internal fraud, external fraud, employment practices and workplace safety, clients, products, and business practice, damage to physical assets, business disruption and systems failures, execution, delivery, and process management
"**Optimum**"	the Optimum closed book mortgage portfolio, as further described in Part 4 of this Circular
"**Ordinary Share**"	means an ordinary share in the capital of the Bank (with a nominal value of £0.05)
"**Orphans**"	has the meaning given in the risk factor entitled *"Risks relating to the proportion of Pace assets and liabilities forming the Bank Section on the Pace Pensions Sectionalisation "* in Part 3 of this Circular
"**Other**"	any activities that cannot be directly attributed to one of the Bank's reportable business segments
"**Overseas Shareholders**"	Shareholders who have registered addresses outside the United Kingdom
"**Pace**"	The pension scheme entitled The Co-operative Bank Pension Scheme (Pace)
"**Pace Heads of Terms**"	the agreement dated 14 July 2017 between the Bank, the Co-operative Group and the Pace Trustee
"**Pace Pensions Sectionalisation**"	has the meaning given in paragraph 11 of Section A of Part 1 in this Circular
"**Pace Trustee**"	the trustee of Pace
"**Panel**"	the Takeover Panel
"**PBS**"	priority business services
"**Pensions Deed**"	the deed dated 28 June 2017 between the Bank, Co-operative Group, and the Pace Trustee
"**Pensions Regulator**"	the UK regulator of work-based pension schemes, as established under the Pensions Act 2004
"**Perry Capital**"	Perry Capital UK LLP
"**PFI**"	project finance initiatives
"**Pillar 1**"	Pillar 1 capital is a prescribed measure of capital required by a bank representing the minimum capital requirements. The Pillar 1 capital ratio is calculated using regulatory capital and RWA. The total capital ratio must be no lower than 8 per cent.

"**Pillar 2**"	Pillar 2a plus Pillar 2b
"**Pillar 2 Capital Add-on**"	the proposal under BRRD II for additional own funds requirements in addition to the minimum Pillar 1 regulatory capital requirements and the Combined Buffers requirements that may be imposed on institution by competent authorities
"**Pillar 2a**"	Pillar 2a is additional capital that the Bank is required to hold above Pillar 1, for risks not captured within Pillar 1. The Bank's internal capital adequacy assessment process is an input into this process, but the Bank's Pillar 2a requirement is ultimately set by the PRA
"**Pillar 2b**"	Pillar 2b is the capital that must be held by the Bank so that in a severe but plausible stress it can continue to meet its Pillar 1 plus Pillar 2a requirements
"**Plan**"	has the meaning given it to in paragraph 2 of Section A of Part 1 of this Circular
"**Platform**"	the Bank's brand of residential mortgage loans sold through mortgage intermediaries
"**PPI**"	payment protection insurance
"**PRA**"	Prudential Regulation Authority
"**PRA Buffer**"	capital that should be held by a bank over and above the level of capital recommended as its ICG and over and above the Combined Buffer required of the bank, set by the PRA as part of its firm-specific supervisory assessment process, which should be of a sufficient amount to allow the bank to continue to meet its regulatory obligations even in adverse circumstances, after allowing for realistic management actions that a bank could, and would, take in a stress scenario.
"**PRA Rulebook**"	the PRA's rulebook containing detailed rules and prudential standards set by the PRA
"**PRC**"	Prudential Regulation Committee
"**Preference Share**"	means a 9.25 per cent. noncumulative irredeemable preference share of £1.00 issued by the Bank
"**Preference Shareholder**"	a holder of a Preference Share
"**Preference Shares Cancellation**"	the cancellation of the Preference Shares held by the Co-operative Group in the Bank
"**Principal Investors**"	funds managed and/or advised by Anchorage Capital Group L.L.C, BlueMountain Capital Management, LLC, Cyrus Capital Partners L.P., GoldenTree Asset Management L.P. and Silver Point Capital, L.P. who executed the Backstop Agreement as Initial Backstop Providers
"**Probability of default**" or "**PD**"	the likelihood that a loan will not be repaid and will fall into default. PD may be calculated for each customer who has a loan (normally applicable to wholesale customers) or for a portfolio of customers with similar attributes (normally applicable to retail customers). To calculate PD, the Bank assesses the credit quality of borrowers and other counterparties and assigns them an internal risk rating. Bonds with no maturity date that do not require the issuer to redeem

"Proposals" .... the proposals that the Bank is inviting Eligible 2023 Noteholders to approve by way of 2023 Noteholder Extraordinary Resolutions at the 2023 Noteholder Meeting, including to

(i) assent to and sanction the modification to the terms and conditions of the 2023 Notes to insert a mandatory cancellation condition pursuant to which 2023 Notes held by Retail Noteholders shall be irrevocably cancelled and the rights, liabilities and obligations thereunder released in consideration of the payment of the Retail Cash Consideration to those Retail Noteholders (subject (in aggregate) to the Maximum Cash Amount);

(ii) waive any and all events of default, potential events of default and any other breach of the terms and conditions of the 2023 Notes or the 2023 Trust Deed (in each case, if any) that have been, are or may be, triggered by or in connection with the Restructuring;

(iii) assent to and sanction the extension of the powers of a meeting of Subordinated Noteholders under the 2023 Trust Deed in order to allow for the assent and sanction of the releases and waivers referred to in (iv) below; and

(iv) assent to and sanction, to the fullest extent permitted by law:

(A) subject to certain conditions, the irrevocable and unconditional, full and final waiver and release and forever discharge from the Settlement Date of (x) all Note Claims; and (y) any and all actions, proceedings, claims, damages, counterclaims, complaints, liabilities, liens, rights, demands and set-offs, whether in this jurisdiction or any other, of whatsoever nature and howsoever arising, whether in law or in equity, in contract (including but not limited to breaches or non-performances of contract), statute or in tort (including but not limited to negligence and misrepresentation), breaches of statutory duty, for contribution, or for interest and/or costs and/or disbursements, whether filed or unfiled, whether or not presently known to the parties or to the law, all claims that each 2023 Noteholder ever had, may have or hereafter can, shall or may have against any Relevant Person in relation to or arising out of or in connection with:

(i) the preparation, negotiation or implementation of the Consent Solicitation and the Creditors' Scheme (including, but not limited to, the Restructuring Deed and Restructuring Implementation Documents); and/or

(ii) the preparation, negotiation or implementation of the Restructuring and Recapitalisation; and/or

(iii) any event or circumstance arising in the period from 1 January 2016 to the Completion Time (as defined in the Restructuring Deed) which caused or, contributed to, directly or indirectly the requirement for the Restructuring and Recapitalisation;

(B) that Relevant Persons may enforce the agreement of each 2023 Noteholder to release liabilities and waive its rights and entitlements, as described in (A) above, subject to and in accordance with the provisions of the Contracts (Rights of Third Parties) Act 1999; and

(C) the modification, abrogation, compromise or arrangement in respect of its rights against the Relevant Persons necessary to give effect to the foregoing provisions of this paragraph (iv)

"**Proposed Co-existence Agreement**"	the co-existence agreement that was being negotiated by the Bank and the Co-operative Group as further described in the risk factor entitled "*The Bank's differentiated customer proposition depends in part on its continued use of the "Co-operative" name."* of Part 3 of this Circular
"**Prospectus Directive**".....................	Directive 2003/71/EC (and any amendments thereto, including the 2010 PD Amending Directive, to the extent implemented in the Relevant Member State), and includes any relevant implementing measure in the Relevant Member State
"**Provisional Allocation Date**"..........	25 July 2017, being the date on which a Shareholder must be a holder of Ordinary Shares on the shareholder register of the Bank to be a Provisional Qualifying Shareholder
"**Provisional Qualifying CREST Shareholder**"	a Provisional Qualifying Shareholder holding Ordinary Shares in uncertificated form
"**Provisional Qualifying Non-CREST Shareholder**"......................	a Provisional Qualifying Shareholder holding Ordinary Shares in certificated form
"**Provisional Qualifying Shareholder**"	a holder of Ordinary Shares on the shareholder register of the Bank at 6.00 p.m. on the Provisional Allocation Date (except for any holder which the Bank believes to be: (i) a Shareholder in the EEA who is not a Qualified Investor; and (ii) a Shareholder who is a U.S. person and who is not a QIB or an Accredited Investor; and (iii) any Excluded Territories Shareholder)
"**Provisional Subscription Allocation**"..	the maximum number of Subscription Shares for which a Provisional Qualifying Shareholder may apply to subscribe under the Members' Equity Subscription (as shown on a Provisional Qualifying Non-CREST Shareholder's Application Form, or as credited to the CREST stock account of a Provisional CREST Shareholder assuming the Provisional Qualifying Shareholder does not sell or transfer any of his holding of Ordinary Shares prior to the Entitlements Record Time
"**PSD1**"	Payment Services Directive (2007/64/EC)
"**PSD2**"	the second payment services directive
"**PSMSA**"	the revised professional services master service agreement entered into between the Bank and the Co-operative Group

"**PSR**"	the Payment Services Regulations, (SI/2009/09, which came into force on 1 November 2009)
"**Purchase Agreement**"	the purchase agreement dated 4 November 2013 between the Bank and certain holders of the Bank's debt securities listed in such agreement
"**QIB**"	a "qualified institutional buyer" as defined in Rule 144A under the Securities Act
"**Qualified Investor**"	a person or entity that is a "qualified investor" as defined under the Prospectus Directive
"**Qualifying CREST Shareholder**"	Qualifying Shareholders holding Ordinary Shares in uncertificated form
"**Qualifying Non-CREST Shareholders**"	Qualifying Shareholders holding Ordinary Shares in certificated form
"**Qualifying Scheme Creditors**"	Scheme Creditors except for: (i) any Scheme Creditor in the EEA who is not a Qualified Investor; (ii) any Scheme Creditor who is a U.S. person and who is not a QIB or an Accredited Investor; and (iii) Scheme Creditors with a registered address, or who are resident or located in, an Excluded Territory at the Entitlements Record Time
"**Qualifying Shareholders**"	Scheme Shareholders (except for: (i) any Shareholder in the EEA who is not a Qualified Investor; (ii) any Shareholder who is a U.S. person, who is not a QIB or an Accredited Investor; and (iii) any Excluded Territories Shareholder) who are registered as a member of the Bank at the Entitlements Record Time
"**RAO**"	the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001
"**Ravensworth**"	funds managed and/or advised by Ravensworth (International) Limited
"**REAF**"	renewable energy and asset finance
"**Receiving Agent**"	Computershare Investor Services PLC
"**Registrar**"	Computershare Investor Services PLC
"**Registrar of Companies**"	the registrar of companies of England and Wales
"**Regulation S**"	Regulation S of the United States Securities Act 1933, as amended
"**Related Party Transaction(s)**"	the Group Related Party Transaction and the Investor Related Party Transactions
"**Relationship Agreement**"	the agreement between the Bank, the Co-operative Group and CBG, dated 4 November 2013, which regulates the basis for the relationship between the parties thereto
"**Relationship-managed Banking**"	the relationship-managed banking sub-segment of the BaCB
"**Released Parties**"	the Bank and each of its Affiliates (together, the "**Wider Bank Group**"), Holdco, any director, officer or employee of the Bank, Holdco or any member of the Wider Bank Group (in each case, (A) in respect of an employee, who is, as at the date hereof,

	employed; or (B) in respect of an officer or director, who is, as at the date hereof, employed or holding office or was at any time, during the period from (and including) 13 February 2017 to the date hereof, employed or held office), the Co-operative Group, each of its current directors, officers, employees and advisers and each of its Affiliates, Lucid Issuer Services Limited, PACE Trustees Limited (trustee of the Co-operative Bank Pension Scheme), the Law Debenture Trustee Limited, Computershare Investor Services PLC, the Advisers, the Principal Investors, the Initial Backstop Providers or any of their Affiliates
"**Relevant Member State**"	each Member State of the EEA which has implemented the Prospectus Directive
"**Relevant Persons**"	The Wider Bank Group, Holdco, any director, officer or employee of the Bank, Holdco or any member of the Wider Bank Group (in each case, (A) in respect of an employee, who is, as at the Settlement Date, employed; or (B) in respect of an officer or director, who is, as at the date hereof, employed or holding office or was at any time, during the period from (and including) 13 February 2017 to the date hereof, employed or held office) the Co-operative Group Limited, each of its current directors, officers, employees and advisers and each of its Affiliates, Lucid Issuer Services Limited, PACE Trustees Limited, (trustee of the Co-operative Bank Pension Scheme), Law Debenture Trustees Limited, Computershare Investor Services PLC, the Advisers, the Principle Investors, the Initial Backstop Providers or any of their Affiliates
"**Relevant Regulator(s)**"	one or both of the PRA and/or the FCA as the context requires
"**Relevant Situation**".........................	a situation which occurs as described in paragraph 4.13 of Part 15 of this Circular
"**Remediation Projects**"....................	the category of the Bank's investment expenditure which relates to IT remediation, integration and resilience as well as activity associated with the Bank's separation from Co-operative Group
"**Remuneration Committee**"	the remuneration committee of the Board
"**Resolutions**"....................................	the resolutions to be proposed at the General Meeting as set out in Part 18 of this Circular
"**Restructuring and Recapitalisation**"...............................	has the meaning given to it in paragraph 5 of Section A of Part 1
"**Restructuring Deed**".......................	the restructuring deed to be entered into between the Bank, Holdco, the Scheme Shareholders, the Scheme Creditors, the Escrow Agent and the Holding Period Trustee substantially in the form attached at Annex 1 of Part 13 of this Circular (or otherwise in the form modified in accordance with the terms of the Schemes)
"**Restructuring Implementation Documents**"	the documents to which the Scheme Shareholders, or any of them, are named as a party and which are listed and scheduled as such in the Restructuring Deed
"**Retail**"	the segment that comprises customer focused products and services for individuals, sole traders and small partnerships. This includes mortgages, credit cards, consumer loans, current accounts and savings products

"**Retail Accrued Interest**"................ interest accrued on the aggregate principal amount of the 2023 Notes that are subject to the Mandatory Cancellation, for the period from (and including) 20 June 2017 to (but excluding) 31 July 2017 which will be paid in cash and rounded to the nearest £0.01

"**Retail Banking**"............................... the Bank's core retail banking business, which trades as "The Co-operative Bank", "Britannia" and "smile", together with the Bank's intermediary mortgage brand, Platform, and includes retail secured and unsecured lending, deposits and current accounts

"**Retail Cash Consideration**" .... the cash amount that is payable on the Settlement Date (separate to the Retail Accrued Interest payment) pursuant to the Mandatory Cancellation to Retail Noteholders in respect of their 2023 Notes, such cash amount being subject (in aggregate) to the Maximum Cash Amount and, accordingly, shall be the lesser of:

(i) £4.50 per £10 in principal amount of 2023 Notes; and

(ii) the amount (rounded to the nearest £0.01) per £10 in principal amount of 2023 Notes calculated by (a) dividing the Maximum Cash Amount by the aggregate principal amount of 2023 Notes that will be subject to the Mandatory Cancellation, and (b) multiplying the resultant figure by 10.

The amount to be paid to each Retail Noteholder in respect thereof shall be calculated by the Registrar as further described in the Consent Solicitation Memorandum

"**Retail Confirmation**" .... an instruction by which a 2023 Noteholder may confirm its status as a Retail Noteholder, which must be made by submission of:

(i) in respect of 2023 Notes held through Euroclear and Clearstream, Luxembourg, the electronic instruction to be submitted by a Direct Participant to the Information Agent through such Clearing System, in the form described in the relevant notice that has been delivered through the Clearing System;

(ii) in respect of 2023 Notes held through CREST, the submission of a TTE Instruction in respect of the Holder's 2023 Notes, specifying the Registrar as escrow agent; or

(iii) in respect of 2023 Notes held in certificated form outside the Clearing Systems, the Certificated Holding Consent Instruction or Retail Confirmation

"**Retail Confirmation Deadline**"...... 10.00 a.m. on the third Business Day following, but not including, the Members' Scheme Effective Date

"**Retail Noteholder**" .... a Retail Noteholder is:

(A) a Subordinated Noteholder who as at 5.00 p.m. on the Retail Record Date satisfied and, at the Entitlements Record Time will continue to satisfy, the following conditions:

(i) it is an individual person;

(ii) it is the Beneficial Owner of less than £100,000 in aggregate principal amount of 2023 Notes;

(iii) (a) if it is resident in the United States, it is not an Accredited Investor, or (b) if it is not resident in the United States, it is not a "qualified investor" as defined in the Prospectus Directive; and

(iv) it is not a Sanctions Restricted Person,

(B) who (i) has validly confirmed the matters set out in paragraph (A) above in accordance with the procedures set out in the notice of meeting in respect of the 2023 Noteholder Meeting and the Consent Solicitation Memorandum; or (ii) has been assessed, on reasonable enquiry, by the Bank to satisfy the criteria set out in paragraph (A) above, (which assessment shall be conclusive and binding) on or prior to the Retail Confirmation Deadline

"**Retail Record Date**"........................ 27 June 2017

"**Return on Equity**" or "**RoE**".......... the ratio of profit for the year (after tax) to Shareholders equity, expressed as a percentage

"**Reverse Shadowing Letter**" .... the reverse shadowing letter entered into between the Bank and CFSMS on 9 January 2017

"**Risk Committee**"............................. means the risk committee of the Bank

"**RMBS**" .... residential mortgage-backed securities

"**RMF**".. the Bank's risk management framework

"**RWAs**".. means risk weighted assets

"**SAS**" .... select access saver

"**Sanctions Authority**"...................... means:

(i) the United States government;

(ii) the United Nations;

(iii) the European Union (or any of its member states including, without limitation, the United Kingdom);

(iv) any other equivalent governmental or regulatory authority, institution or agency which administers economic, financial or trade sanctions; or

(v) the respective governmental institutions and agencies of any of the foregoing including, without limitation, the Office of Foreign Assets Control of the U.S. Department of the Treasury, the United States Department of State, the United States Department of Commerce and Her Majesty's Treasury.

"**Sanctions Restricted Person**"......... each Person or entity (a "**Person**"):

(i) that is, or is directly or indirectly owned or controlled by a Person that is, described or designated in (a) the most current "Specially Designated Nationals and Blocked Persons" list (which as of the date hereof can be found at: https://www.treasury.gov/ofac/downloads/sdnlist.pdf) or (b) the most current "Foreign Sanctions Evaders List" (which as of the date hereof can be found at https://www.treasury.gov/ofac/downloads/fse/fselist.pdf) or

(c) the most current "Consolidated list of persons, groups and entities subject to EU financial sanctions" (which as of the date hereof can be found at: https://data.europa.eu/euodp/en/data/dataset/consolidated-list-of-persons-groups-and-entities-subject-to-eu-financial-sanctions); or

(ii) that is otherwise the subject of any sanctions administered or enforced by any Sanctions Authority, other than solely by virtue of their inclusion in: (a) the most current "Sectoral Sanctions Identifications" list (which as of the date hereof can be found at https://www.treasury.gov/ofac/downloads/ssi/ssilist.pdf) (the "**SSI List**"), (b) Annexes 3, 4, 5 and 6 of Council Regulation No. 833/2014, as amended by Council Regulation No. 960/2014 (the "**EU Annexes**") or (c) any other list maintained by a Sanctions Authority, with similar effect to the SSI List or the EU Annexes.

"**Scheme**"	the Members' Scheme or the Creditors' Scheme
"**Scheme Claim**"	has the meaning given to it in paragraph 4 of Part 2 of this Circular
"**Scheme Court Hearing**"	the hearing of the Court to sanction the Members' Scheme
"**Scheme Creditor**"	a person who is the beneficial owner of and/or the owner of the ultimate economic interest in any of the Subordinated Notes, whose interests in the Subordinated Notes are held either through records maintained in book entry form by all or any of Euroclear, Clearstream and CREST, each of their respective nominees and successors, and any other system designed for similar or analogous purposes, as appropriate or in certificated form
"**Scheme Creditors' A Share Entitlement**"	has the meaning given to it in paragraph 4 of Part 2 of this Circular
"**Scheme Creditors' Equity Subscription**"	the subscription in aggregate for such number of Subscription Shares as represent 64.1915 per cent. of the total number of fully-diluted A Shares for an aggregate cash consideration of £237.5 million
"**Scheme Creditors' Equity Subscription Entitlement**"	has the meaning given to it in paragraph 4 of Part 2 of this Circular
"**Scheme Sanction Order**"	the order of the Court sanctioning the Members' Scheme pursuant to section 889 of the Companies Act
"**Scheme Shareholder**"	a holder of Scheme Shares
"**Scheme Shares**"	Ordinary Shares: (i) in issue at the date of this Circular; (ii) (if any) issued after the date of this Circular but before the Scheme Voting Record Time; and (iii) (if any) issued at or after the Scheme Voting Record Time and at or prior to the Entitlements Record Time on terms that the holders will be bound by the Scheme
"**Scheme Voting Record Time**"	5.00 p.m. on 17 August 2017 or, if the Members' Scheme Court Meeting is adjourned, 5.00 p.m. on the date which is two Business Days before the date fixed for the adjourned meeting

"**section 75 debt**"	a debt pursuant to section 75 of the Pensions Act 1995
"**Sectionalisation Parties**"	the Bank, the Co-operative Group and the Pace Trustee
"**Secured Obligations**"	has the meaning given to it in Part 16 of this Circular
"**Securities Act**"	United States Securities Act 1933, as amended
"**Senior Independent Director**"	a senior independent director of the Bank from time to time
"**Senior Managers**"	those persons listed as senior managers in Section B of Part 5 of this Circular
"**Senior Notes**"	the £400,000,000 5.125 per cent. Notes due 20 September 2017 issued by The Co-operative Bank p.l.c. pursuant to its £3,000,000,000 Euro Note Programme
"**Separation Cost Share Agreement**"	the agreement entered into between the Bank and the Co-operative Group (amongst others) on 22 January 2015
"**Serengeti Asset Management**"	funds managed and/or advised by Serengeti Asset Management LLP
"**Settlement Date**"	the date on which the Restructuring and the Recapitalisation is completed, as determined in accordance with the Restructuring Deed
"**Share Transfer**"	the transfer of all the Ordinary Shares to Holdco in exchange for A Shares to be implemented on the Settlement Date by way of the Members' Scheme
"**Shareholder**"	a holder of an Ordinary Share
"**Silver Point**"	SP Coop Investment, Ltd. (Cayman)
"**Silver Point Capital**"	Silver Point Capital L.P.
"**Silver Point Capital Related Party Transaction**"	the arrangements with Silver Point Capital described in paragraph 11 of Section A of Part 1 of this Circular
"**Small and Medium Enterprises customers**" or "**SME customers**"	small and medium-sized businesses engaging with the Bank as customers
"**SME**"	small and medium-sized enterprises
"**SMR**"	the senior managers regime under FSMA
"**Solicitation Agency Agreement**"	the Solicitation Agency Agreement dated 28 July 2017 as further described in paragraph 17.1 of Part 16 of this Circular
"**Solicitation Agents**"	Merrill Lynch International and UBS Limited in their capacity as solicitation agents in connection with the Consent Solicitation
"**Sopra**"	Sopra Steria Limited
"**Special Resolution**"	a bank is in Special Resolution where it is subject to procedures under the Special Resolution Regime
"**Special Resolution Regime**"	the special resolution regime introduced by the Banking Act, see paragraph 2.8 of Part 11 of this Circular for a summary
"**SPEs**"	special purpose entities

"**SRT**"..	has the meaning given to it in of Part 3 of this Circular
"**Stabilisation Powers**"......................	has the meaning given to it in paragraph 2.8 of Part 11 of this Circular
"**Sterling Over Night Index**" or "**SONIA**"...	yield curves used by the Bank for swap arrangements. These are based on overnight indexed rates
"**Stichting Value Partners**"...............	funds managed and/or advised by Stichting Value Partners
"**Strategic Projects**"	the category of the Bank's investment expenditure which relates to those projects that are transformational in nature and deliver cost or income benefits to the Bank's business
"**Structured Risk-based Remediation Programme**"...............	the Bank's structured risk-based assessment of products and provisions of which the primary focus was the discovery and remediation of existing and new conduct and legal issues
"**Subordinated Noteholders**"............	a person who is the beneficial owner of and/or the owner of the ultimate economic interest in any of the Subordinated Notes, whose interests in the Subordinated Notes are held either through records maintained in book entry form by a clearing system or in certificated form
"**Subordinated Notes**".......................	the 2023 Notes and 2025 Notes
"**Subscription Deadline**"...................	3.00 p.m. on the Business Day after the Entitlements Record Date, which is expected to be 22 August 2017
"**Subscription Price**".........................	£0.040977 per A Share
"**Subscription Proceeds**"...................	the subscription of an aggregate £250 million of A Shares in Holdco by Qualifying Scheme Creditors and Qualifying Shareholders, to be implemented pursuant to the Scheme Creditors' Equity Subscription and the Members' Equity Subscription, or, to the extent such amount is not so subscribed by Qualifying Scheme Creditors and Qualifying Shareholders the subscription of such A shares, by the Backstop Providers pursuant to the Backstop Arrangements under the Backstop Agreement
"**Subscription Shares**"	the A Shares in Holdco to be subscribed by Qualifying Shareholders and Qualifying Scheme Creditors pursuant to the Equity Subscription, representing in aggregate 67.57 per cent. of the total number of fully-diluted issued A Shares of Holdco immediately following Completion, for an aggregate of £250 million, to be implemented pursuant to the Members' Scheme and the Creditors' Scheme, respectively
"**subsidiary**"......................................	a subsidiary as defined by section 1159 of the Companies Act
"**Supplemental Trust Deeds**"............	together (i) the first supplement to the 2023 Trust Deed to be executed if the 2023 Notes First Extraordinary Resolution is passed at the relevant Meeting; (ii) the second supplement to the 2023 Trust Deed to be executed if the Consent Solicitation Conditions are satisfied
"**SVR**"..	the Bank's Standard Variable Rate
"**SYSC**"	the outsourcing rules set out in the FCA Handbook

"systemic risk buffer"......................	not currently applicable. The systemic risk buffer is expected to be introduced and applied to individual institutions by the PRA from 2019
"Tabulation Agent"	Lucid Issuer Services Limited in its capacity as tabulation agent in respect of the 2025 Notes, in connection with the Liability Management Exercise
"TDAP"..	means the Co-operative Bank p.l.c. Transitional Deferral Awards Plan
"Term Funding Scheme".................	the Government's Term Funding Scheme
"The Bank's Annual Report and Accounts 2014"	the annual report and accounts of the Bank for the financial year ended 31 December 2014, issued on 27 March 2015
"The Bank's Annual Report and Accounts 2015"	the annual report and accounts of the Bank for the financial year ended 31 December 2015, issued on 1 April 2016
"The Bank's Annual Report and Accounts 2016"	the annual report and accounts of the Bank for the financial year ended 31 December 2016, issued on 9 March 2017
"Threshold Conditions"	the Threshold Conditions for which the PRA and FCA are responsible in relation to the Bank, which set out the minimum standards to be met relating to financial and non-financial resources, including capital, risk management, liquidity, and technology, are set out in the FSMA
"Tier 1"	means Tier 1 capital as defined in the CRR
"Tier 1 Capital Ratio".....................	Tier 1 capital divided by RWAs
"Tier 2"	means Tier 2 capital as defined in the CRR
"TLAC"...	total loss-absorbing capacity as proposed by the Financial Stability Board's November 2015 "term sheet" for TLAC
"Transferred Shares"......................	has the meaning given to it in paragraph 1 of Part 12 of this Circular
"Transitional Services Agreement"	the transitional services letter agreement entered into between the Bank and CFSMS on 21 December 2016
"Treasury"	the Bank's treasury business, which forms a part of its Core Business
"Tribunal"..	the tribunal where challenges to decisions of the PRA or FCA are heard
"Trust Deed(s)"	the 2023 Trust Deed and the 2025 Trust Deed each a Trust Deed as the context requires and together the Trust Deeds
"TSA"..	the transitional services agreement entered into on 28 November 2014 between the Bank and CISGIL
"TTE Instruction"	the "transfer to escrow" instruction pursuant to which CREST Participants may (among other things): (i) submit Consent Instructions in respect of Subordinated Notes held in CREST pursuant to the terms of the Consent Solicitation; and (ii) issue electronic instructions to participate in the Creditors' Equity Subscription and the Backstop Arrangements

"**TUPE**"	Transfer of Undertakings (Protection of Employment) Regulations 1981
"**UK**" or "**United Kingdom**"	the United Kingdom of Great Britain and Northern Ireland
"**UK Corporate Governance Code**"	the UK Corporate Governance Code published by the Financial Reporting Council
"**Undertaking**"	the agreement entered into on 4 November 2013 between the Co-operative Group and the Bank
"**Unrelated Directors**"	the Directors other than Alistair Asher and Charles Bralver
"**U.S.**" or "**United States**"	the United States of America, its territories and possessions, including without limitation any state of the United States and the District of Columbia
"**USE**"	Unmatched Stock Event
"**U.S. Investor Letter**"	a letter furnished to the Bank by an Eligible 2023 Noteholder who is a U.S. Person in connection with their submission of a Consent Instruction containing certain representations and warranties, including representations and warranties required under U.S. securities laws
"**U.S. Person**"	a "U.S. person" as defined in Regulation S under the Securities Act
"**U.S.-UK Treaty**"	has the meaning given to it in paragraph 2 of Part 14 of this Circular
"**UTCCR**"	the Unfair Terms in Consumer Contracts Regulations 1999
"**V&E Committee**"	means the values and ethics committee of the Bank
"**Values & Ethics**"	has the meaning given to it in Part 4 of this Circular
"**Values & Ethics Report**"	the value and ethics report prepared by the Bank and launched in June 2016
"**Variation and Director Appointment Deed**" or "**VDAD**"	the deed summarised at paragraph 16.7 of Part 16 of this Circular
"**VAT**"	(a) any tax imposed in compliance with the council directive of 28 November 2006 on the common system of value added tax (EC Directive 2006/112) (including, in relation to the United Kingdom, value-added tax imposed by VATA); and (b) any other tax of a similar nature, whether imposed in a member state of the European Union in substitution for, or levied in addition to, such tax referred to in (a), or elsewhere
"**VATA**"	in the United Kingdom, the Value Added Tax Act 1994 and legislation and regulations supplemental thereto and, elsewhere, legislation and regulations of a similar nature
"**VocaLink**"	VocaLink Holdings Limited
"**Warwick Finance One**"	Warwick Finance Residential Mortgages Number One plc
"**Warwick Finance Two**"	Warwick Finance Residential Mortgages Number Two plc
"**Warwick Notes**"	the Warwick One Notes and the Warwick Two Notes

"**Warwick One Notes**"	the securitisation of approximately £1.5 billion comprising part of the Optimum portfolio through Warwick Finance One in May 2015
"**Warwick Two Notes**"	the £1.65 billion securitisation transaction through Warwick Finance Two in September 2015
"**Wider Bank Group**"	the Bank and each of its Affiliates
"**Wholesale Funding Ratio**"	total wholesale funding divided by total liabilities
"**WMS**"...	Western Mortgage Services Limited
"**Working Capital Period**"	the 12 months following the date of this Circular
"**Working Capital Stress Scenario**"	has the meaning given to it in paragraph 2.16 of Part 7 of this Circular
"**York Capital**"	York Capital Management Europe (UK) Advisers LLP

ALTERNATIVE PERFORMANCE MEASURES

In this Circular, the Bank uses the following financial measures in the analysis of its business and financial condition, which the Bank considers to constitute Alternative Performance Measures for the purposes of the ESMA Guidelines on Alternative Performance Measures. Such financial measures are not calculated in accordance with IFRS. Accordingly, they should not be considered as alternatives to 'results from operating activities' or 'profits' as indicators of the Bank's performance. However, the Bank believes that such financial measures are commonly used by investors and as such useful for disclosure. The presentation of these financial measures may not be comparable to similarly titled measures reported by other companies due to differences in the ways the measures are calculated.

Terminology	Definition
"**CET1 capital ratio**"	Capital ratios express the Bank's capital as a percentage of its RWAs as defined by the PRA. CET1 is broadly equivalent to tangible shareholders' funds less certain capital deductions.
"**cost:income ratio**"	The proportion of the Bank's revenue which is used to fund its operating costs calculated by dividing operating costs plus operational projects (including the associated depreciation) by operating income excluding losses on asset sales.
"**leverage ratio**"	A ratio calculated by reference to CRD IV Tier 1 capital (after deductions) divided by adjusted balance sheet exposure.
"**Net interest margin**" or "**NIM**"......	Net interest margin (the difference between interest received from loans/other assets and interest paid out on deposits/other liabilities) divided by average total assets (being the average of the opening and closing asset balances for the period).
"**SREP**"	Supervisory review and evaluation process.
"**total capital ratio**"	The ratio of total capital resources to the Bank's total RWAs.
"**Total RWAs**"	RWAs are required to be calculated for the Bank to provide for three types of risk: (i) Credit risk; (ii) Market risk; and (iii) Operational risk. The Bank considers market risk within credit risk. The Bank's capital ratios are calculated from the sum of the three RWA categories.