The Co-operative Bank plc
Interim Financial Report 2014

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Certain terms

The term the 'Bank' means The Co-operative Bank plc together with its consolidated subsidiaries.

In this report the abbreviations '£m' represent millions of pounds sterling.

Unless otherwise stated, the income statement analyses and compares the 6 months to 30 June 2014 to the corresponding 6 months of 2013. The balance sheet comprises the corresponding position as at 31 December 2013. Unless otherwise stated, all disclosed figures relate to continuing operations. Relevant terms that are used in this document but are not defined under applicable regulatory guidance or International Financial Reporting Standards (IFRS) are explained in non-IFRS measures below.

Non-IFRS measures

Certain non-IFRS measures are provided within the Interim Financial Report. This can be found mainly (but not exclusively) on the Detailed financial review pages.

Restatement

Furthermore, certain 2013 balance sheet items have been restated. For further information, see note 3 to the Bank financial statements.

Forward-looking statements

This document contains certain forward-looking statements with respect to certain of the Bank's strategy, plans and its current goals and expectations relating to its future financial condition and operating performance. The Bank cautions readers that no forward-looking statement is a guarantee of future performance and that actual results could differ materially from those contained in the forward-looking statements. These forward-looking statements can be identified by the fact that they do not relate only to historical or current facts. Forward-looking statements sometimes use words such as 'may', 'will', 'seek', 'continue', 'aim', 'anticipate', 'target', 'projected', 'expect', 'estimate', 'intend', 'plan', 'goal', 'believe', 'achieve', 'predict', 'should' or in each case, their negative or other variations or comparable terminology, or by discussion of strategy, plans, objectives, goals, future events or intentions. These forward-looking statements include all matters that are not historical facts. Examples of forward-looking statements include, among others, statements regarding the Bank's future financial position, income growth, assets, impairment charges, business strategy, capital ratios, leverage, payment of dividends, the industry in which the Bank operates, projected costs, commitments in connection with the Recapitalisation Plan and the Bank's 4-5 year turnaround plan, estimates of capital expenditures and plans and objectives for future operations and other statements that are not historical fact.

By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend on circumstances that may or may not occur in the future, for example, macroeconomic and business conditions, the effects of continued volatility in credit markets, market related risks such as changes in interest rates and foreign exchange rates, effects of changes in valuation of credit market exposures, changes in values of issued notes, the policies and actions of governmental and regulatory authorities (including requirements regarding capital and group structures and the potential for one or more countries exiting the Eurozone), changes in legislation, the further development of standards and of standards under IFRS, the outcome of current and future legal competition, a number of such factors being beyond the Bank's control. As a result, the Bank's actual future results may differ materially from the plans, goals and expectations set forth in the Bank's forward-looking statements. Forward-looking statements are not guarantees of future performance. In addition, even if the Bank's results of operations, financial condition, and the development of the financial services industry are consistent with the forward-looking statements in this document, those results or developments may not be indicative of results or developments in subsequent periods.

Readers are advised to read, in particular, the Principal risks and uncertainties section in this Interim Financial Report, as well as the 2013 Annual Report and Accounts and the Risk Factors document and prospectus published as part of the 2014 capital raising, both of which are available on our website (www.co-operativebank.co.uk) for a summary of factors that could affect the Bank's future performance. In light of these risks, uncertainties and assumptions, the events and targets described in the forward-looking statements in this document may not occur.

Any forward-looking statements made in this document speak only as of the date they are made except as required by the FCA, the PRA, the LSE or applicable law. The Bank expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in the Bank's expectations with regard thereto or any change in events, conditions or circumstances on which such statement is based. The reader should, however, consult any additional disclosures that the Bank has made or may make in documents it has published or may publish via the Regulatory News Service of the LSE.

Chairman's statement

The management team is making good progress to put the Bank back on track.

Our capital position has been strengthened by an additional £1.9bn raised through the successful completion of the Liability Management Exercise (LME) last December and the additional capital raising in May this year. We are also greatly encouraged about our progress in reducing risk weighted assets, having reduced Non-core customer assets by £1bn in the first six months of the year. We can report that our CET1 ratio at the end of June 2014 stood at 11.5%.

Despite the uncertainty in this period, the Core Bank has remained more stable than we could have expected. Whilst there has been some reduction in deposits and an increase in the number of current account customers switching away from the Bank following negative publicity and significant competitor activity, our customers have remained very loyal. We are extremely grateful to them for their support and the impressive response to our Values and Ethics Poll illustrates how important it is to them that they can again feel proud of banking with us.

My focus has been to renew the Board and the reform of the governance of the Bank. Sir Christopher Kelly's independent review detailed serious failings in this area and we have already made considerable progress on many of the issues he raised. The reshaping of the Board is well advanced and we have recruited some excellent independent Non-Executive Directors. Recently, we welcomed Laura Carstensen to chair the Board's Values and Ethics Committee established at the end of 2013. Laura's experience both as a Commissioner at the Equality and Human Rights Commission and as the former Deputy Chairman of the UK Competition Commission brings significant insight and scrutiny to this role. This is a vital appointment and marks an important step forward in the Bank's move to embed co-operative values and ethics in its governance. We have also recruited Maureen Laurie who has over 30 years of experience in senior HR roles, including for organisations such as the British Council, NYSE EURONEXT and Barclays, to chair the Remuneration Committee. Derek Weir, who has over 25 years of financial services experience holding a range of senior positions in corporate and commercial banking, joins the Board as an Independent Non-Executive Director and the first Shareholder Nominated Director. In addition, earlier this year we put out to tender our external audit services contract resulting in the appointment of Ernst & Young LLP as the Bank's auditors at our Annual General Meeting.

I announced in May my intention to step down from the Bank during 2014 and I will leave the Board on 1 October 2014. Whilst the Board's search for my successor is underway, Dennis Holt, who joined the Board in February as the Senior Independent Director, will be interim Chairman. In Niall Booker our CEO, the Bank is in experienced hands and I am confident the management team will continue to strengthen the Bank for the benefit of all our stakeholders. I would like to take this opportunity to wish Niall and his team well as they drive forward the transformation required. Running a bank underpinned by co-operative values is more relevant today than it has ever been. Whilst executing the plan remains challenging, the progress we have made and continue to make should reassure customers that if they believe in those values and ethics The Co-operative Bank should remain their bank of choice.

Richard Pym
Chairman
21 August 2014

Chief Executive's interim statement

We have strengthened our liquidity and capital, are ahead of schedule in the reduction of Non-core assets and have improved governance, particularly at Board level.

In my first statement as Chief Executive of The Co-operative Bank a year ago I talked about the deep rooted issues facing the Bank. As our results show today, those issues will continue to impact performance for some time but a year on we have taken significant steps forward. We have strengthened our liquidity and capital, are ahead of schedule in the reduction of Non-core assets and have improved governance, particularly at Board level. I would like to thank colleagues for their continued commitment throughout this period.

We continue to work closely with the Co-operative Group with whom we are united by our brand and the many customers we share. Whilst the Co-operative Group remains our largest shareholder, the Bank now has a range of shareholders who are invested in the future of the business. Their support through the additional capital raising in May is an endorsement of the business plan, the brand and our Co-operative values and ethics which sit at the heart of the organisation. We believe our Ethical Policy should help us not only define the type of customers we lend to but also inform how we operate. Alongside fixing the fundamentals in the Bank, this is central to rebuilding our retail franchise and growing our assets in the future. This was reflected by over 73,000 customers and colleagues taking part in our poll in June to refresh our Ethical Policy and we are greatly encouraged by customers' willingness to engage and share their views.

Transforming the organisation into a viable and profitable business in the long term still requires significant change – both operationally and culturally. To deliver the change required we have continued to strengthen the management team. In addition, as outlined in the Chairman's statement, we have reshaped the Board to improve the governance in the Bank. As announced earlier this year our Chairman Richard Pym will step down from his role in October and the Board is currently undertaking a full and rigorous process to appoint his successor. On behalf of the Board I would like to thank Richard for the Board transformation he has achieved. Our strengthened governance framework places us in a much better position to drive forward the business plan and face the challenges ahead. We are very grateful to him for the leadership he has provided during a time of considerable change at the Bank.

Performance review

In the first half of 2014, the financial performance of the business, although still dominated by the issues that came to light during 2013, was considerably better than the same period last year. The statutory loss before taxation was £76 million compared to a loss of £845 million at half year 2013. The main reason for this change is significant reductions in the level of credit impairments from a charge of £496 million in the first half of 2013 to a credit of £87 million in the first half of 2014. Our review of products and practices is continuing; however no new categories of conduct or legal risk have been provided for in the first half of 2014 with total charges, including PPI, down from £163 million in June 2013 to £39 million in June 2014.

The performance also shows the early progress the Bank is making in the implementation of the business plan in a number of key areas, particularly in the management of Non-core assets. The speed of the disposal of Non-core assets and the reduction in risk weighted assets reflects the headway made by the dedicated team we set up to manage the run down and disposal of these assets together with the benefit of the favourable economic conditions. A significant contributor to the write back of credit impairment provisions in Non-core is write backs on sale of restructured assets. This is in addition to upward revisions to valuations for assets still held, where we have received credible offers at levels in excess of carrying values as a result of work undertaken to increase the capital value of these assets. Two connections in this category were restructured and account for around half of the overall credit impairment write back. The faster than expected deleveraging of these assets has contributed to increased liquidity in the first half of the year as well as the improved CET1 ratio.

The performance of the Core Bank has undoubtedly been impacted by the continuing uncertainty the Bank has faced over the last 6 months. However, despite the negative publicity surrounding reviews into past failings and the need to raise additional capital, on a net basis our total current account customers have reduced by less than 2%. On the asset side we remain impacted by the actions we took in 2013 to slow asset growth in order to preserve liquidity. In addition, mortgage sales have been affected by the new mortgage market regulations which came into force earlier this year. Progress has been made on addressing the cost base in the Core Bank as we continue our work to reshape the Bank as a smaller and more agile organisation serving our individual and SME customers.

Strengthened capital position

This time last year the immediate priority was on maintaining adequate liquidity and improving the capital position of the Bank. A total of over £1.9 billion equity share capital has been added over the last 12 months through the successful completion of the Liability Management Exercise (LME) in December 2013 together with the additional £400 million capital raising in May this year. Raising this amount of capital in a short timeframe is a major achievement and provides some headroom for the management team to implement the business plan.

As at 30 June 2014 the Bank's CET1 ratio stood at 11.5%, exceeding our previous guidance. This is driven by the write back of credit impairment provisions in Non-core, the speed and timing of the deleveraging of Non-core assets, and reduced losses on disposals. Previous guidance assumed a charge for pension deficit contributions, and some adverse RWA model changes, as well as timing differences on asset sales, which may still come to fruition in the second half of 2014 with a consequent impact on the balance sheet and therefore the capital ratio. It is currently not possible to quantify the exact amount of this; however, the impact on the capital position is expected to be less than previously guided.

Simplifying the business

Now that this additional capital has been secured, the management team has turned its attention to further simplifying the business and reducing costs. In the retail business we have completed 46 branch closures in the first half of 2014, and will be closing further branches during the second half of the year. Cost reduction is underway though some of this has been offset by the need to incur additional expenditure in relation to necessary remediation of systems and processes. In the first half of the year the Bank's cost reduction programme has started to deliver savings through the reduction in the size of the Branch network, improving process efficiency and reducing 3rd party spend.

Run down and exit in Non-core

In the first half of this year we have already reduced Non-core assets by £1 billion through a combination of formal trade sales, proactive rebanking of our Corporate clients and the natural run off of the Corporate book.

Performance of the Core Bank

Whilst good progress has been made in the Non-core area, there is more work to do on our Core franchise. This is where the management team has been focused since the completion of the capital raising.

On my visits to branches and call centres I am always struck by the ongoing dedication of colleagues and I would like to convey my appreciation for the high levels of customer service they have maintained throughout the turmoil the Bank has faced.

The Core Bank continues to remain more stable than we might have expected given the ongoing uncertainty. Our current account switching data for the first half of 2014 as anticipated, and as noted in our capital raise circular, saw an increase in the number of customers switching out of the Bank. While this is disappointing the numbers remain small relative to our total number of current account customers whose continuing loyalty to the Bank is deeply appreciated. There has been some managed reduction in deposits with Core Retail deposit balances at £27.2 billion at the end of June 2014. Recent trends suggest the net outflow of retail customers has slowed and, having successfully restored the capital position of the Bank, our attention is on rebuilding customers' trust.

Progress has been made on addressing the cost base in the Core Bank with direct costs reduced by 10% in the first half of 2014 against the first half of 2013. Core Retail net interest income is relatively stable at £201.5 million.

Values and ethics remain a key reason for customers to bank with us and the Bank has recently been able to re-engage customers and seek their opinions through our poll to renew and revise our Ethical Policy. In addition, we launched a new switching offer at the beginning of the year. We have seen some growth since we re-entered the intermediary mortgage market but continue to maintain tight control over our lending standards given the current state of the housing market, especially in London and the South East. We continue to review our SME proposition and intend to implement the findings of that review over time.

Transforming the Bank

At year end I talked about simplifying our product range for both Retail and SME customers, strengthening our IT platform and investing in our digital capabilities to make it easier and more convenient for our customers to do business with us.

There have been over 400,000 mobile banking apps downloaded. Looking ahead, we have committed in the region of £500 million over the next three years to achieve the changes necessary in our systems and processes and have now begun our investment programme. This is a major task and there are significant execution risks around the scale of the transformation required but it is essential to the future of the Bank.

Progress has been made on the remediation of day to day regulatory issues, systems and processes but there is still significant work to be done. The process of separating the Bank from the Co-operative Group is also ongoing. Given the long history between the organisations, the separation issues are complicated but we are continuing to make progress and to work constructively with the Co-operative Group to achieve mutually beneficial outcomes.

Values and ethics

Our ethical policy and broader values both define and differentiate us. Our ownership structure has changed but I can reassure customers that values and ethics remain at the heart of our bank as we rebuild.

At the time of the LME we embedded the co-operative values and ethics into our Articles of Association for the first time. We have also established a Board Committee to ensure our adherence to those standards and appointed a new independent Chair of that committee, Laura Carstensen. In June we launched our values and ethics poll designed to refresh our ethical policy and our customers have readily engaged in this process with over 73,000 taking part. We will be going back to our customers with a renewed ethical policy in the autumn.

Outlook

There is still considerable work ahead of us as we undertake our 4-5 year Turnaround Plan but we are encouraged by the progress made in some key areas. This now allows us to push forward with simplifying the business, increasing revenue streams, reducing costs and investing in the technology to service customers in a way that suits them best. It also means we have begun to re-engage customers on what matters to them and we are re-investing in the brand and in its distinctiveness in the financial landscape. Our capital position is better than originally forecast but it is important to recognise we still need to ensure our capital base can meet the challenges ahead in terms of potential pension deficits, asset disposals, forthcoming stress tests and the outcome of regulatory reviews.

Following the capital raising in May, the Board has formed a committee to consider the feasibility and timing of an IPO and this is expected to meet for the first time in September and quarterly thereafter. The committee will take into account internal factors such as progress made in the Turnaround Plan, the ability of management to undertake an IPO and maintain its focus on improving the Core Bank's performance and the required robustness of systems and processes in financial reporting. In addition it will consider external factors such as the strength of the market, macroeconomic and political risks, the viability and relative merits of alternative strategic options and the views of the stakeholders, including the Bank's regulators and shareholders. The PRA has indicated it would be concerned if an IPO were to distract focus from the primary goal of delivering the Bank's Turnaround Plan and the Board from providing effective oversight of, and direction to, the business. It is logistically unlikely that an IPO could be executed before the end of 2014.

Sir Christopher Kelly's independent review detailed wide-ranging failings in the Bank. The Board recently reviewed the changes made in the Bank against the points raised in the review. It was noted that considerable progress had been made in governance and provisioning policy management and the journey has begun on embedding a revised risk management framework. IT sustainability, day to day systems and processes and cultural changes however remain work in progress. Creating the right culture across the organisation is key to the future performance of the business. Our service ethic and empathy are real strengths but we must combine this with greater accountability, speed and ability to execute. In addition, ongoing external factors such as Government and regulatory reviews could negatively impact our progress in the months ahead.

Against this, we believe The Co-operative Bank has a valuable role to play in providing customers with a different choice in the market set apart as it is by the values and ethics that remain a key reason why customers choose to bank with us. As we head back to our roots focusing on our retail and SME customers, we are determined to restore confidence by ensuring those values and ethics act as the guiding principles by which we serve our customers day to day.

Niall Booker
Chief Executive

Summary financial review

Capital and balance sheet

- £400m (pre costs) additional CET1 raised in May.
- £150m capital commitment from the Co-operative Banking Group received.
- Total assets reduced by £2.3bn since December 2013.
- CET1 ratio 11.5% at June 2014 (7.2%[1] at December 2013), however the Bank remains below Individual Capital Guidance (ICG).

Liquidity

- Liquidity has increased in the period with an increase in primary liquidity of £624.1m and secondary liquidity of £265.5m.

Business performance

- Statutory loss before tax of £76m (June 2013: £845m loss) represents a significant improvement over 2013.
- Credit impairment £87m benefit to the income statement (June 2013: £496m charge[2]) reflecting management action taken to restructure client facilities including rebanking of customers together with macroeconomic improvements leading to improved collateral values.
- Review of products and practices is ongoing, however no new categories of conduct or legal risk have been provided for during the period.
- Non-core customer assets reduced by £990m since December 2013, in line with deleveraging strategy.
- Overall Core Bank customer franchise remained stable and Retail customer assets reduced by £1.5bn.
- Total assets reduced by £2.3bn since December 2013.

Brand

- Values and Ethics poll completed with over 73,000 customers and colleagues taking part.
- Brand relaunch work commenced.

1 Following the restatement discussed in note 3 CET1 ratio would have been 7.3% as at 31 December 2013. This restatement will be part of the regulatory capital calculation only once formally audited.
2 The £496m credit impairment charge for the first half of 2013 includes £4m in relation to a customer fraud provision.

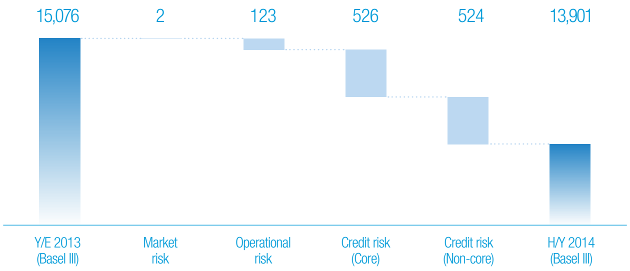
Detailed financial review

Capital

The Basel III capital framework came into effect from 1 January 2014 and within the European Union this has been implemented by a new Capital Requirements Directive (CRD IV). Under Basel III a Leverage Ratio has been introduced which is a simpler measure of Bank capital levels and is based on the amount of good quality capital (Tier 1) compared to the overall balance sheet of the Bank.

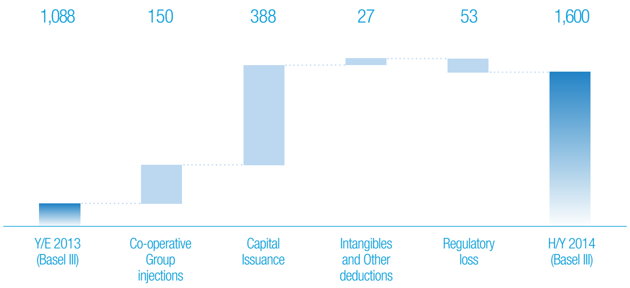
During the first half of 2014, the Bank has made good progress toward improving the capital position and reducing the overall risk profile of the Bank. Completion of the £400m capital raising, together with the planned £150m injection from the Co-operative Banking Group and ongoing deleveraging, has resulted in a significant improvement in the capital position of the Bank.

Risk Weighted Assets £m

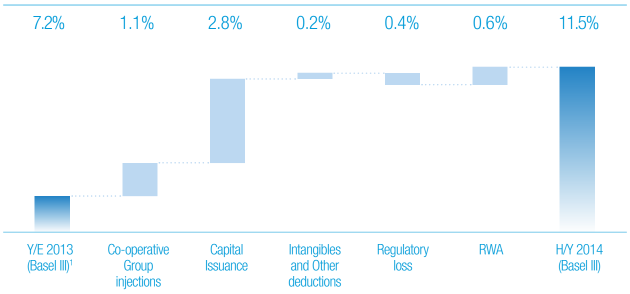


* Credit risk, market risk, operational risk are defined in the glossary

Common Equity Tier 1 £m



Common Equity Tier 1%



1 Following the restatement discussed in note 3 CET1 ratio would have been 7.3% as at 31 December 2013. This restatement will be part of the regulatory capital calculation only once formally audited.

CRD IV fully-loaded capital position

	As at 30 June 2014	As at 31 December 2013	Change
Capital ratios			
Common Equity Tier 1 ratio	**11.5%**	7.2%	4.3%
Total capital	**13.4%**	9.0%	4.4%
Risk weighted assets (£bn)	**13.9**	15.1	(1.2)
Leverage ratio	**3.7%**	2.4%	1.3%

The £400m additional capital raising in May and the Co-operative Banking Group CET1 injections of £50m in January and £100m in June were the primary factors in the Bank's CET1 position increasing by £0.5bn to £1.6bn between December 2013 and June 2014. A further CET1 injection of £163m from the Co-operative Banking Group is due to be provided before the end of 2014. The increase in CET1 has resulted in the Bank's fully-loaded CRD IV CET1 ratio increasing by 4.3%, from 7.2% to 11.5%.

Risk weighted assets have decreased by £1.2bn since the year end. Non-core assets have been actively reduced and this is reflected in the £0.6bn reduction in Non-core risk weighted assets.

Leverage ratio is 3.7%, an increase of 1.3% since the 2013 year end. This is now above the proposed 3.0% regulatory minimum, due to be implemented in 2018.

The Bank is not currently compliant with its Individual Capital Guidance (ICG), being the PRA's statement as to the regulatory capital it expects the Bank to hold, although the Bank does meet its Pillar 1 capital requirements.

The capital plan, which has been shared with the PRA, forecasts that the Bank will meet the 7% CET1 ratio throughout the planning period. The capital plan anticipates sustainably meeting ICG by the latter part of the planning period, however full compliance with its current Capital Planning Buffer (CPB) is not anticipated during the planning period.

Liquidity

Overview

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

The focus of the funding and liquidity strategy of the Bank continues to be to:

- Reduce the holding of investment grade bonds not eligible for inclusion in the liquid asset buffer (LAB). This has maintained the cash held at central banks. It has also reduced the reliance on short dated secured financing to fund such assets and in turn reduced the amount of Treasury assets encumbered by the Bank;
- Increase secondary liquidity by further increasing the availability of mortgage collateral for funding; and
- Maintain ratings of secured funding programmes by the implementation of rating agency compliant back-up servicing arrangements to help ensure market access.

Credit rating

In 2013, Fitch and Moody's downgraded the Bank by several notches. In April 2014, Moody's further downgraded the Bank to Caa2 from Caa1. The current ratings are:

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

The credit rating downgrades have:

i. Led to sub-investment grade ratings on the Bank's senior debt in turn leading to a significant reduction in the demand for these types of instrument;

ii. Negatively impacted the Bank's ability to access short term unsecured wholesale funding; and

iii. Increased the Bank's collateral requirements within some clearing systems.

Liquidity portfolio

The Bank's liquidity resources as at 30 June 2014 were £12.1bn compared to £11.2bn as at 31 December 2013. The table below analyses the Bank's liquidity portfolio by product and by liquidity value. Primary liquidity consists of liquid assets that are eligible under BIPRU 12.7 (LAB) and secondary liquidity consists of all other liquid assets (including self-issued retained securitisations and whole loans).

Liquidity has increased over the period with an increase in primary liquidity of £624.1m and secondary liquidity of £265.5m.

	June 2014 £m	December 2013 £m	Change £m
Operational balances with central banks	**5,804.9**	5,076.3	728.6
Gilts	**974.2**	789.5	184.7
Central government and multilateral development bank bonds	**823.0**	1,112.2	(289.2)
Total primary liquidity	**7,602.1**	6,978.0	624.1
Total secondary liquidity	**4,480.9**	4,215.4	265.5
Total liquidity	**12,083.0**	11,193.4	889.6

Retail and commercial funding

The majority of the Bank's funding comes from retail and commercial accounts. As at 30 June 2014, customer deposits were £31.5bn compared to £33.0bn as at 31 December 2013.

Retail deposits reduced over the period by c.£0.7bn.

The total amount of the Bank's corporate deposits has reduced by c.£1.0bn over the first half of the year. This was due to term deposits maturing which had been placed before last year's credit rating downgrades.

	June 2014 £m	December 2013 £m	Change £m
Current accounts			
Retail	**3,361.1**	3,378.1	(17.0)
Corporate	**2,181.6**	2,298.9	(117.3)
Total current accounts	**5,542.7**	5,677.0	(134.3)
Instant access savings accounts			
Retail	**7,498.7**	8,097.2	(598.5)
Corporate	**583.9**	666.2	(82.3)
Total instant access saving accounts	**8,082.6**	8,763.4	(680.8)
Term deposits and bonds			
Retail	**9,642.0**	9,879.5	(237.5)
Corporate	**534.1**	1,344.9	(810.8)
Total term deposits and bonds	**10,176.1**	11,224.4	(1,048.3)
Individual savings accounts (ISA):			
Retail – ISA Fixed	**3,914.6**	3,853.1	61.5
Retail – ISA Demand	**2,519.2**	2,455.2	64.0
Total ISA accounts	**6,433.8**	6,308.3	125.5
Other deposits	**1,223.8**	1,028.3	195.5
Total customer deposits	**31,459.0**	33,001.4	(1,542.4)

Wholesale funding

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

In January, the Bank repaid a c.£400m bilateral facility and in February, the Bank redeemed a €25m Medium Term Note (MTN). Notice has been given for the optional redemption of the Silk Road Finance Number Two securitisation in September 2014. This is referred to in more detail in note 20.

	June 2014 £m	December 2013 £m	Change £m
Preference shares, PSBs and subordinated debt	**206.7**	196.3	10.4
Secured funding	**3,706.3**	4,339.5	(633.2)
Repos	**1,496.2**	2,119.3	(623.1)
Market borrowing	**61.5**	56.6	4.9
MTNs	**850.9**	884.0	(33.1)
Total wholesale funding	**6,321.6**	7,595.7	(1,274.1)

	June 2014 £m	December 2013 £m	Change £m
Repayable in less than 1 month	**678.5**	2,010.3	(1,331.8)
Repayable between 1 and 3 months	**1.0**	67.8	(66.8)
Repayable between 3 and 12 months	**1,232.4**	157.2	1,075.2
Repayable between 1 and 5 years	**996.7**	1,800.8	(804.1)
Repayable in more than 5 years	**3,413.0**	3,559.6	(146.6)
Total	**6,321.6**	7,595.7	(1,274.1)

The table does not include the Funding for Lending Scheme. The Bank accessed the Funding for Lending Scheme in the first half of 2013, drawing £900m of UK treasury bills. The UK treasury bills remain available to the Bank until March 2017.

Figures are based on nominal values and accrued interest as at 30 June 2014 and 31 December 2013.

2014 Financial Performance

Total Bank financial performance

The financial results for the first half of 2014 reflect initial progress in the Bank's Turnaround Plan with a statutory loss before taxation of £75.8m (H1 2013: £844.6m loss[1]) representing a significant improvement on the first half of 2013. The main factors impacting on the overall Bank performance are credit impairment stabilisation and a steady operating expenditure base. Our review of products and practices is continuing, however no new categories of conduct and legal risk have been provided for in the first half of 2014.

The Bank is continuing to successfully implement its Non-core asset deleverage strategy with customer assets reducing by £989.7m since December 2013 to £11.5bn. Overall the Bank's balance sheet has contracted by £2.3bn since December 2013 mainly due to a reduction in customer assets. As well as the Non-core strategy, Retail mortgage lending has been impacted by the Mortgage Market Review (MMR) and increased redemptions.

There remain a number of challenges ahead, including a continuing need to control and reduce the cost base, generate additional Core Bank income and complete the separation from the Co-operative Group.

	June 2014 £m	June 2013 £m	Change £m
Retail contribution[a]	**177.7**	156.4	21.3
BaCB contribution[a]	**20.8**	30.1	(9.3)
Treasury/other contribution[a]	**(31.9)**	17.7	(49.6)
Core contribution profit[a]	**166.6**	204.2	(37.6)
Operations and central costs[b]	**(174.5)**	(169.2)	(5.3)
Project costs	**(60.0)**	(45.2)	(14.8)
Core operating loss	**(67.9)**	(10.2)	(57.7)
Non-core operating result[b]	**97.3**	(490.4)	587.7
Bank operating result	**29.4**	(500.6)	530.0

a The Bank manages segmental analysis on a contribution basis. Contribution excludes operations and centralised costs and project costs. Comparative numbers have been restated for H1 2013 on a like for like basis.

b Operations and central costs are not allocated across the business segments within Core and Non-core. £9.8m is attributable to Non-core.

The Core business generated an operating loss of £67.9m (H1 2013: £10.2m loss) the variance of £57.7m is driven by Treasury/other contribution losses of £31.9m (H1 2013: £17.7m profit)[2] as a result of holding higher liquidity as well as a different asset quality mix of liquidity levels, and Retail contribution has improved by £21.3m on 2013 with lower income being more than offset by improving credit impairment and reduced costs.

The Non-core business, targeted for rundown and exit as part of the Bank's strategy, generated an operating result of £97.3m (H1 2013: £490.4m loss) benefiting significantly from improving credit conditions and management actions which allowed releases of credit impairment provisions.

The Bank's Net Interest Margin (NIM) improved to 1.17% (H1 2013: 1.02%) with the Core bank NIM at 1.58% up on 2013 by 3bps. Retail NIM improved year on year (H1 2014: 2.51%, H1 2013: 2.30%). This increase is driven by reduced pricing on liability products and increased mortgage redemption income offset by a higher liquidity recharge.

The margin increases in the Retail business have been offset by reductions in NIM in both BaCB (driven by a reduction of liability balances) and in the Treasury portfolio (driven by excess liquidity).

	June 2014 £m	June 2013 £m	Change £m
Operating income	**308.5**	347.4	(38.9)
Operating expenditure[c]	**(297.0)**	(307.2)	10.2
Project costs[d]	**(68.8)**	(48.9)	(19.9)
Impairment gains/(losses) on loans and advances[e]	**86.7**	(491.9)	578.6
Operating result	**29.4**	(500.6)	530.0
FSCS levy (Bank)	**(25.3)**	(24.7)	(0.6)
Share of post tax (losses)/profits from joint ventures	**(0.1)**	0.3	(0.4)
Intangible asset impairment	**–**	(148.4)	148.4
Conduct and legal risk[4]	**(38.6)**	(163.0)	124.4
Fair value amortisation	**(41.2)**	(8.2)	(33.0)
(Loss)/profit before taxation	**(75.8)**	(844.6)	768.8

1 H1 2013 includes: a restatement of £24.8m additional expense relating to FSCS Levy, (£(8.0)m interest income and £(0.4)m non-interest income), relating to changes to hedge accounting methodology. (See note 3).

2 H1 2013 includes profits from sale of assets of £40.4m (£35.0m non-interest income and £5.4m interest income).

3 H1 2013 Cost income ratio has been restated to 88.4% due to the inclusion of £4.1m of fraud, previously classified within impairment and the £8.4m charge to income relating to changes to hedge accounting methodology.

4 H1 2013 Conduct and legal risk excludes £3.7m redress costs relating to interest payments, which has been included within operating expenditure.

In 2013 we showed operating costs split between 'steady state' and 'strategic initiatives'. These classifications have now been amended as follows:

c Steady state operating costs have now been split into direct costs (by business segment) and operations and centralised costs. These are known collectively as operating expenditure at divisional level for Core, Non-core and Total Bank.

d Strategic initiatives are now classified as 'Project costs'. Project costs also include 'Non-operating costs' reported in 2013 below operating result.

e H1 2013 includes £4.1m reclassification to direct operating costs related to losses associated with fraudulent customer activities that were identified during the period.

The numbers referenced and presented on these pages are on a management accounts basis. A reconciliation of these numbers to the statutory accounts basis is provided in the segmental information in note 4.

Balance sheet contraction and lower non-interest income has led to income falling by £38.9m to £308.5m. This, coupled with stable operating costs, as set out below, has led to an increase in the cost income ratio to 96.3% (H1 2013: 88.4%)[3].

Operating costs

	June 2014 £m	June 2013 £m	Change £m
Core Bank direct costs	**(98.5)**	(110.0)	11.5
Non-core direct costs	**(14.2)**	(8.6)	(5.6)
Operations and central costs	**(184.3)**	(188.6)	4.3
Total operating costs	**(297.0)**	(307.2)	10.2

The costs above reflect the operating costs of the Bank and exclude all project expenditure. Costs for the first half of 2014 are £297.0m, a reduction of £10.2m (3%) on the same period in 2013.

Within the Core Bank, direct costs for H1 2014 are £98.5m (H1 2013: £110.0m), a year on year reduction of £11.5m (10%). This is mainly as a result of cost saving initiatives including the reduction of branches from 294 to 248 resulting in a saving of £3m in H1 2014 (£6.8m annualised). Other initiatives include reduced third party contract spend and process improvements to deliver headcount reductions.

Non-core direct costs are £14.2m (H1 2013: £8.6m). This year on year increase of £5.6m (65%) reflects the cost of managing the accelerated deleveraging activity.

Operations and central costs are £184.3m (H1 2013: £188.6m), a year on year reduction of £4.3m (2%). Process improvements in the first half of the year driven by IT and Operations have resulted in reduced headcount and third party spend delivering cost reductions of c.£15m (£34m annualised). (H1 2013 also included a one-off provision for ATM rates not included in expenses for H1 2014 of £14m.) These cost reductions are offset by c.£10m of incremental costs arising as a result of the separation of the Bank from the Co-operative Group. This comprises one-off third party contract separation costs and incremental VAT (predominantly associated with delays in separation) and further ongoing costs arising from separation dis-synergies. Incremental costs have also arisen as a result of colleague bonuses, the impact of recognising the Britannia pension scheme on the Bank's balance sheet and the incremental cost of implementing increased banking industry regulation.

	June 2014 £m	June 2013 £m	Change £m
Staff costs	**(127.8)**	(123.8)	(4.0)
Non staff costs	**(169.2)**	(183.4)	14.2
Total operating costs	**(297.0)**	(307.2)	10.2

Staff costs have increased year on year by £4m. Staff numbers (full time equivalents) year on year have fallen by 21% to 5,860 delivering a 10% sustainable reduction in salary costs in H1 2014. This has been offset by a short to medium term increase in contractor costs (primarily specialist resource required to support the Bank's transition), a provision for colleague bonuses as part of the Bank's staff retention initiatives and the impact of recognising the unfunded Britannia pension scheme in the accounts of the Bank.

Non staff costs have fallen by £14.2m year on year. The main drivers for the cost reduction relate to a one-off ATM rates provision included in H1 2013 of £14m and the financial impact of cost reduction initiatives as outlined above. These have been offset by additional costs arising from separation and fees associated with the cost of managing the accelerated deleveraging activity.

Project costs

	June 2014 £m	June 2013 £m	Change £m
Operational projects	**(20.3)**	(12.6)	(7.7)
Remediation, integration and resiliency projects	**(20.9)**	(5.0)	(15.9)
Strategic projects and exceptional items	**(27.6)**	(31.3)	3.7
Total project expenditure	**(68.8)**	(48.9)	(19.9)

Non-capital project costs for the half year are £68.8m, an increase of £19.9m on 2013. Although total project investment spend (revenue and capital) is in line with 2013, a focus on remediation and regulatory projects resulted in a higher charge to revenue and a reduced level of capitalisation in H1 2014. Capital spend is anticipated to increase in H2 2014 and continue in future years of the Plan as strategic projects are initiated and existing projects progress.

Operational project expenditure is necessary to ensure the regulatory and mandatory requirements of the Bank are met. Increased expenditure in H1 2014 of £7.7m is mainly due to further investment in the Regulatory Reporting Programme to comply with the Basel III reporting regulations and on Mortgage Business Review to deliver a solution to meet the MMR and Mortgages Conduct of Business legislation.

Expenditure on remediating, integrating and improving resiliency has increased in H1 2014 as work on the IT Remediation Programme, which was initiated in H2 2013, continues. A further £6.8m has been incurred in H1 2014 in separating the Bank from the Co-operative Group, its former parent.

Strategic projects predominantly cover spend on the delivery of a new platform to provide enhanced digital capabilities for online and mobile banking. Additional strategic investment in H1 2014 included redundancy costs of £7.4m and £6.9m relating to the impairment of branch related infrastructure as a result of new technology in the branches. Phase 1 of the Branch Transformation Programme was provided for in H2 2013 and no incremental costs have therefore been incurred in H1 2014. Further branch transformation costs will be incurred in H2 for additional branch closures.

Impairment losses

All segments of the business have lower impairment losses as a result of improved credit conditions. In particular a Non-core impairment of £88.2m benefit has been recognised in the first half of the year (H1 2013: £469.1m charge), due to the new team focusing on the distressed asset work-out and turnaround capability and, as a result of both this specialist team and the improving economic environment, assets have been disposed of at favourable prices resulting in write-back of previously recognised impairment provisions. In addition, the Bank has booked upwards revisions to valuations for assets still held, where credible offers at levels in excess of carrying values as a result of work undertaken. Two connections in this category which were restructured in the latter part of the period account for around half of the overall credit impairment write back.

At 30 June 2014, the year on year improvement in the impairment losses is also reflected in the Bank's balance sheet position with provision coverage reduced to 28.4% (H1 2013: 33.3%) and impaired loans as a percentage of assets at 11.5% (H1 2013: 12.3%).

Conduct and legal risk

Whilst the review of products and practices is continuing, no new categories of conduct risk have been provided for in 2014.

The total conduct and legal risk charge for the period of £38.6m (H1 2013: £163.0m) includes £29m relating to previously identified breaches of the technical requirements of the Consumer Credit Act (CCA) within the unsecured book, a further £5m increase for Payment Protection Insurance (PPI) and an additional net £4.6m for mortgage related conduct risk (see note 13).

The additional PPI provision reflects the latest trends and expectations of complaint volumes, uphold rates, payout data and costs. The CCA provision includes £16m for the first half of 2014 of interest foregone per prior guidance plus an additional amount of £13m due to revision of previous estimates from 2013. A review of methodology led to the additional mortgage related provision due to the availability of better information as work continues through the remediation and customer redress process which is expected to be completed in 2015.

Total Bank balance sheet

Total assets

	June 2014 £m	December 2013 £m	Change £m
Cash and balances at central banks	**6,103.7**	5,418.8	684.9
Loans and advances to banks	**1,644.6**	1,594.4	50.2
Loans and advances to customers	**27,836.4**	30,322.2	(2,485.8)
Investment securities	**4,197.9**	4,499.4	(301.5)
Other assets[f]	**1,294.0**	1,562.5	(268.5)
Total assets	**41,076.6**	43,397.3	(2,320.7)

f Restatement of 2013 Other assets by £1.2m. Comprising of fair value on hedged risk accounting change £(1.3)m and deferred tax £2.5m. (See note 3).

Loans and advances to customers have reduced, primarily in the Core Retail business due to lower mortgage originations which have been affected by the on-going impact of the MMR (increased requirements for banks to ensure the product is suitable for the customer) and mortgage redemptions. In addition the Non-core asset deleverage strategy has reduced the Bank's balance sheet by £1bn.

Total liabilities

	June 2014 £m	December 2013 £m	Change £m
Deposits by banks	**2,136.3**	2,757.5	(621.2)
Customer accounts	**31,459.0**	33,001.4	(1,542.4)
Debt securities and derivatives[g]	**4,361.9**	4,746.2	(384.3)
Other borrowed funds	**196.3**	196.3	0.0
Other liabilities[h]	**807.9**	903.4	(95.5)
Total liabilities	**38,961.4**	41,604.8	(2,643.4)

g Restatement of 2013 Debt securities and derivatives by £12.3m due to change in fair value on hedged risk accounting. (See note 3).

h Restatement of 2013 Other liabilities by £(26.3)m due to change in FSCS levy accounting. (See note 3).

Customer liabilities have been adversely impacted by past negative media coverage of the Bank and the Co-operative Group with whom we share our brand. To counter this, the Bank has invested in a wide-ranging customer driven review into values and ethics to build upon its ethical stance and consolidate brand loyalty. The Bank has commenced work on a marketing campaign which builds on the Bank's brand positioning.

Retail

	June 2014 £m	June 2013 £m	Change £m
Net interest income	**201.5**	203.5	(2.0)
Non-interest income	**55.9**	65.0	(9.1)
Net income	**257.4**	268.5	(11.1)
Direct costs[i]	**(78.4)**	(90.4)	12.0
Impairment losses on loans and advances[i]	**(1.3)**	(21.7)	20.4
Contribution result	**177.7**	156.4	21.3
Net interest margin (annualised)	**2.51%**	2.30%	0.21%

	June 2014 £m	December 2013 £m	Change £m
Customer assets	**15,335.5**	16,790.9	(1,455.4)
Customer liabilities	**27,249.1**	27,899.3	(650.2)

i H1 2013 includes £3.2m reclassification to direct costs from impairment on loans and advances, related to losses associated with fraudulent customer activities that were identified during the period.

The Retail contribution result for 2014 is £177.7m (H1 2013: £156.4m). This performance reflects lower non-interest income, improved costs and lower impairments.

Net interest margin has increased year on year to 2.51% (increase of 0.21%). This increase is driven by maintaining net interest income levels relative to reducing customer balances. Despite lower customer receipts, the Retail Bank has benefited from lowering customer rates on long term savings products in line with the market. Additional income from mortgage redemptions has been offset by higher liquidity recharging as a result of a change in allocation policy. The Retail Bank has seen interest income reductions resulting from balance outflows due to negative publicity and mortgage pricing actions taken in 2013. In addition, mortgage sales have been affected by the new mortgage market regulations which came into force earlier this year.

However, despite the adverse publicity of late 2013 and early 2014, and focused marketing action from competitors resulting in some loss of customers, the overall customer base remains loyal. During the first half of the year the Bank had a net loss of 28,199 current accounts, which represents less than 2.0% of the opening stock of accounts. Alongside recommencement of Retail mortgage lending activities, recent trends indicate that the net outflow of retail customers has slowed. Furthermore, income reductions have been offset by the favourable macro impairment climate, mainly driven by increases in the house price index this year.

Business and Commercial Banking (BaCB)

	June 2014 £m	June 2013 £m	Change £m
Net interest income	**23.0**	34.4	(11.4)
Non-interest income	**7.9**	7.7	0.2
Net income	**30.9**	42.1	(11.2)
Direct costs[j]	**(8.7)**	(11.5)	2.8
Impairment losses on loans and advances[j]	**(1.4)**	(0.5)	(0.9)
Contribution result	**20.8**	30.1	(9.3)
Net interest margin (annualised)	**5.67%**	7.18%	(1.51%)

	June 2014 £m	December 2013 £m	Change £m
Customer assets	**778.8**	844.9	(66.1)
Customer liabilities	**2,594.6**	3,479.0	(884.4)

j H1 2013 includes £0.9m reclassification to direct costs from impairment on loans and advances, related to losses associated with fraudulent customer activities that were identified during the period.

Similarly, BaCB has experienced contraction in its balance sheet as a result of difficult trading conditions. In particular, in line with expectations, customer deposits have reduced by £884.4m in the first 6 months, as annual fixed term deposits have not been renewed by ratings sensitive depositors.

Total net interest income has fallen driven by the reduction in the liability balances, and as customer assets are significantly lower than the liability balances, the net interest margin has materially reduced.

Treasury/Other

	June 2014 £m	June 2013 £m	Change £m
Net interest income	**(3.6)**	(1.4)	(2.2)
Non-interest income	**(18.1)**	27.8	(45.9)
Net income	**(21.7)**	26.4	(48.1)
Direct costs	**(11.4)**	(8.1)	(3.3)
Impairment gains/(losses) on loans and advances	**1.2**	(0.6)	1.8
Contribution result	**(31.9)**	17.7	(49.6)
Net interest margin (annualised)	**(0.06)%**	0.06%	(0.12)%

	June 2014 £m	December 2013 £m	Change £m
Assets	**11,387.7**	10,932.4	455.3
Liabilities	**6,886. 5**	8,040.4	(1,153.9)

The reduction in net interest income has been driven by two factors:

- The change in asset and liability mix of the Treasury balance sheet; and
- A revised policy on distributing the cost of holding liquidity.

Treasury continued to reduce assets not eligible for the liquid asset buffer, resulting in an asset portfolio consisting materially of highly liquid gilts, multilateral development banks and cash. The downgrade of the Bank's credit ratings in 2013 to below investment grade led to a reduction in the Bank's rating sensitive deposits. These deposits had a relatively low cost of funding compared to non-rating sensitive deposits. There was also wholesale funding entered into with a higher cost of funding, which together with the rating sensitive deposit impact increased the average cost of funding of the Bank's liquidity portfolio. Furthermore, due to lower credit ratings, the Bank is required to maintain collateral postings within central payment systems. These assets typically consist of lower yielding government bonds and Treasury bills thereby further impacting net interest income.

The allocation policy for the cost of holding the Bank's liquid asset buffer (LAB) was changed at the start of 2014, resulting in Treasury absorbing the cost of holding any liquid assets above the liquidity risk appetite (LRA) amount directly attributable to products (as opposed to allocating out the entire LAB cost). The impact of this policy change in H1 2014 was a reduction in net interest income for Treasury of c.£11m as more of the cost was retained and not distributed to other business segments.

The Bank has reviewed its hedge accounting strategies in conjunction with its auditors and the interpretations applied to hedge accounting in accordance with IAS 39 (Financial Instruments: Recognition and Measurement) and best practice. Based on this review the Bank has amended its calculation of hedge ineffectiveness resulting from these models and retrospectively restated prior year results for the change in methodology (see note 3). This has decreased the net interest income by £3.4m (H1 2013: £(8.0)m) in the first 6 months of 2014. This does not affect the economic performance of the hedge.

Non-interest income has reduced significantly when compared to the first half of 2013 due to:

- Losses on the sale of non-liquid assets; and
- The hedge accounting adjustment loss on cross currency swaps.

During the first six months of 2013 profits from asset sales accounted for c.£35m of non-interest income whilst there was a loss of c.£4m on asset sale proceeds recorded in H1 2014.

The hedge accounting review (see note 3) has resulted in a loss of £6.4m (H1 2013: £0.4m loss) on cross currency micro hedging which has added to the reduction in non-interest income.

Non-core

	June 2014 £m	December 2013 £m	Change £m
Corporate CoAM	**4,867.9**	5,646.1	(778.2)
Optimum	**7,117.4**	7,326.1	(208.7)
Illius	**156.0**	162.2	(6.2)
Assets	**12,141.3**	13,134.4	(993.1)
Corporate CoAM	**809.3**	831.0	(21.7)
Optimum	**–**	–	–
Illius	**–**	–	–
Liabilities	**809.3**	831.0	(21.7)
Customer assets	**11,483.7**	12,473.4	(989.7)
Customer liabilities	**809.3**	831.0	(21.7)

	June 2014 £m	June 2013 £m	Change £m
Net interest income	**27.0**	4.5	22.5
Non-interest income	**14.9**	5.9	9.0
Net income	**41.9**	10.4	31.5
Operating expenditure	**(24.0)**	(28.0)	4.0
Project costs	**(8.8)**	(3.7)	(5.1)
Impairment gains/(losses) on loans and advances	**88.2**	(469.1)	557.3
Operating result	**97.3**	(490.4)	587.7

In line with its strategy, the Bank is actively reducing its Non-core assets. The Bank has been able to achieve favourable disposal proceeds due to proactive restructuring of assets and improved credit conditions and has benefited from the establishment of a dedicated team focused on the deleverage of the book. The team has special skills in managing Non-core/ defaulted/ non-performing assets. Consequently, the Non-core operating result shows a profit in the first half of 2014 of £97.3m (H1 2013: £490.4m loss).

The Corporate portfolio contributions were £96.3m (H1 2013: £406.2m loss) driven by impairment credits, and the Optimum portfolio (a closed book of intermediary and acquired mortgage book assets) recorded a contribution of £26.1m (H1 2013: £41.6m loss).

The Illius business (a closed residential property portfolio) incurred a contribution loss of £6.5m (H1 2013: £19.5m loss). This favourable improvement on last year is mainly as a result of reduced fair value impacts to the asset portfolio H1 2014: £6.1m charge (H1 2013: £18.9m charge).

Balance sheet liabilities – Non-core

Corporate liabilities have fallen in line with strategy as there is active management of customers to enable them to move into an ongoing relationship with another provider.

Balance sheet assets – Non-core

The Corporate CoAM assets, net of provisions, have decreased by £0.8bn as at 30 June 2014 to £4.9bn through the deleveraging strategy. The closed Optimum portfolio has also reduced by £0.2bn as customers continue to pay down their mortgages.

Outlook

The Bank is in the early stages of its Turnaround Plan and we have made good progress in delivering some aspects of the strategy particularly in Non-core deleveraging which is on track to deliver against its revised short to medium term targets. The additional capital raise in the first half of the year has provided a firmer foundation to deliver the Core Bank strategy of serving the needs of individuals and SMEs where the Bank has heritage and strong customer relationships. The management team continues to believe the Plan will deliver a sustainable improvement in performance over time.

We have seen improvements in the macroeconomic outlook, however the Bank continues to face both internal and external challenges in the effective execution of the objectives that underpin the strategy. The most significant of the risks and challenges the Bank faces are summarised in the Principal risks and uncertainties section of this Interim Financial Report.

Principal risks and uncertainties

Background to the significant risks and uncertainties faced by the Bank

Significant elements of the uncertainty around the going concern status of the Bank were removed with the successful completion of the two capital raising exercises in December 2013 and May 2014, however, the Bank continues to face challenges in executing its Turnaround Plan. The Bank will need to simultaneously execute a number of complex and concurrent changes in an environment where adverse publicity regarding events and the Bank's difficulties (and the circumstances that led to those difficulties) may have damaged the Bank's brand and reputation. More details of the risks facing the Bank are set out in the risk factors which were set out in the offering circular in May 2014 for the recent capital raising which can be located on our website (http://www.co-operativebank.co.uk/assets/pdf/bank/news/Risk-factors-May-2014.pdf).

External factors

Many of these are similar to those other financial institutions may face, for example, deterioration in general economic conditions, instability of global financial markets and the management of credit risk, interest rate risk, currency risk and market risk and risks from regulatory change and an increasing regulatory enforcement and litigious environment.

In July 2014, the Competition and Markets Authority (CMA) announced a potential review into the operation of the current account and SME banking markets. Such enquiries tend to be time consuming and require management time and attention. It is currently not possible to ascertain whether the impact of such a review and any consequential structural changes or requirements for the industry as a whole would be positive for or harmful to the position of the Bank.

Internal factors

Outlined below is the most significant of those risks and uncertainties specific to the Bank and which could have a meaningful impact on the Bank's results of operations, financial conditions and prospects.

Key strategic risks and uncertainties

- The Bank's Turnaround Plan is in the early stages of implementation and has yet to be proven. A failure to successfully implement or a delay in implementing the Bank's strategy may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements;
- The Bank does not have a track record in successfully executing large scale changes like those contemplated by its plan;
- The required improvement and re-engineering of the Bank's IT platform and operational process is significant in scale, complexity and cost. Any delays in, or failure by, the Bank to deliver the re-engineering of the Bank's IT platform may result in on-going risk of technology failure, significant additional investment costs, subject the Bank to further regulatory scrutiny and impact the Bank's ability to deliver its turnaround strategy;
- Along with the wider banking industry, the Bank must comply with multiple regulatory changes which may add complexity to an already difficult technology and prudential change programme;
- These regulatory initiatives may also have an impact on systems, processes and product design with potential compliance and investment costs;
- A new Chairman will need to be appointed and there are a number of recent appointments to the Board which need to be embedded. Despite progress on retention and recruitment, the Bank is dependent on its Directors, senior management team and skilled personnel and the loss of one or more Directors or members of senior management or the loss of or failure to recruit and retain skilled personnel may have an adverse effect on the Bank's business, operating results, financial condition and prospects and its ability to achieve its strategy;
- Implementation of significant cost reductions, branch closures, redundancies and reorientation of the Bank's distribution channels may not achieve the targeted cost savings. These cost savings may have a negative impact on the Bank's brand, customer service and levels of customer satisfaction and therefore income;
- The inability of the Bank to deleverage its Non-core assets in a controlled and capital efficient manner may have a negative impact 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. Any greater than expected costs or delays in deleveraging the Non-core assets may divert funding from and adversely impact the growth of the Core business;
- The Non-core business has impairment risk, especially given the concentration of the Non-core corporate asset book;
- Given the relative size of the Bank's retail deposit base as compared with other sources of funding, the Bank is particularly exposed to liquidity risks caused by any serious loss of confidence by its depositors resulting in unusually high levels of withdrawals;
- 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 may be required to hold more regulatory capital, or to take other steps to mitigate the risks identified, as part of the stress tests of capital adequacy, profitability and capital ratios that the Bank and seven other UK banks submitted in 2014 to the FCA and PRA for consideration by the fourth quarter of 2014;
- The Bank needs the ongoing forbearance of the PRA regarding its ICG deficit. The PRA has the discretion to revisit, change or withdraw that forbearance. If the Bank fails to meet its ICG, there is a risk that the PRA may exercise any of its wide-ranging powers over the Bank including imposing a resolution procedure on the Bank at any time;
- Additional non-CET1 capital is contemplated by the Bank's four to five year Turnaround Plan. Further additional equity and/or debt capital may be required, beyond that contemplated currently, because of increased capital requirements (applicable to the Bank or banks generally), actual costs and losses exceeding those estimated in the Bank's plan or if the Bank does not deliver on its plan as anticipated the Bank may be unable to raise any additional CET1 or other capital it may need on favourable terms, when needed, or at all;

- Future legislative and regulatory changes could 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;
- There is a risk that the Bank's ownership structure following the Liability Management Exercise and the Capital Raising may undermine the Bank's reputation as being more focused on values and ethics than its competitors. Such a reputation has been a competitive advantage for the Bank;
- The Bank will continue to rely on the Co-operative brand. Should, as a result of matters relating to the Co-operative Group, the Bank's brand, levels of customer satisfaction or the co-operative movement more generally be damaged, this would 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 stated strategy;
- The Co-operative Group could sell some or all of its ordinary shares in the Bank to an unknown third party; and
- In the event that the current process of consultation on changes to governance arrangements at the Co-operative Group or any adverse findings of any of the various enquiries and investigations underway which impact on the Co-operative Group, result in organisational disruption in operations or decision making at the Co-operative Group, the execution risks to the process of logistical separation could increase with an associated risk of increased costs and disruption for the Bank.

Key operational risks and uncertainties

In this section, by operational risks and uncertainties, we mean risks and uncertainties relating to the Bank's internal activities, systems and controls. The most significant operational risks and uncertainties faced by the Bank include:

- The Bank's underlying business and financial systems are dated and suffer from a lack of integration and investment since the Britannia merger in 2009; consequently many processes rely on significant manual intervention to cope with a poor systems infrastructure;
- The Bank has new external auditors who have yet to complete an audit of the Bank's accounts. This may result in a reassessment of current accounting practices and increased reputational risk;
- The Bank's systems of control have been weak and there have been failings by the Bank's business units in a number of areas in the past;
- Although the foundation of the Bank's more robust controls including the Bank's revised and updated Risk Management Framework (adopted in September 2013) have been laid, it will take time and significant work to embed across the Bank. Inadequate risk management processes could lead to exposures outside the Bank's risk appetite and unforeseen losses;
- 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;
- 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 currently depends on the Co-operative Group to provide a number of services including certain critical functions: IT, personnel, assets and to on-supply certain services, data and assets by third party suppliers. The Bank is operationally dependent on the Co-operative Group and has significant counterparty exposure to the Co-operative Group. Further deterioration or perceived deterioration in the soundness of the Co-operative Group may have a material adverse effect on the Bank's business, financial condition, operating results, reputation and prospects;
- A complex project to separate the Bank from the Co-operative Group is underway. Negotiations continue with the Co-operative Group in relation to the transfer of key assets used by the Bank, and arrangements for the provision of key functions and services to the Bank, including IT. The separation project is complex and may be more costly than currently contemplated. Any new arrangements may be less favourable to the Bank than the existing arrangements;
- In total balances owed by the Co-operative Group to the Bank exceed amounts owed by any other single counterparty. These obligations are under continuous review, however the Board considers that impairment is not currently required; and
- The Bank does not have any documented right to occupy several of its principal establishments and places of business. The Bank's current occupation of some properties owned by the Co-operative Group is in breach of the terms of the lease for that property.

Key regulatory and conduct risks and uncertainties

The Bank is under intense regulatory scrutiny and expects that environment to continue. The Bank is also the subject of multiple regulatory and other investigations and enquiries into events at the Bank and circumstances surrounding them. These are discussed and considered in detail in the 2013 Annual Report and Accounts.

- The Treasury Select Committee has been conducting an ongoing review which began in the second quarter of 2013 and has focused on numerous concerns surrounding the Bank. The Committee will publish a report of its findings, the timing of which is not known;
- The Treasury announced on 22 November 2013 that it would conduct an independent investigation into events at the Bank and the circumstances surrounding them from 2008, including the Verde transaction and Britannia acquisition. The investigation will include a review of the conduct of regulators and Government, but is not anticipated to commence until it is clear that it will not prejudice the outcome of the FCA and PRA enforcement investigations;
- The FCA announced on 6 January 2014 that it will be undertaking enforcement investigations into events at the Bank. The investigation will look at the decisions and events up to June 2013; and
- The PRA announced on 6 January 2014 that it is undertaking an enforcement investigation in relation to the Bank and as part of that investigation will consider the role of former senior managers.

Both FCA and PRA investigations are underway but still in the early stages and the Bank is co-operating fully.

It is still too early to predict the outcome of each of these investigations with any degree of certainty. These investigations and inquiries are likely to result in:

- Significant expense which may include damages, fines and other penalties;
- Greater scrutiny and/or intervention from regulators, further regulatory action and/or litigation;
- Taking a significant amount of management time and resources away from management of the Bank's business including execution of the Bank's plan; and
- Further adverse publicity and reputational damage to the Bank, its brand and its ability to recruit and retain personnel and customers.

In addition, 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 regulators to be inappropriate, unfair or non-compliant with applicable law or regulations. Any failure to manage these risks adequately could lead to further significant provisions, costs and liabilities and/or reputational damage.

The Bank's approach to provisions for historic mis-selling issues such as PPI, interest rate swaps and packaged accounts is based on the views and requirements of the regulator. Any change in the regulator's current approach, such as an extension of the period covered by the requirement for proactive contact with customers, could have a material impact.

The Bank is exposed to many forms of legal and regulatory risk, which may arise in a number of ways. As part of its strategy to identify and resolve outstanding liability issues, the Bank has started a structured risk-based assessment, of which the primary focus is the discovery and remediation of existing and new issues. These efforts have already resulted in the discovery of existing and new issues and the Bank is seeking to remediate such matters. However, while much work has been undertaken and progress has been made in identifying conduct issues, no assurance can be given that further issues will not be identified, or that the already identified issues may not require further provision.

The Bank has a large number of remediation projects to execute relating to conduct issues and failings from past business practices, some of which have continuing annual impacts until remediated and which require considerable management time and attention. Such projects are complex, timely and costly and depend on limited subject matter expertise within the Bank. Failing to implement the projects in a timely and efficient fashion could result in ongoing loss of income, increased costs of implementation, regulatory fine or censure and reputational damage.

In connection with the Bank's mortgage securitisation and covered bond transactions, the Bank makes various representations and warranties relating to the mortgage loans, including in relation to ownership, compliance with legislation and organisation procedures. If the representations and warranties are breached subject to any applicable materiality determination, or if any actual breaches identified are determined to be material the Bank may be required to repurchase the affected mortgage loans or in some circumstances pay compensation to the securitisation vehicle. There is a risk that a number of the underlying matters giving rise to conduct and legal provisions have given rise to breaches by such representations and warranties and that the process of remediation will require contact with the Trustee. Accordingly, there is a risk that the Bank may be required to pay compensation or to repurchase affected mortgage loans in amounts that may reduce the Bank's liquidity.

The Bank also faces both financial and reputational risk where legal or regulatory proceedings are brought against it or other financial institutions. Liability for damages may be incurred by third parties harmed by the conduct of the Bank's business.

The Bank continues to be exposed to the risks of non-compliance with the Consumer Credit Act. While the Bank has identified certain instances where its documentation or processes have not been fully compliant with the technical requirements, there may be other instances of non-compliance which have not yet been identified. Until remediation of the issues already identified is complete, the Bank remains in breach of the technical requirements of the Act and will be unable to enforce interest charges on the affected products.

Regulatory responsibility for the Consumer Credit Act passed to the FCA on 1 April 2014 and may lead to additional sanctions on banks in the event they are not fully compliant, or a requirement to pay additional redress to customers.

Pensions risks and uncertainties

The Bank participates in the following pensions schemes:

- The Pace Scheme, whose sponsoring employer is the Co-operative Group. The Bank is a participating employer in this scheme;
- The Britannia Scheme, whose sponsoring employer is CFS Management Services Limited; and three of the Bank subsidiaries are participating employers in this scheme. The Bank is a guarantor in respect of this scheme.

Pace

Currently, the Pace Scheme is accounted for by the Bank as a defined contribution plan. In the future, the Bank will account for the Pace Scheme as a defined benefit scheme. This is referred to in more detail in note 15 in the Bank Interim Financial Report.

There remains no contractual agreement determining how the deficit recovery contributions are funded by the participants. The Bank therefore has not recognised a liability in respect of any part of the existing deficit funding. The Bank is currently paying £0.5m per month in deficit funding.

The Bank's obligations to contribute to Pace would increase significantly if another large employer in Pace becomes insolvent while the Bank continues to participate. If the Bank seeks to address these risks by terminating its participation, the default position is that material liabilities in respect of the deficit in Pace will arise. The Co-operative Group and the Bank have agreed that at either party's request it may enter into good faith discussions to manage this by reaching agreement so that the liabilities properly attributable to the Bank (and an equivalent proportion of assets) would be transferred to a separate scheme, or a segregated section of Pace, on the Bank's exit but, as no arrangements have yet been agreed (and there is a risk that none can be agreed), there is uncertainty over the amount that the Bank will have to pay in the event that it exits Pace. The Pace Scheme is not sectionalised and operates on a 'last man standing' basis. In the event that other participating employers become insolvent and the full statutory debt is not recovered on insolvency, the Bank would become liable for the remaining liabilities.

Details of the latest triennial valuation of the Pace scheme are discussed in note 15.

Britannia

In respect of the Britannia Scheme, the Bank will need to manage the liabilities that could arise on separation from the Co-operative Group; this will require the co-operation of the trustees of the Britannia Scheme, which may not be forthcoming.

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

Responsibility statement

We confirm that to the best of our knowledge:

- The condensed set of financial statements has been prepared in accordance with IAS 34 Interim Financial Reporting as adopted by the EU; and
- The interim management report includes a fair review of the information required by:
  - DTR 4.2.7R of the Disclosure and Transparency Rules, being an indication of important events that have occurred during the first half of the financial year and their impact on the condensed set of financial statements; and a description of the principal risks and uncertainties for the remaining half of the year; and
  - DTR 4.2.8R of the Disclosure and Transparency Rules, being related party transactions that have taken place in the first half of the current financial year and that have materially affected the financial position or performance of the entity during that period; and any changes in the related party transactions described in the last annual report that could do so.

By Order of the Board

Niall Booker
Chief Executive

21 August 2014

The Co-operative Bank plc Board of Directors:

Richard Pym	Chairman
Dennis Holt	Senior Independent Director
Niall Scott Kilgour Booker	Chief Executive Officer
Laura Martine Carstensen	Non-Executive Director
John Richard Coates	Non-Executive Director
Richard Graeme Barclay Hardie	Non-Executive Director
Maureen Laurie	Non-Executive Director
William Gennydd Thomas	Non-Executive Director
Derek James Weir	Non-Executive Director

Risk management

For the period ended 30 June 2014 (unaudited)

All amounts are stated in £m unless otherwise indicated

Introduction

The Bank's risk management responsibilities are laid out in the Risk Management Framework, which creates clear ownership and accountability, with the purpose that the Bank's most significant risk exposures are understood and managed in accordance with agreed risk appetite, and there is regular reporting of both risk exposures and the operating effectiveness of controls. It includes those risks incurred by the Bank that are foreseeable, continuous and material enough to merit establishing specific Bank-wide control frameworks.

Further details on these risks and how they are managed is available in the 2013 Annual Report and Accounts.

There have been no significant changes to the Bank's Principal Risks and Risk Management Framework. The risks remain as Credit Risk, Liquidity Risk, Market Risk, Operational Risk, Reputational Risk, Strategic and Business Risk, People Risk, Regulatory Risk, Conduct Risk and Pension Risk as per the 2013 Annual Reports and Accounts.

The following section gives an overview of the performance in Credit Risk, Liquidity Risk and Market Risk.

1. Credit risk

1.1 Overview

Credit risk is one of the principal risks set out in the Risk Management Framework and is an integral part of the business activities of this and all other banks. It is inherent in both traditional banking products (loans, commitments to lend and contingent liabilities such as letters of credit) and in 'traded products' (derivatives such as forwards, swaps and options, repurchase agreements, securities borrowings and lending transactions).

1.2 Credit exposure

The following analysis of credit exposure shows:

- carrying amounts by class of asset in the balance sheet;
- the gross credit exposure by class of asset (excluding allowance for losses but including credit commitments); and
- the net credit exposure by class of asset (including allowance for losses and credit commitments).

Cash and balances at central banks are credit exposures with the Bank of England and have been excluded from the analysis.

30 June 2014	Loans and advances to banks	Loans and advances to customers	Investment securities	Derivative financial instruments	Total
Analysis of balance in note 19					
Gross balance	**1,644.6**	**28,598.2**	**4,197.9**	**440.5**	**34,881.2**
Less: allowance for losses	**–**	**(761.8)**	**–**	**–**	**(761.8)**
	1,644.6	**27,836.4**	**4,197.9**	**440.5**	**34,119.4**
Analysis of credit risk exposure					
Not impaired	**1,644.6**	**25,461.1**	**4,197.9**	**438.1**	**31,741.7**
Impaired	**–**	**3,137.1**	**–**	**2.4**	**3,139.5**
	1,644.6	**28,598.2**	**4,197.9**	**440.5**	**34,881.2**
Credit commitments	**362.3**	**2,985.2**	**–**	**–**	**3,347.5**
Gross credit risk exposure	**2,006.9**	**31,583.4**	**4,197.9**	**440.5**	**38,228.7**
Less:					
Allowance for losses	**–**	**(761.8)**	**–**	**–**	**(761.8)**
Net credit risk exposure	**2,006.9**	**30,821.6**	**4,197.9**	**440.5**	**37,466.9**

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

31 December 2013	Loans and advances to banks	Loans and advances to customers	Investment securities	Derivative financial instruments	Total
Analysis of balance in note 19					
Gross balance	1,594.4	31,274.6	4,519.4	555.8	37,944.2
Less: allowance for losses	–	(952.4)	(20.0)	–	(972.4)
	1,594.4	30,322.2	4,499.4	555.8	36,971.8
Analysis of credit risk exposure					
Not impaired	1,594.4	27,894.9	4,499.4	548.8	34,537.5
Impaired	–	3,379.7	20.0	7.0	3,406.7
	1,594.4	31,274.6	4,519.4	555.8	37,944.2
Credit commitments	570.1	3,519.9	–	–	4,090.0
Gross credit risk exposure	2,164.5	34,794.5	4,519.4	555.8	42,034.2
Less:					
Allowance for losses	–	(952.4)	(20.0)	–	(972.4)
Net credit risk exposure	2,164.5	33,842.1	4,499.4	555.8	41,061.8

Impaired and not impaired balances in the tables above are defined in the following sections on retail credit risk, corporate credit risk and investment securities credit risk.

Fair value adjustments

At the time of the merger of Britannia Building Society with the Bank in 2009, all of the assets and liabilities of Britannia were acquired at their then estimated fair values. Valuations of Britannia's assets included adjustments made for their lifetime future expected losses at that date, referred to as the credit fair value adjustments. Previously, the credit fair value adjustments have been disclosed separately in the above table; the table has now been revised to set off the credit fair value adjustments within the not impaired and impaired gross balances, to better show their gross carrying values in the Bank.

For the purposes of internal management reporting of coverage ratios, loss provisions are grossed up by the amount of remaining credit fair value adjustments and compared to the gross amounts owed by customers, as shown in section 1.3 Credit risk management.

1.3 Credit risk management

The following sections provide further analysis and disclosure of the Bank's credit risk associated with:

- 1.3.1 Loans and advances to customers;
- 1.3.2 Investment securities;
- 1.3.3 Loans and advances to banks; and
- 1.3.4 Derivative financial instruments.

1.3.1 Loans and advances to customers

The tables below analyse the gross balance by impairment classification for the Core (Retail and BaCB) and Non-core (Corporate CoAM, Optimum and Illius) divisions. They include credit commitments, impairment provisions, fair value adjustments and a reconciliation to gross customer balances as this is the basis on which the business manages risk.

The decrease in impairment provisions in the period to 30 June 2014 was observed primarily for the Non-core business, being driven by deleverage activity and updated collateral values.

The Non-core business continues to have additional impairment risk given the underlying assets, which includes Optimum, a closed book of predominantly interest-only intermediary and acquired mortgage book assets. Worsening economic and market conditions and/or increasing interest rates and/or a fall in house prices could result in the Non-core assets suffering from more than expected impairments which would adversely impact on the Bank's operating results and financial position (in particular, its net interest margin) and, in the longer term, its ability to comply with its regulatory capital requirements. The Non-core business' corporate asset book is also relatively concentrated, with the result that a small number of borrowers account for a large proportion of the total loans outstanding. Any significant future impairment of these borrowers would result in a disproportionate impact on the Bank's operating results and financial position.

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

	Core			Non-core			
	Retail banking						
30 June 2014	Secured	Unsecured	BaCB	Corporate	Optimum	Unity Trust Bank	Total
Analysis of balance in note 19							
Gross loans and advances	**14,210.0**	**1,243.1**	**802.0**	**5,493.0**	**6,661.1**	**189.0**	**28,598.2**
Less: allowance for losses	**(4.8)**	**(189.5)**	**(7.0)**	**(531.0)**	**(24.1)**	**(5.4)**	**(761.8)**
	14,205.2	**1,053.6**	**795.0**	**4,962.0**	**6,637.0**	**183.6**	**27,836.4**
Analysis of credit risk exposure							
Not impaired	**14,062.5**	**1,001.2**	**624.3**	**3,856.5**	**5,745.5**	**171.1**	**25,461.1**
Impaired	**147.5**	**241.9**	**177.7**	**1,636.5**	**915.6**	**17.9**	**3,137.1**
	14,210.0	**1,243.1**	**802.0**	**5,493.0**	**6,661.1**	**189.0**	**28,598.2**
Credit commitments	**43.6**	**2,144.1**	**257.6**	**497.1**	**–**	**42.8**	**2,985.2**
Gross credit risk exposure	**14,253.6**	**3,387.2**	**1,059.6**	**5,990.1**	**6,661.1**	**231.8**	**31,583.4**
Less:							
Allowance for losses	**(4.8)**	**(189.5)**	**(7.0)**	**(531.0)**	**(24.1)**	**(5.4)**	**(761.8)**
Net credit risk exposure	**14,248.8**	**3,197.7**	**1,052.6**	**5,459.1**	**6,637.0**	**226.4**	**30,821.6**
Reconciliation of accounting to customer balances							
Gross loans and advances	**14,210.0**	**1,243.1**	**802.0**	**5,493.0**	**6,661.1**	**189.0**	**28,598.2**
Fair value adjustments	**3.8**	**–**	**–**	**93.3**	**83.4**	**–**	**180.5**
Other accounting adjustments	**0.5**	**–**	**–**	**–**	**5.8**	**–**	**6.3**
Gross customer balances	**14,214.3**	**1,243.1**	**802.0**	**5,586.3**	**6,750.3**	**189.0**	**28,785.0**

	Core			Non-core			
	Retail banking						
31 December 2013	Secured	Unsecured	BaCB	Corporate	Optimum	Unity Trust Bank	Total
Analysis of balance in note 19							
Gross loans and advances	15,524.6	1,294.6	840.8	6,504.3	6,922.1	188.2	31,274.6
Less: allowance for losses	(4.5)	(160.2)	(5.8)	(738.4)	(35.5)	(8.0)	(952.4)
	15,520.1	1,134.4	835.0	5,765.9	6,886.6	180.2	30,322.2
Analysis of credit risk exposure							
Not impaired	15,379.6	1,077.7	825.2	4,526.5	5,918.8	167.1	27,894.9
Impaired	145.0	216.9	15.6	1,977.8	1,003.3	21.1	3,379.7
	15,524.6	1,294.6	840.8	6,504.3	6,922.1	188.2	31,274.6
Credit commitments	41.1	2,222.5	399.1	815.5	0.1	41.6	3,519.9
Gross credit risk exposure	15,565.7	3,517.1	1,239.9	7,319.8	6,922.2	229.8	34,794.5
Less:							
Allowance for losses	(4.5)	(160.2)	(5.8)	(738.4)	(35.5)	(8.0)	(952.4)
Net credit risk exposure	15,561.2	3,356.9	1,234.1	6,581.4	6,886.7	221.8	33,842.1
Reconciliation of accounting to customer balances							
Gross loans and advances	15,524.6	1,294.6	840.8	6,504.3	6,922.1	188.2	31,274.6
Fair value adjustments	4.2	–	–	97.7	92.3	–	194.2
Other accounting adjustments	(7.8)	23.6	29.7	(76.1)	1.8	(0.3)	(29.1)
Gross customer balances	15,521.0	1,318.2	870.5	6,525.9	7,016.2	187.9	31,439.7

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

The comparative table has been updated to reflect the changes to Core and Non-core divisions, and in order to show BaCB and Corporate CoAM watchlist accounts being included within impaired balances.

Unity Trust Bank is accounted for as a subsidiary of the Bank. It operates its own credit processes as a separate bank, and is not included in the subsequent analysis of credit risk.

Within the analysis of credit risk exposure in the tables above, fair value adjustments relating to expected credit losses on assets obtained on the merger with Britannia Building Society in 2009 are no longer shown separately, instead they have been allocated against impaired assets.

Other accounting adjustments include accrued interest, interest fair value adjustments and effective interest rate adjustments.

The disclosures in sections Secured residential credit risk, Unsecured retail credit risk and Corporate credit risk are all based on the gross customer balances in the above tables.

Secured residential credit risk

Acquisition and account management

Mortgages are loans to customers secured by a first charge over a residential property. Mortgages are originated directly to customers via branches, telephone and the internet under the Britannia and The Co-operative Bank brands, and via intermediaries under the Platform brand. In the period to 30 June 2014, 51% (2013: 66%) of mortgages were originated directly and 49% (2013: 34%) through intermediaries.

The Britannia and The Co-operative Bank brands only originate prime residential mortgages, while Platform primarily originates a combination of prime residential, almost prime residential and buy-to-let loans.

Historically, these loans have been advanced on a capital and interest payment basis, where the loan is repaid over the term of the loan, or interest only, where the capital element of the loan is repayable at the end of the term. All new advances are on a capital repayment basis, with the exception of buy-to-let lending and existing interest only customers moving home.

During the term of the mortgage, interest only mortgages are managed consistently with capital and repayment mortgages, except for our customer contact strategy. For interest only mortgages this aims to determine if the customer has a satisfactory repayment strategy in place upon loan maturity.

The table below shows residential mortgage completions in the period, analysed by loan-to-value (LTV) and repayment method:

	30 June 2014			31 December 2013		
	Amount advanced	**Average LTV %**	**Interest only %**	Amount advanced	Average LTV %	Interest only %
Retail prime	**135.7**	**53.1**	**4.9**	1,416.1	62.6	1.8
Platform prime	**106.3**	**66.5**	**–**	607.2	68.7	–
Total prime	**242.0**	**58.8**	**2.9**	2,023.3	64.6	1.3
Buy-to-let	**24.2**	**66.0**	**89.0**	128.1	64.7	86.1
Almost prime	**0.1**	**52.2**	**–**	2.4	52.7	–
Total completions	**266.3**	**59.4**	**10.4**	2,153.8	64.5	6.2

A cautious approach to lending, as well as a change to mortgage regulation and time lag between application and completion, has led to a significant reduction in completions in the first half of 2014 when compared to 2013.

The default risk in the portfolio is recalculated monthly, using internally developed behavioural models. A regional house price index is used to reflect any changes in the value of collateral (see below). This process is also used to determine the amount of capital which is required to be held for individual loans.

Mortgages originated prior to 2009, by Platform or acquired by Britannia, are managed as part of a closed portfolio, Optimum. These loans include a range of asset types, including prime residential (both income verified and self-certified), buy-to-let, and non-conforming mortgages.

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

The table below shows gross customer balances for residential mortgages analysed by current LTV banding and repayment method:

	30 June 2014				
	Retail secured		Optimum		
	Interest only	Other	Interest only	Other	Total
Less than 50%	**1,166.2**	**4,713.7**	**267.2**	**311.3**	**6,458.4**
50% to 60%	**570.1**	**1,785.8**	**333.4**	**206.4**	**2,895.7**
60% to 70%	**694.5**	**2,019.1**	**688.2**	**254.5**	**3,656.3**
70% to 80%	**312.9**	**1,893.5**	**1,023.5**	**267.5**	**3,497.4**
80% to 90%	**155.3**	**606.0**	**1,220.3**	**222.5**	**2,204.1**
90% to 100%	**92.5**	**104.5**	**1,080.7**	**105.7**	**1,383.4**
Greater than 100%	**64.6**	**35.5**	**738.4**	**30.7**	**869.2**
	3,056.1	**11,158.1**	**5,351.7**	**1,398.6**	**20,964.5**

	31 December 2013				
	Retail secured		Optimum		
	Interest only	Other	Interest only	Other	Total
Less than 50%	1,211.0	4,656.3	241.3	291.8	6,400.4
50% to 60%	559.1	1,841.4	268.1	194.9	2,863.5
60% to 70%	855.5	2,151.9	584.7	248.8	3,840.9
70% to 80%	426.9	2,096.8	1,019.4	278.9	3,822.0
80% to 90%	173.7	1,104.2	1,199.1	263.2	2,740.2
90% to 100%	115.1	160.6	1,222.7	149.8	1,648.2
Greater than 100%	95.7	72.8	993.3	60.2	1,222.0
	3,437.0	12,084.0	5,528.6	1,487.6	22,537.2

Interest only balances are contractually due to mature as shown below:

	30 June 2014					
	< 1 year	1 – 5 years	5 – 10 years	10 – 20 years	20+ years	Total
Retail Secured	**102.1**	**371.6**	**570.0**	**1,516.3**	**496.1**	**3,056.1**
Optimum	**27.9**	**341.9**	**626.1**	**4,108.1**	**247.7**	**5,351.7**
	130.0	**713.5**	**1,196.1**	**5,624.4**	**743.8**	**8,407.8**

	31 December 2013					
	< 1 year	1 – 5 years	5 – 10 years	10 – 20 years	20+ years	Total
Retail Secured	97.0	391.0	608.5	1,717.5	623.0	3,437.0
Optimum	17.9	346.4	616.8	4,260.6	286.9	5,528.6
	114.9	737.4	1,225.3	5,978.1	909.9	8,965.6

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

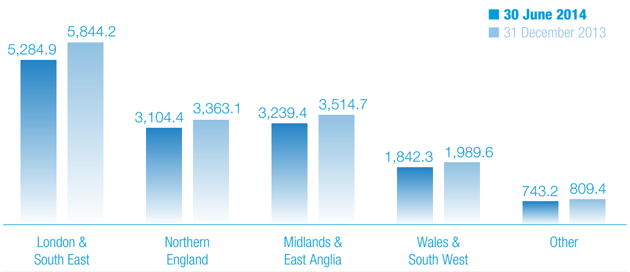
The table below shows gross customer balances for residential mortgages analysed by asset class, the LTV shown is the current average percentage:

	30 June 2014					
	Retail secured			**Optimum**		
	Gross customer balance	**Average LTV %**	**Interest only %**	**Gross customer balance**	**Average LTV %**	**Interest only %**
Prime residential	**13,210.6**	**39.5**	**16.8**	**603.9**	**72.9**	**74.4**
Buy-to-let	**876.5**	**57.2**	**87.4**	**1,970.1**	**72.7**	**92.5**
Self-certified	**77.6**	**39.2**	**77.3**	**1,789.5**	**70.6**	**79.1**
Almost prime	**47.7**	**48.7**	**29.2**	**801.4**	**85.2**	**71.8**
Non-conforming	**1.9**	**60.9**	**53.0**	**1,585.4**	**70.2**	**68.7**
	14,214.3	**40.4**	**21.5**	**6,750.3**	**73.0**	**79.3**

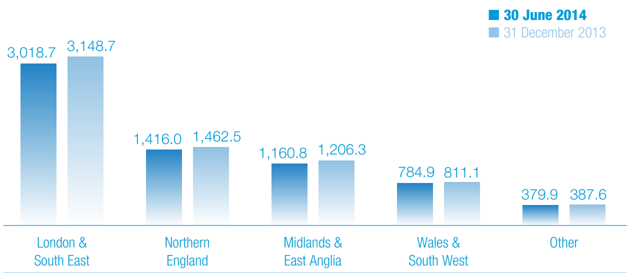
	31 December 2013					
	Retail secured			Optimum		
	Gross customer balance	Average LTV %	Interest only %	Gross customer balance	Average LTV %	Interest only %
Prime residential	14,349.9	41.4	17.1	640.5	74.5	74.1
Buy-to-let	1,032.2	59.0	87.9	2,041.6	75.1	92.2
Self-certified	82.4	41.3	77.0	1,867.1	73.2	78.6
Almost prime	54.3	51.0	30.1	824.6	88.1	71.2
Non-conforming	2.2	63.2	60.5	1,642.4	72.5	68.0
	15,521.0	42.3	22.1	7,016.2	75.3	78.8

The charts below show gross customer balances analysed by geographical location:

Retail secured



Optimum



All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

Collateral

Mortgages are secured by a first charge over the property being purchased or remortgaged. Valuation of the property is normally assessed by a Royal Institution of Chartered Surveyors (RICS) certified surveyor from the Bank's approved panel. Valuations may also be assessed through the use of an automated valuation model (AVM).

It is normal practice for the Bank to reassess the valuation of collateral for the non-default book on a quarterly basis using a regional property price index. The table below analyses the indexed value of property collateral held against mortgage portfolios:

	30 June 2014					
	Retail Secured			**Optimum**		
	Gross customer balance	**Collateral**	**Cover %**	**Gross customer balance**	**Collateral**	**Cover %**
Impaired	**151.3**	**150.8**	**99.7**	**999.9**	**978.6**	**97.9**
Not impaired	**14,063.0**	**14,052.7**	**99.9**	**5,750.4**	**5,713.2**	**99.4**
	14,214.3	**14,203.5**	**99.9**	**6,750.3**	**6,691.8**	**99.1**

	31 December 2013					
	Retail Secured			Optimum		
	Gross customer balance	Collateral	Cover %	Gross customer balance	Collateral	Cover %
Impaired	149.0	148.3	99.5	1,095.9	1,062.5	97.0
Not impaired	15,372.0	15,356.1	99.9	5,920.3	5,866.2	99.1
	15,521.0	15,504.4	99.9	7,016.2	6,928.7	98.8

In the table, collateral is constrained to a maximum of 100% of the exposure to each customer to correctly reflect the maximum protection available to the Bank.

Impairment

The table shown below reports coverage ratios calculated using:

- Carrying values in the accounts; and
- Impaired balances defined as one payment past due or in default (6+ months past due, possession, litigation, bankruptcy or Law of Property Act (LPA) receiver appointed).

	30 June 2014		31 December 2013	
	Retail secured	**Optimum**	Retail secured	Optimum
Gross loans and advances	**14,210.0**	**6,661.1**	15,524.6	6,922.1
of which impaired	**147.5**	**915.6**	145.0	1,003.3
Impaired as a % of gross loans and advances	**1.0%**	**13.7%**	0.9%	14.5%
Allowance for losses	**4.8**	**24.1**	4.5	35.5
Coverage	**3.3%**	**2.6%**	3.1%	3.5%

The movement in Optimum impairment provisions in the period to 30 June 2014 was driven by updated experience of the credit risk impairment policy, primarily reflecting an updated view of the shortfall required in the determination of Loss Given Default.

The Bank manages recovery of customer arrears on a gross customer balance basis (excluding credit fair value adjustments and other accounting entries). Gross loans and advances to customers comprise mortgages that were acquired by the Bank at discounts to the amounts that were advanced to the mortgagors (including the whole of the Optimum portfolio), and mortgages that were originated by the Bank.

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

In order to aid comparability with its peers, for internal management reporting purposes the Bank also calculates allowance for losses on the basis of amounts originally advanced to mortgagors, regardless of whether the Bank acquired or originated these mortgages. On this basis the retail secured allowance for losses is £8.6m (2013: £8.7m) and the coverage ratio is 5.8% (2013: 5.8%) and the Optimum allowance for losses is £107.5m (2013: £127.8m) and the coverage ratio is 10.8% (2013: 11.7%).

The Bank has refined its approach to include a calculation of coverage ratios by reference to 90+ days past due and default balances. On this new basis:

- The retail 90+ days past due and default balance is £48.5m (2013: £53.1m), 0.3% of total customer balances (2013: 0.3%) and the coverage ratio is 17.7% (2013: 16.4%); and
- The Optimum 90+ days past due and default balance is £533.5m (2013: £579.9m), 7.9% of total customer balances (2013: 8.3%) and the coverage ratio is 20.3% (2013: 22.0%).

The movements in impaired customer balances during the year are shown below:

	30 June 2014	
	Retail secured	**Optimum**
Balance at start of year	**149.0**	**1,095.9**
Classified as impaired during the year	**50.1**	**200.4**
Transferred to unimpaired during year	**(31.2)**	**(226.7)**
Net repayments and other	**(16.6)**	**(69.7)**
Balance at the end of year	**151.3**	**999.9**

The table below shows the credit quality of customer balances that are not impaired:

	30 June 2014			31 December 2013		
	Retail secured	**Optimum**	**Total**	Retail secured	Optimum	Total
Low to medium risk	**13,798.7**	**4,303.2**	**18,101.9**	15,084.5	4,438.2	19,522.7
Medium to high risk	**264.3**	**1,447.2**	**1,711.5**	287.5	1,482.1	1,769.6
	14,063.0	**5,750.4**	**19,813.4**	15,372.0	5,920.3	21,292.3

Low to medium risk is defined as exposures with a probability of default (PD) in the next year of 1% or below. Medium to high risk is defined as exposures with a PD in the next year of greater than 1%. All PDs are calculated using the internal ratings based (IRB) approach under Basel III.

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

Forbearance

Forbearance occurs when, for reasons relating to actual or apparent financial difficulty of the borrower, a temporary or permanent concession is granted. A concession may involve short term restructuring of the payment terms of the loan or an extension of the maturity date.

The table below analyses secured residential mortgage balances by type of forbearance and the associated gross impairment coverage (including credit fair value adjustments).

	30 June 2014				31 December 2013			
Optimum	Neither past due nor impaired	Impaired	Loans subject to forbearance	Impairment coverage	Neither past due nor impaired	Impaired	Loans subject to forbearance	Impairment coverage
Concessions	11.4	14.7	26.1	(0.7)	8.9	21.6	30.5	(1.0)
Arrangements	70.9	151.7	222.6	(10.3)	91.8	194.3	286.1	(13.9)
Term extensions	16.5	0.3	16.8	(0.2)	19.7	0.2	19.9	(0.2)
Assisted Voluntary Sale	–	0.7	0.7	(0.1)	–	–	–	–
Interest only switches	5.4	1.8	7.2	(0.2)	7.7	2.4	10.1	(0.3)
Capitalisations	0.1	0.1	0.2	–	0.4	–	0.4	–
	104.3	169.3	273.6	(11.5)	128.5	218.5	347.0	(15.4)

	30 June 2014				31 December 2013			
Retail secured	Neither past due nor impaired	Impaired	Loans subject to forbearance	Impairment coverage	Neither past due nor impaired	Impaired	Loans subject to forbearance	Impairment coverage
Concessions	6.3	7.4	13.7	(0.1)	5.1	8.3	13.4	(0.2)
Arrangements	19.8	24.5	44.3	(0.5)	43.3	38.9	82.2	(0.7)
Term extensions	238.5	0.8	239.3	(1.0)	335.9	1.0	336.9	(1.2)
Assisted Voluntary Sale	–	0.3	0.3	–	–	–	–	–
Interest only switches	15.0	1.1	16.1	(0.4)	31.2	1.2	32.4	(0.4)
Capitalisations	0.3	–	0.3	–	0.3	–	0.3	–
	279.9	34.1	314.0	(2.0)	415.8	49.4	465.2	(2.5)

The reduction in the level of forborne balances between December 2013 and June 2014 reflects adoption of the Bank's latest forbearance policy.

The table has been re-presented to reflect reporting consistent with the Bank's forbearance policy. The forbearance policy distinguishes between payments received through forbearance activity and those where a court order has been obtained, with court orders excluded from this re-statement. Secondly, accounts subject to forbearance are reported as forborne for a minimum duration of 12 months.

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

Unsecured retail credit risk

Acquisition and account management

The Bank offers unsecured lending through loans, credit cards and overdrafts. Customers' applications for credit are assessed using a combination of credit scoring and policy rules. Credit cards and overdrafts are subject to ongoing account management to determine any increase or decrease in credit limit that should apply as well as to manage over limit authorisations.

The portfolio risk is reassessed monthly using behavioural scorecards to determine the amount of capital required to be held for individual exposures.

The following table shows unsecured lending gross customer balances (including undrawn commitments) by product type:

	30 June 2014	31 December 2013
Loans	**499.1**	570.8
Professional and career development loans	**82.9**	82.5
Credit cards	**2,467.4**	2,532.4
Overdrafts	**337.8**	355.0
	3,387.2	3,540.7

Impairment

Coverage ratios calculated using carrying values in the accounts are shown in the table below:

	30 June 2014	31 December 2013
Gross loans and advances	**1,243.1**	1,294.6
of which impaired	**241.9**	216.9
Impaired as a % of gross loans and advances	**19.5%**	16.8%
Allowance for losses	**189.4**	160.2
Coverage	**78.3%**	73.9%

The movement in unsecured impairment provisions in the period to 30 June 2014 was driven by updated experience of the credit risk impairment policy, primarily reflecting realisation of extended recovery periods in the determination of Loss Given Default.

The Bank now includes balances sent to debt collection agencies in gross loans and advances, impaired balances and allowance for losses. The 2013 comparison has not been represented but would result in a coverage ratio of 82.1%.

Forbearance

A number of forbearance options, including concessionary arrangements, are available to borrowers in financial difficulty. These are handled either with customers directly or through a third party whom they have chosen to represent them. Accounts classified as forborne remain so until the period of financial difficulty has passed and the account has demonstrated it can operate under sustainable terms.

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

Corporate credit risk

Acquisition and account management

The Bank operates to a lending policy which is subject to meeting criteria as laid down in the corresponding sector strategy guidelines and strict policy with regards to single name and sector concentrations.

The tables below show the distribution of the BaCB and CoAM gross customer balances (including commitments) by sector and risk grade, where PD grades have been mapped to regulatory slotting categories for ease of interpretation in this report.

30 June 2014	Standardised	Strong	Good	Satisfactory	Weak	Default	Total
BaCB							
Accommodation, food and licensed services	12.9	7.6	19.0	4.6	–	–	44.1
Care	14.2	14.2	24.4	0.5	–	–	53.3
Education	53.8	5.3	4.2	0.5	–	–	63.8
Financial services	11.2	25.9	17.0	0.8	–	0.2	55.1
Football clubs	–	–	–	–	–	–	–
Housing associations	2.1	31.8	0.8	–	–	–	34.7
Manufacturing	2.2	10.4	8.7	1.3	–	–	22.6
Motor trade and garages	1.0	4.6	3.2	–	–	–	8.8
PFI	–	–	–	–	–	–	–
Professional services	14.9	9.8	3.0	0.5	–	0.2	28.4
Property and construction:							
Commercial investment	3.8	8.7	182.0	1.9	–	1.9	198.3
Residential investment	2.0	0.1	46.9	0.1	–	–	49.1
Commercial development	–	0.1	11.4	–	–	–	11.5
Residential development	0.7	–	7.3	–	–	–	8.0
Public sector entities	0.2	–	–	–	–	–	0.2
Renewable energy	–	–	–	–	–	–	–
Retail and wholesale trade	1.5	78.4	7.7	166.2	–	–	253.8
Services	81.9	16.7	23.1	2.6	0.3	0.3	124.9
Transport, storage and communication	1.8	6.5	1.3	–	–	–	9.6
Utilities	0.1	1.1	0.3	–	–	–	1.5
Business banking	0.4	39.8	6.0	2.6	0.6	0.2	49.6
Other	3.9	1.2	–	0.3	–	–	5.4
	208.6	262.2	366.3	181.9	0.9	2.8	1,022.7

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

30 June 2014	Standardised	Strong	Good	Satisfactory	Weak	Default	Total
Corporate CoAM							
Accommodation, food and licensed services	89.6	21.6	59.4	22.2	14.4	186.7	393.9
Care	114.0	6.4	10.6	31.0	2.3	28.8	193.1
Education	27.4	14.6	–	0.6	–	0.1	42.7
Financial services	6.6	30.8	8.4	1.8	–	2.8	50.4
Football clubs	–	22.2	–	0.4	0.1	15.8	38.5
Housing associations	5.2	967.5	0.9	–	–	–	973.6
Manufacturing	4.9	6.1	8.4	2.3	0.1	0.6	22.4
Motor trade and garages	–	11.2	14.9	0.8	0.6	6.7	34.2
PFI	–	68.7	1,081.1	–	20.0	12.9	1,182.7
Professional services	19.8	4.9	11.3	6.4	–	1.7	44.1
Property and construction:							
Commercial investment	25.0	20.9	562.8	105.5	51.7	887.8	1,653.7
Residential investment	4.2	–	54.6	44.4	20.7	104.6	228.5
Commercial development	44.2	1.0	73.8	36.3	5.4	78.5	239.2
Residential development	3.9	–	12.1	4.6	2.2	10.2	33.0
Public sector entities	152.6	0.3	–	–	–	–	152.9
Renewable energy	513.6	–	–	–	–	11.8	525.4
Retail and wholesale trade	4.4	6.1	8.8	3.5	1.0	8.2	32.0
Services	93.2	45.9	10.2	11.3	0.2	28.5	189.3
Transport, storage and communication	2.9	3.4	0.6	5.1	–	13.9	25.9
Utilities	15.2	–	2.5	0.1	–	1.4	19.2
Business banking	–	–	–	–	–	0.4	0.4
Other	0.6	0.2	0.5	1.4	–	0.1	2.8
	1,127.3	1,231.8	1,920.9	277.7	118.7	1,401.5	6,077.9
Total exposure	1,335.9	1,494.0	2,287.2	459.6	119.6	1,404.3	7,100.6

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

31 December 2013	Standardised	Strong	Good	Satisfactory	Weak	Default	Total
BaCB							
Accommodation, food and licensed services	14.8	11.1	18.2	4.9	–	–	49.0
Care	20.3	12.4	26.5	0.5	–	–	59.7
Education	45.9	15.0	5.0	–	–	–	65.9
Financial services	11.5	25.6	20.0	0.8	–	0.2	58.1
Football clubs	–	–	–	–	–	–	–
Housing associations	2.2	33.6	0.8	–	–	–	36.6
Manufacturing	4.3	8.0	13.7	1.8	–	0.4	28.2
Motor trade and garages	1.5	3.8	5.2	–	–	–	10.5
PFI	–	–	–	–	–	–	–
Professional services	21.1	9.9	5.0	0.1	–	0.3	36.4
Property and construction:							
Commercial investment	6.0	9.8	226.6	0.3	–	0.1	242.8
Residential investment	2.9	0.6	55.9	–	–	–	59.4
Commercial development	0.3	0.5	14.3	–	–	–	15.1
Residential development	0.7	1.2	11.3	–	–	–	13.2
Public sector entities	3.6	–	–	–	–	–	3.6
Renewable energy	–	–	–	–	–	–	–
Retail and wholesale trade	2.3	307.8	9.3	0.2	–	–	319.6
Services	98.6	18.3	23.4	1.8	–	0.3	142.4
Transport, storage and communication	1.9	6.6	3.1	0.2	–	–	11.8
Utilities	0.1	1.5	0.3	–	–	–	1.9
Business banking	0.9	40.1	7.4	3.0	0.6	0.1	52.1
Other	5.0	1.9	0.7	–	–	–	7.6
	243.9	507.7	446.7	13.6	0.6	1.4	1,213.9

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

31 December 2013	Standardised	Strong	Good	Satisfactory	Weak	Default	Total
Corporate CoAM							
Accommodation, food and licensed services	113.7	82.4	107.7	26.1	16.2	221.8	567.9
Care	112.8	1.1	16.8	31.7	2.4	31.6	196.4
Education	29.1	17.9	–	0.6	–	0.1	47.7
Financial services	52.6	33.0	6.2	3.8	–	4.4	100.0
Football clubs	–	32.2	–	0.4	0.1	15.9	48.6
Housing associations	5.3	1,063.0	0.9	–	–	–	1,069.2
Manufacturing	17.9	9.8	6.5	16.0	0.1	6.6	56.9
Motor trade and garages	–	53.7	16.4	1.7	0.7	7.2	79.7
PFI	–	32.4	1,122.3	–	33.4	–	1,188.1
Professional services	35.6	5.5	11.5	10.0	0.2	2.0	64.8
Property and construction:							
Commercial investment	31.1	75.5	722.6	141.8	27.7	1,190.3	2,189.0
Residential investment	3.3	0.1	83.1	54.6	25.6	127.4	294.1
Commercial development	44.0	4.1	107.0	44.9	1.1	79.7	280.8
Residential development	4.9	–	42.3	11.3	2.2	9.0	69.7
Public sector entities	174.2	0.3	–	–	–	–	174.5
Renewable energy	566.9	–	–	–	–	11.2	578.1
Retail and wholesale trade	38.5	7.4	7.2	7.1	1.1	15.1	76.4
Services	109.1	74.0	18.8	21.2	0.5	29.6	253.2
Transport, storage and communication	15.3	3.4	0.6	6.7	–	6.3	32.3
Utilities	17.9	–	0.7	0.1	–	1.5	20.2
Business banking	–	–	–	–	–	0.4	0.4
Other	0.5	0.7	0.2	1.6	–	2.1	5.1
	1,372.7	1,496.5	2,270.8	379.6	111.3	1,762.2	7,393.1
Total exposure	1,616.6	2,004.2	2,717.5	393.2	111.9	1,763.6	8,607.0

The large increase in Satisfactory BaCB exposures since December 2013 is primarily due to the change in grading of one large connection. The reduction in Corporate CoAM exposures reflects the continuing deleveraging activity.

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

Collateral

Property valuations are obtained on first approval of the facility and revalued in accordance with our lending procedures.

The table below analyses the market value of the property collateral held against assets in the property and construction sectors:

	30 June 2014			31 December 2013		
	Exposure	**Collateral**	**Impairment provision**	Exposure	Collateral	Impairment provision
BaCB						
Non-default loans with ≤1 year until refinancing and all defaulted exposures regardless of term						
Less than 50%	**20.1**	**20.1**	**–**	25.4	25.4	–
50% to 60%	**8.8**	**8.8**	**–**	13.9	13.9	–
60% to 70%	**1.4**	**1.4**	**–**	5.4	5.4	–
70% to 80%	**0.9**	**0.9**	**–**	–	–	–
80% to 90%	**–**	**–**	**–**	0.1	0.1	–
90% to 100%	**0.6**	**0.6**	**–**	0.2	0.2	–
Greater than 100%	**–**	**–**	**–**	–	–	–
Unsecured	**1.0**	**–**	**–**	2.7	–	–
	32.8	**31.8**	**–**	47.7	45.0	–
Non-default loans with > 1 year until refinancing and all non-loan non-defaulted exposures regardless of term						
Less than 50%	**133.5**	**133.5**	**–**	139.3	139.3	–
50% to 60%	**60.7**	**60.7**	**–**	84.8	84.8	–
60% to 70%	**29.3**	**29.3**	**–**	48.4	48.4	–
70% to 80%	**1.2**	**1.2**	**–**	2.8	2.8	–
80% to 90%	**–**	**–**	**–**	1.2	1.2	–
90% to 100%	**3.5**	**3.5**	**–**	1.0	1.0	–
Greater than 100%	**4.2**	**4.0**	**–**	3.4	3.0	–
Unsecured	**2.1**	**–**	**–**	1.8	–	–
	234.5	**232.2**	**–**	282.7	280.5	–
	267.3	**264.0**	**–**	330.4	325.5	–

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

	30 June 2014			31 December 2013		
	Exposure	**Collateral**	**Impairment provision**	Exposure	Collateral	Impairment provision
Corporate CoAM						
Non-default loans with ≤1 year until refinancing and all defaulted exposures regardless of term						
Less than 50%	**44.1**	**42.8**	**1.3**	53.9	51.7	2.2
50% to 60%	**47.6**	**46.3**	**1.4**	90.9	69.1	21.7
60% to 70%	**34.7**	**34.2**	**0.5**	107.8	107.0	0.8
70% to 80%	**48.9**	**43.0**	**5.9**	135.0	130.6	4.5
80% to 90%	**85.8**	**65.1**	**20.8**	104.1	85.6	18.4
90% to 100%	**101.1**	**82.6**	**18.2**	48.2	34.8	13.4
Greater than 100%	**818.0**	**495.8**	**263.3**	1,155.0	687.4	452.9
Unsecured	**111.1**	**–**	**103.3**	73.6	–	60.5
	1,291.3	**809.8**	**414.7**	1,768.5	1,166.2	574.4
Non-default loans with > 1 year until refinancing and all non-loan non-defaulted exposures regardless of term						
Less than 50%	**132.8**	**132.8**	**–**	115.0	115.0	–
50% to 60%	**256.4**	**256.4**	**–**	283.7	283.7	–
60% to 70%	**303.6**	**303.6**	**–**	372.7	372.7	–
70% to 80%	**85.3**	**85.3**	**–**	137.9	137.9	–
80% to 90%	**19.0**	**19.0**	**–**	47.9	47.9	–
90% to 100%	**11.4**	**11.4**	**–**	22.0	22.0	–
Greater than 100%	**43.6**	**41.0**	**–**	55.2	19.9	–
Unsecured	**10.9**	**–**	**–**	30.7	–	–
	863.0	**849.5**	**–**	1,065.1	999.1	–
	2,154.3	**1,659.3**	**414.7**	2,833.6	2,165.3	574.4

In the table, collateral is constrained to a maximum of 100% of the exposure to each customer to correctly reflect the maximum protection available to the Bank.

There were two cases on 31 December 2013 in the 50-60% LTV band which have had significant impairment provisions applied against them. In one case the provision represented the loss of key rental income combined with swap break costs, in the other the anticipated final losses on completion of the sale of the property.

As at 30 June 2014, £14.0m (31 December 2013: £59.3m) of the above collateral are not held as first charge.

Impairment

Corporate customers are placed on a watchlist and treated as impaired when they show signs of unsatisfactory performance and require close monitoring.

The collective unidentified impairment provision (CUIP) provides cover for the performing portfolio using a formulaic approach based on default experience across the portfolio.

	30 June 2014		31 December 2013	
	BaCB	**CoAM**	BaCB	CoAM
Gross loans and advances	**802.0**	**5,493.0**	840.8	6,504.3
of which impaired	**177.7**	**1,636.5**	15.6	1,977.8
Impaired as a % of gross loans and advances	**22.1%**	**29.8%**	1.9%	30.4%
Individual allowance for losses	**0.9**	**504.1**	0.5	698.4
Impairment coverage (excluding collective provisions)	**0.5%**	**30.8%**	3.2%	35.3%
Collective allowance for losses	**6.1**	**26.9**	5.3	40.0

The increase in impaired loans in BaCB is due to one large connection being placed on a watchlist on 30 June 2014.

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

The Bank manages recovery of customer arrears on a gross customer balance basis (excluding credit fair value adjustments and other accounting entries). Gross loans and advances to customers comprise mortgages that were acquired by the Bank at discounts to the amounts that were advanced to the mortgagors, and mortgages that were originated by the Bank. In order to aid comparability with its peers, for internal management reporting purposes the Bank also calculates allowance for losses on the basis of amounts originally advanced to mortgagors, regardless of whether the Bank acquired or originated these mortgages. On this basis the BaCB allowance for losses is £0.9m (2013: £0.5m) and the coverage ratio is 0.5% (2013: 3.2%) and the CoAM allowance for losses is £597.4m (2013: £796.1m) and the coverage ratio is 34.5% (2013: 39.5%).

The movements in impaired customer balances during the year are shown below:

	30 June 2014		31 December 2013	
	BaCB	**CoAM**	BaCB	CoAM
Balance at start of year	**15.5**	**2,017.7**	8.4	2,447.6
Classified as impaired during the year	**187.3**	**146.9**	15.8	552.4
Transferred to unimpaired during year	**(3.7)**	**(28.0)**	(0.9)	(3.6)
Amounts written off	**(0.1)**	**(95.4)**	(0.4)	(246.2)
Net repayments, disposals (including asset sales) and other	**(9.2)**	**(322.1)**	(7.4)	(732.6)
Balance at the end of year	**189.8**	**1,719.1**	15.5	2,017.7

The large volume of new BaCB impaired balances is primarily due to one large connection being placed on a watchlist on 30 June 2014.

Forbearance

If the Bank is confident of a customer's ability and commitment to address their financial difficulties, it may agree to grant concessions to the original contractual terms. The table below analyses the exposures subject to forbearance:

	30 June 2014			31 December 2013		
	Forborne	**Non-forborne**	**Total**	Forborne	Non-forborne	Total
BaCB						
Default	**1.9**	**0.9**	**2.8**	–	1.4	1.4
On watchlist	**1.7**	**185.4**	**187.1**	8.8	5.5	14.3
Neither default nor on watchlist	**4.2**	**828.6**	**832.8**	1.9	1,196.3	1,198.2
	7.8	**1,014.9**	**1,022.7**	10.7	1,203.2	1,213.9
Corporate CoAM						
Default	**710.1**	**691.5**	**1,401.6**	936.5	825.7	1,762.2
On watchlist	**195.3**	**122.2**	**317.5**	116.2	204.8	321.0
Neither default nor on watchlist	**37.2**	**4,321.6**	**4,358.8**	16.3	5,293.6	5,309.9
	942.6	**5,135.3**	**6,077.9**	1,069.0	6,324.1	7,393.1
	950.4	**6,150.2**	**7,100.6**	1,079.7	7,527.3	8,607.0

Impairment provisions are recognised on accounts, which are in default and on the watchlist, subject to forbearance.

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

1.3.2 Investment securities

At the balance sheet date, the Bank has a total investment securities portfolio of £4,197.9m (31 December 2013: £4,499.4m) of which £nil (31 December 2013: £20m) is considered impaired and against which full provisions are held.

The following tables analyse the gross balance by impairment classification and type of investment security:

	Investment securities				
30 June 2014	**Loans and receivables**	**Available for sale**	**Fair value through income or expense**	**Held for trading**	**Total**
Analysis of balance per note 19					
Gross balance	**16.0**	**2,925.2**	**1,256.7**	**–**	**4,197.9**
Less: allowance for losses	**–**	**–**	**–**	**–**	**–**
	16.0	**2,925.2**	**1,256.7**	**–**	**4,197.9**
Analysis of credit risk exposure					
Not impaired	**16.0**	**2,925.2**	**1,256.7**	**–**	**4,197.9**
Impaired	**–**	**–**	**–**	**–**	**–**
Gross credit risk exposure	**16.0**	**2,925.2**	**1,256.7**	**–**	**4,197.9**
Less: allowance for losses	**–**	**–**	**–**	**–**	**–**
Net credit risk exposure	**16.0**	**2,925.2**	**1,256.7**	**–**	**4,197.9**

	Investment securities				
31 December 2013	Loans and receivables	Available for sale	Fair value through income or expense	Held for trading	Total
Analysis of balance per note 19					
Gross balance	23.6	2,752.4	1,743.4	–	4,519.4
Less: allowance for losses	–	(20.0)	–	–	(20.0)
	23.6	2,732.4	1,743.4	–	4,499.4
Analysis of credit risk exposure					
Not impaired	23.6	2,732.4	1,743.4	–	4,499.4
Impaired	–	20.0	–	–	20.0
Gross credit risk exposure	23.6	2,752.4	1,743.4	–	4,519.4
Less: allowance for losses	–	(20.0)	–	–	(20.0)
Net credit risk exposure	23.6	2,732.4	1,743.4	–	4,499.4

Fair value adjustments relating to expected credit losses on assets obtained on merger with Britannia Building Society in 2009 are no longer shown separately, instead they have been allocated against the relevant assets.

All amounts are stated in £m unless otherwise indicated

1. Credit risk continued

Collateral

Policies are in place with regard to the management and valuation of collateral. Repos and secured lending positions are revalued daily. Margin calls on collateralised swaps are made dependent on the counterparty. Eligible financial collateral for Basel III reporting purposes typically includes gilts held under reverse repo agreements and cash held under both repo agreements and collateralised swap arrangements. At the half year end and year end there were no gilts held under reverse repo agreements, but the Bank did hold some non-UK Sovereign Collateral.

Guarantees relied upon are either parental guarantees held against subsidiary exposures within bank groups or sovereign guarantees.

Impaired assets

Investment securities are considered past due where the contractual interest or principal payments are in arrears and it is determined that the Bank will be able to collect all principal and interest outstanding according to the contractual terms of the agreements.

Investment securities are considered impaired where it is determined that the Bank will be unable to collect all principal and interest outstanding, according to the contractual terms of the agreements.

At the balance sheet date, the Bank assesses its investment securities for objective evidence that an impairment loss has occurred. Particular consideration is given to evidence of any significant difficulty of the issuer or measurable decrease in the estimated cash flows from the investments.

Not impaired assets

The Bank only invests in treasury assets which comply with the credit risk policy and Treasury credit risk control standard. Within the Treasury investment security portfolio 100% (31 December 2013: 100%) of exposures have an external credit rating equivalent to Fitch A or above.

1.3.3 Loans and advances to banks

None of the Bank's exposures to loans and advances to banks are impaired. The Bank considers that its exposures to loans and advances to banks are all of low to medium risk.

Derivative financial instruments

The Bank enters into collateral agreements to mitigate credit risk from derivative counterparties. The majority of the Bank's collateral agreements are bi-lateral. None of the Bank's derivatives are cleared using a central clearing counterparty. Most derivatives that are subject to collateral agreements are collateralised using cash. Some derivatives linked to funding programmes can place government securities, cash, or other eligible securities as collateral as agreed by rating agencies and subject to ratings triggers.

Occasionally the Bank enters into unilateral agreements for certain derivatives; these are used for credit risk mitigation in securitisation structures.

	30 June 2014		31 December 2013	
	Derivative notional (net)	**Derivative fair value (net)**	Derivative notional (net)	Derivative fair value (net)
Interest rate				
Bi-lateral collateral agreements	**16,554.9**	**(275.8)**	15,327.9	(255.6)
One way collateral agreements	**3,977.0**	**12.6**	5,078.6	(11.0)
No collateral agreement	**1,274.4**	**100.3**	1,494.9	91.8
Foreign exchange				
Bi-lateral collateral agreements	**463.7**	**12.5**	651.3	6.1
One way collateral agreements	**1,328.0**	**110.9**	1,504.3	186.1
No collateral agreement	**84.8**	**0.5**	–	–
	23,682.8	**(39.0)**	24,057.0	17.4

The above table has been represented in order to separately identify one way collateral agreements.

1. Credit risk continued

1.4 Wholesale credit risk

The Bank remains a UK focused retail and commercial operation with limited sovereign exposures to Eurozone governments. Limits have been set to enable the management of Treasury credit risk concentrations. These limits are monitored along with related country limits with more granular limits to cover asset class, sector exposures and counterparty groups, to prevent unacceptable concentrations.

As at 30 June 2014 the Bank had a £297.0m (31 December 2013: £299m) gross exposure to the Government of Finland. It held no other material non-UK sovereign debt (31 December 2013: £nil).

1.4.1 Direct exposures

During the first six months of 2014, exposures to financial institutions in European countries were broadly consistent with the year end with a total gross exposure outstanding at 30 June 2014 of £116.7m (31 December 2013: £110.2m). After credit risk mitigation, the net exposure was £116.7m (31 December 2013: £110.2m).

Within the Treasury portfolio there are a number of risk mitigation techniques available including netting and collateralisation agreements. Other methods such as disposal and credit derivatives are used periodically to mitigate the credit risk associated with particular transactions.

Treasury operates a risk based approach which monitors counterparty limits and exposure via a credit risk register. Both the counterparties and assets held are monitored against a Board approved matrix of risk tolerance and associated indicators. The credit risk register is updated for rating actions, market events and financial results as they are announced which may influence a change in risk status and possible escalation requiring management actions and inclusion on the watchlist.

The Treasury risk team reviews the portfolio and watchlists monthly for appropriate risk status bandings and any associated management actions. As at 30 June 2014 there were no red (highest risk) Eurozone exposures outstanding (31 December 2013: £nil).

1.4.2 Indirect exposures

Treasury risk management monitoring extends beyond the direct risk incurred through counterparty trading to the underlying exposures which Treasury's counterparties may maintain on their own balance sheets. In analysing each counterparty's secondary exposure, we assess the vulnerability and impact on that counterparty should it suffer different degrees of losses.

Where secondary sovereign exposure or contagion risk is deemed to undermine the performance of the counterparty, remedial management actions are taken in respect of Treasury's counterparty limits and exposure.

All amounts are stated in £m unless otherwise indicated

2. Liquidity risk

The Bank faces inherent risks concerning liquidity, particularly if the availability of traditional sources of funding such as retail and corporate deposits and, to a lesser extent, wholesale funding (these being the principal sources of the Bank's funding) become limited and/or more expensive. This may result in an inability to operate in the ordinary course of business, and/or a failure to meet liquidity requirements, and/or may adversely impact the Bank's business and/or the implementation of its strategy.

In the period to 30 June 2014, the Bank increased its liquid asset ratio to 18.5% at the balance sheet date (31 December 2013: 16%). This liquid asset ratio improvement is due to a reduction in total assets, and an increase in primary liquidity. The Bank continues to proactively manage its liquidity position, above regulatory minima. From a management perspective, liquidity is monitored on a daily basis via a suite of liquidity risk metrics supported by cash flow forecasts and stress tested forecasts.

2.1 Liquidity framework

The Bank's liquidity Risk Management Framework comprises:

- a defined risk appetite, controls and governance in the Bank's liquidity management policies;
- articulation of how liquidity risk is identified, measured, monitored and managed in the Individual Liquidity Adequacy Assessment (ILAA) and procedures and governance in place to mitigate the risk;
- liquidity risk quantification and mitigation techniques and processes;
- management actions linked through to stress testing and liquidity planning models, enabling a method of mitigating the effects of a number of stress scenarios for varying periods of time and to ensure that the Bank operates within its agreed risk appetite parameters in all planning models; and
- a process to attribute the cost, benefit and risks of liquidity to specific business lines via the Bank's funds transfer pricing mechanism.

2.2 Liquidity risk

The Board's risk appetite for liquidity risk is defined in terms of:

- survival periods which measure the ability of liquid assets to support the Bank's activity over time under a number of stress scenarios;
- adherence to strategic liquidity risk measures; and
- compliance with all regulatory liquidity risk limits.

The stress tests encompass survival across various timescales and a range of adverse liquidity events, both firm specific and market wide, which endeavour to cover all aspects of the liquidity risk to which the Bank is exposed.

The strategic measures approved by the Board include:

- customer loan/deposit ratio 91% (31 December 2013: 95%) – the ratio of gross loans and advances to customers to total customer deposits;
- encumbrance ratio 26% (31 December 2013: 27%) – the ratio of encumbered assets divided by total assets;
- regulatory framework – Net Stable Funding ratio and Internal Liquidity Guidance; and
- internal liquidity stress tests – the survival period of the Bank under a range of stressed scenarios.

Liquid asset portfolios

The Bank calculated its total liquidity resources as at 30 June 2014 as £12,083.0m (31 December 2013: £11,193.4m). The table below analyses the Bank's liquidity portfolio by product and liquidity value. Primary liquidity is liquid assets that are eligible under BIPRU 12.7 and secondary liquidity is all other liquid assets (excluding non-buffer assets described below). The table below excludes self-issued retained securitisation notes of £1.5bn (31 December 2013: £0.8bn).

	30 June 2014	31 December 2013
Operational balances with central banks	**5,804.9**	5,076.3
Gilts	**974.2**	789.5
Central government and multilateral development bank bonds	**823.0**	1,112.2
Total primary liquidity	**7,602.1**	6,978.0
Total secondary liquidity	**4,480.9**	4,215.4
Total liquidity	**12,083.0**	11,193.4
Average balance	**11,862.0**	9,357.2

All amounts are stated in £m unless otherwise indicated

2. Liquidity risk continued

The Bank uses any combination of these asset pools to manage liquidity, with primary liquidity used predominantly for short term cash flow movements, while secondary liquidity is used for creating longer term or contingent liquidity. Regular realisation through repo transactions and outright sales provide assurance that these asset pools remain sufficiently liquid. The overall quantum of liquidity remained stable in the first half of 2014 supported by an injection of cash through equity issuance in May 2014. The secondary liquidity portfolio reflects own assets eligible for discounting at central banks, and has remained stable in the first half of 2014.

The Bank has focused its funding and liquidity strategy on the reduction of holding of investment grade bonds that were not eligible to be included in the liquid asset buffer. The remaining bonds are set out in the table below:

	30 June 2014	31 December 2013
Other public sector securities	**2.7**	2.8
Floating rate notes	**2.4**	2.5
Total non-buffer assets	**5.1**	5.3

Wholesale funding

The Bank uses wholesale funding to supplement retail and commercial deposits by raising longer term funds (over one year in duration) and to diversify the source of funds to support the business plan of the Bank. The Bank has a variety of long term wholesale funding sources outstanding, including securitisations, covered bond and Euro medium-term notes, as shown in the table below:

	30 June 2014	31 December 2013
Preference shares, PSBs, and subordinated debt	**206.7**	196.3
Secured funding	**3,706.3**	4,339.5
Repos	**1,496.2**	2,119.3
Market borrowing	**61.5**	56.6
MTNs	**850.9**	884.0
Total wholesale funding	**6,321.6**	7,595.7

The table does not include the Funding for Lending Scheme. The Bank accessed the Funding for Lending Scheme in the first half of 2013, drawing £900m of UK treasury bills. The UK treasury bills remain available to the Bank until March 2017.

The following table sets out the Bank's contractual wholesale funding by maturity.

	30 June 2014	31 December 2013
Repayable in less than 1 month	**678.5**	2,010.3
Repayable between 1 and 3 months	**1.0**	67.8
Repayable between 3 and 12 months	**1,232.4**	157.2
Repayable between 1 and 5 years	**996.7**	1,800.8
Repayable in more than 5 years	**3,413.0**	3,559.6
Total external funding	**6,321.6**	7,595.7

The credit rating downgrades by the rating agencies in 2013 have led to sub-investment grade ratings being applied to the Bank's senior debt, leading to a reduction in potential primary and secondary demand for such unsecured instruments.

The credit rating downgrades also resulted in the downgrade of the Bank's covered bond by both Fitch and Moody's. Moody's also placed all the notes within the Bank's securitisation programmes on review for downgrade in 2013 and subsequently in early 2014, in order to mitigate the effect of the Bank downgrades and comply with certain contractual obligations. In 2014 the Bank implemented third party back-up servicing and back-up cash management, and other changes to comply with the rating agency structured funding criteria. These implementations required the consent of note-holders, which was obtained through separate consent solicitations for each transaction. In February 2014, Moody's confirmed the current ratings of all securitisation programme notes (removing the review for downgrade statuses), with the exception of the Leek Finance Number Eighteen class Ca and Cc notes (which remained on review for downgrade due to the cross currency derivative counterparty this transaction maintains exposure to).

All amounts are stated in £m unless otherwise indicated

2. Liquidity risk continued

2.4 Liquidity gap

Details of contractual maturities for assets and liabilities underpin the management of liquidity risk. However, in order to reflect more accurately the expected behaviour of the Bank's assets and liabilities, measurement and modelling of the behavioural aspect of each is constructed.

Gross cash flows include interest and other revenue cash flows. The following table is an analysis of:

- gross undiscounted contractual cash flows of financial assets and liabilities held at the balance sheet date; and
- behavioural adjustments that reflect the actual behaviour of customers based on historic cash flow profiles over a period of ten years.

30 June 2014 Contractual cash flows	Carrying value	Gross nominal flow	Less than 1 month	1–3 months	3–12 months	1–5 years	Over 5 years
Assets							
Cash and balances at central banks	6,103.7	6,103.7	6,103.7	–	–	–	–
Loans and advances to banks	1,644.6	1,644.6	1,606.7	37.9	–	–	–
Loans and advances to customers	27,894.4	37,965.0	1,149.6	352.1	1,628.7	8,590.6	26,244.0
Investment securities							
Loans and receivables	16.0	18.1	–	7.0	0.1	1.1	9.9
Available for sale	2,925.2	3,246.3	100.5	108.0	138.2	1,560.7	1,338.9
Fair value through income or expense	1,256.7	1,333.8	1.5	10.4	42.0	1,255.9	24.0
Held for trading	–	–	–	–	–	–	–
Derivative financial instruments	440.5	358.1	4.8	9.4	29.2	60.0	254.7
Amounts owed by other Co-operative Group undertakings	–	–	–	–	–	–	–
Other assets	795.5	–	–	–	–	–	–
Total recognised assets	41,076.6	50,669.6	8,966.8	524.8	1,838.2	11,468.3	27,871.5
Liabilities							
Deposits by banks	2,136.3	2,069.6	1,108.8	35.2	732.4	193.2	–
Customer accounts	31,070.1	31,040.8	18,454.7	2,234.4	5,547.6	4,693.3	110.8
Customer accounts – capital bonds	388.9	316.6	8.7	22.3	169.0	116.6	–
Debt securities in issue	3,880.8	4,960.5	68.5	479.7	98.4	3,624.7	689.2
Derivative financial instruments	481.1	1,238.7	12.6	24.9	98.9	438.2	664.1
Other borrowed funds	196.3	427.9	5.7	–	17.0	96.6	308.6
Other liabilities	807.9	–	–	–	–	–	–
Total recognised liabilities	38,961.4	40,054.1	19,659.0	2,796.5	6,663.3	9,162.6	1,772.7
Unrecognised loan commitments	3,242.9	3,242.9	2,903.0	–	90.5	249.4	–
Total liabilities	42,204.3	43,297.0	22,562.0	2,796.5	6,753.8	9,412.0	1,772.7
Behavioural adjustments							
Loans and advances to customers	–	–	(397.4)	1,117.2	2,934.4	5,968.3	(9,622.5)
Customer accounts	–	–	17,229.4	1,331.2	1,982.6	(20,654.0)	110.8
Net cash flow – behavioural	–	7,372.6	3,236.8	176.7	1.4	(12,629.4)	16,587.1

All amounts are stated in £m unless otherwise indicated

2. Liquidity risk continued

31 December 2013 Contractual cash flows	Carrying value (as restated)	Gross nominal flow	Less than 1 month	1–3 months	3–12 months	1–5 years	Over 5 years
Assets							
Cash and balances at central banks	5,418.8	5,418.8	5,418.8	–	–	–	–
Loans and advances to banks	1,594.4	1,594.4	1,594.4	–	–	–	–
Loans and advances to customers	30,428.5	44,368.1	1,474.8	452.9	2,810.1	11,852.5	27,777.8
Investment securities							
Loans and receivables	23.6	28.4	7.0	0.1	0.1	2.9	18.3
Available for sale	2,732.4	3,137.3	67.9	137.0	101.9	1,092.4	1,738.1
Fair value through income or expense	1,743.4	1,890.1	6.6	13.7	198.4	1,637.0	34.4
Held for trading	–	–	–	–	–	–	–
Derivative financial instruments	555.8	265.8	2.0	7.7	26.7	23.7	205.7
Amounts owed by other Co-operative Group undertakings	–	–	–	–	–	–	–
Other assets	900.4	–	–	–	–	–	–
Total recognised assets	43,397.3	56,702.9	8,571.5	611.4	3,137.2	14,608.5	29,774.3
Liabilities							
Deposits by banks	2,757.5	2,991.9	1,833.0	41.2	153.3	964.4	–
Customer accounts	32,463.3	33,349.4	21,144.6	1,796.5	2,213.3	8,195.0	–
Customer accounts – capital bonds	538.1	536.4	10.2	94.7	146.4	285.1	–
Debt securities in issue	4,207.6	5,391.0	75.4	34.1	628.1	3,964.0	689.4
Derivative financial instruments	538.6	1,031.2	13.7	34.5	106.6	354.4	522.0
Other borrowed funds	196.3	433.6	–	5.7	17.0	91.0	319.9
Other liabilities	903.4	–	–	–	–	–	–
Total recognised liabilities	41,604.8	43,733.5	23,076.9	2,006.7	3,264.7	13,853.9	1,531.3
Unrecognised loan commitments	4,003.6	4,003.6	3,578.5	–	–	425.1	–
Total liabilities	45,608.4	47,737.1	26,655.4	2,006.7	3,264.7	14,279.0	1,531.3
Behavioural adjustments							
Loans and advances to customers	–	–	112.0	194.0	1,146.0	7,829.0	(9,281.0)
Customer accounts	–	–	20,901.0	(977.0)	(6,283.0)	(13,641.0)	–
Net cash flow – behavioural	–	8,965.8	2,929.1	(2,178.3)	(5,264.5)	(5,482.5)	18,962.0

2.5 Encumbrance

The Bank aims to have sufficient eligible and unencumbered assets available to meet the needs of its secured funding programmes. Details of the Bank's encumbered assets are shown in note 19.

All amounts are stated in £m unless otherwise indicated

3. Market risk

Market risk is the risk of loss as a result of the value of financial assets or liabilities (including off-balance sheet instruments) being adversely affected by movements in market rates or prices. This loss can be reflected in the near term earnings by changing net interest income, or in the longer term because of changes in the economic value of future cash flows.

The main source of market risk within the Bank is driven by mismatches between the repricing profiles of asset and liability customer products within the Retail, BaCB and CoAM businesses and certain characteristics embedded within these products and basis risk. Treasury also creates market risk through its various portfolio management activities along with currency risk.

3.1 Interest rate risk

The Bank's biggest exposure to market risk is from changes in interest rate risk. Interest rate risk policy statements specify the scope of the Bank's wholesale market activity, market risk limits and delegated authorities.

3.1.1 Non-treasury interest rate risk

Basis risk is the risk that different assets and liabilities re-price with reference to different indices and at different times. This exposes the Bank to income volatility if indices do not move in a ratio of one to one. The overall exposure to basis risk has remained a net base rate asset throughout the first half of 2014 as customers continue to favour variable rate mortgages (where the introductory rate is linked to Bank of England base rate) and a large proportion of the liquidity of the Bank is placed in the Bank of England reserve account. Basis risk is monitored by Bank Market Risk Forum (BMRF) and Asset-Liability Committee (ALCO) monthly and action is taken as required, which includes pricing, new products or external hedging.

The table below illustrates the greater than 12 month net gap position at the end of the period on the Bank's balances, excluding wholesale treasury and customer currency balances which are managed within the Treasury risk framework. The gap is driven by product pricing and product mix. The gap is calculated by placing all assets and liabilities at the earliest of their re-pricing or maturity date and then summing by time band. The aim is to have assets evenly spread so that the Bank is not exposed to sudden rate movements. The net position shows the amount that the Bank is either over or under invested at a point in time. A £100m positive gap position would equate to the Bank's income increasing by £1m per annum if rates increased by 1%. The maximum sensitivity for the period shown below equates to approximately a £14.7m (31 December 2013: £8.0m) decrease in income if rates increased by 1%.

Net greater than 12 month gap position	**30 June 2014**	31 December 2013
At the period end	**(1,095)**	(802)
Average for the period	**(1,185)**	(376)
Maximum sensitivity for the period	**(1,472)**	(802)
Minimum sensitivity for the period	**(931)**	(45)

3.1.2 Treasury interest rate risk

Treasury manages the Bank's liquid asset portfolios and executes derivative instruments with the wholesale markets on behalf of the Bank and its customers. Treasury operates a trading book, however currently there are no exposures as at 30 June 2014.

The Bank assesses the interest rate risk arising within the liquid asset portfolios via key measures; Value at Risk and PV01, with associated delegated limits. These are supplemented by additional controls such as maturity and stop loss limits.

3.1.2.1 Value at risk (VaR)

VaR measures the daily maximum potential gain or loss due to market volatility within a statistical confidence level of 99% with a ten-day holding period. The VaR methodology employed is an historical simulation using a time series of five year to latest day and was £18.6m at 30 June 2014 for the treasury portfolios.

A number of limitations should be considered in relation to the VaR model:

- Historic data is not necessarily a reliable predictor of future events;
- The model, by definition, does not capture potential losses outside the 99% confidence level, particularly those events that are extreme in nature; and
- VaR is based on exposures at close of business and, therefore, does not necessarily reflect intra-day exposures.

The outputs from the VaR model were reviewed in 2014 to ensure that they were consistent with methodology employed. The Bank does not have PRA VaR model permission and VaR is not used in regulatory reporting. The maturity method is used for reporting general interest rate risk for prudential reporting purposes.

3. Market risk continued

3.1.2.2 PV01

The Bank also employs PV01 which illustrates the change in valuation on a fixed income portfolio given a 1 basis point increase in rates. A negative PV01 figure relates to a net asset position and will create a loss if rates rise. A positive PV01 figure relates to a net liability position and will create a profit if rates rise. The effects of a 1 basis point increase in interest rates are £0.02m (31 December 2013: £0.01m) and a 1 basis point decrease £0.02m (31 December 2013: £0.01m).

3.1.3 Swap spread risk

The Bank is exposed to swap spread risk arising within the liquid asset portfolios whereby a proportion of assets are held in fixed rate government securities and are accompanied by a Libor linked product such as interest rate swaps or futures to hedge against changes in interest rates. However, there remains a risk associated with the possible movement in the spread between sovereign debt yields and swap rates and therefore creates market value volatility. For example the market value falls if the yield on the sovereign debt increases more than swap rates, as the market value loss on the sovereign debt will then be higher than the market value profit on the swap.

The risk is only crystallised if the sovereign debt and the associated swap are sold. The risk is controlled by PV01 and maturity limits.

3.2 Currency risk

The Bank's treasury foreign exchange activities primarily involve:

- Providing a service in meeting the foreign exchange requirements of customers;
- Maintaining liquidity in euros and US dollars by raising funds and investing these to generate a return; and
- Performing limited intra-day trading and overnight positioning in major currencies to generate incremental income.

For the period ended 30 June 2014 (unaudited)

All amounts are stated in £m unless otherwise indicated

3. Market risk continued

The table below provides an analysis of the Bank's assets and liabilities by currency:

	30 June 2014					31 December 2013 (as restated)				
	£	**$**	**€**	**Other**	**Total**	£	$	€	Other	Total (as restated)
Assets										
Cash and balances at central banks	**6,103.7**	**–**	**–**	**–**	**6,103.7**	5,418.8	–	–	–	5,418.8
Loans and advances to banks	**1,550.8**	**44.4**	**48.1**	**1.3**	**1,644.6**	1,520.6	28.3	42.9	2.6	1,594.4
Loans and advances to customers	**27,743.6**	**28.5**	**52.6**	**11.7**	**27,836.4**	30,225.8	28.9	54.8	12.7	30,322.2
Fair value adjustments for hedged risk	**58.0**	**–**	**–**	**–**	**58.0**	106.3	–	–	–	106.3
Investment securities										
Loans and receivables	**16.0**	**–**	**–**	**–**	**16.0**	23.6	–	–	–	23.6
Available for sale	**2,924.3**	**0.9**	**–**	**–**	**2,925.2**	2,732.4	–	–	–	2,732.4
At FV through income or expense	**1,256.7**	**–**	**–**	**–**	**1,256.7**	1,743.4	–	–	–	1,743.4
Held for trading	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–
Derivative financial instruments	**436.4**	**–**	**4.1**	**–**	**440.5**	515.4	–	40.4	–	555.8
Equity shares	**5.8**	**–**	**–**	**–**	**5.8**	5.8	–	–	–	5.8
Investments in joint ventures	**4.6**	**–**	**–**	**–**	**4.6**	4.7	–	–	–	4.7
Investment properties	**158.0**	**–**	**–**	**–**	**158.0**	164.1	–	–	–	164.1
Property, plant and equipment	**114.0**	**–**	**–**	**–**	**114.0**	115.2	–	–	–	115.2
Intangible fixed assets	**93.6**	**–**	**–**	**–**	**93.6**	110.7	–	–	–	110.7
Amounts owed by other Co-operative Group undertakings	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–
Other assets	**392.4**	**0.7**	**7.2**	**–**	**400.3**	478.9	–	2.0	–	480.9
Prepayments and accrued income	**16.0**	**–**	**–**	**–**	**16.0**	16.5	–	–	–	16.5
Current tax assets	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–
Deferred tax assets	**3.2**	**–**	**–**	**–**	**3.2**	2.5	–	–	–	2.5
Total assets	**40,877.1**	**74.5**	**112.0**	**13.0**	**41,076.6**	43,184.7	57.2	140.1	15.3	43,397.3
Liabilities										
Deposits by banks	**2,110.2**	**–**	**26.1**	**–**	**2,136.3**	2,730.0	–	27.5	–	2,757.5
Customer accounts	**31,022.6**	**19.2**	**26.3**	**2.0**	**31,070.1**	32,399.7	25.1	36.7	1.8	32,463.3
Customer accounts – capital bonds	**388.9**	**–**	**–**	**–**	**388.9**	538.1	–	–	–	538.1
Debt securities in issue	**3,876.7**	**–**	**4.1**	**–**	**3,880.8**	4,186.8	–	20.8	–	4,207.6
Derivative financial instruments	**481.1**	**–**	**–**	**–**	**481.1**	519.0	–	19.6	–	538.6
Other borrowed funds	**196.3**	**–**	**–**	**–**	**196.3**	196.3	–	–	–	196.3
Amounts owed to other Co-operative Group undertakings	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–
Other liabilities	**159.5**	**0.1**	**7.1**	**–**	**166.7**	200.9	–	2.0	–	202.9
Accruals and deferred income	**17.4**	**–**	**–**	**–**	**17.4**	54.1	–	–	–	54.1
Provisions for liabilities and charges	**544.8**	**–**	**–**	**–**	**544.8**	549.7	–	–	–	549.7
Current tax liabilities	**1.2**	**–**	**–**	**–**	**1.2**	4.2	–	–	–	4.2
Deferred tax liabilities	**77.8**	**–**	**–**	**–**	**77.8**	92.5	–	–	–	92.5
Total liabilities	**38,876.5**	**19.3**	**63.6**	**2.0**	**38,961.4**	41,471.3	25.1	106.6	1.8	41,604.8
Net on balance sheet position	**2,000.6**	**55.2**	**48.4**	**11.0**	**2,115.2**	1,713.4	32.1	33.5	13.5	1,792.5

At 30 June 2014, the Bank's open currency position was the equivalent of £0.8m (31 December 2013: £2.4m). The Bank manages its currency positions against both an overall limit and individual currency limits.

Capital management

For the period ended 30 June 2014 (unaudited)

All the amounts are stated in £m unless otherwise indicated

The Co-operative Banking Group injected £150m Common Equity Tier 1 into the Bank in the six months to June 2014. A further £163m is due to be paid by 31 December 2014.

A further £400m capital raising, before costs, was completed in May 2014. The reason for the additional capital raising was a result of the Bank identifying additional conduct and legal issues which together with significant cost and tax consequences of separation from the Co-operative Group, meant that the starting capital position for the Bank for the four to five year recovery period was weaker than in the plan announced in 2013.

- As at 30 June 2014 CRD IV fully-loaded CET1% has increased to 11.5% from 7.2%[1] as at 31 December 2013. This reflects an increase in CET1 of £513m and a decrease in risk weighted assets of £1.2bn.
- CRD IV fully-loaded leverage ratio has increased to 3.7% from 2.4% as at 31 December 2013.
- The Bank is not currently compliant with its Individual Capital Guidance (ICG), being the PRA's statement as to the regulatory capital it expects the Bank to hold, although the Bank does meet its Pillar 1 requirement.
- The current capital plan does not expect to achieve full compliance with the Capital Planning Buffer (CPB) at any time in the five year planning period, but sustainable ICG compliance is expected by the latter part of the planning period. Leverage ratio will be above 3.0% by the end of the planning period.

The Bank faces risks that may adversely impact the ability of the Bank to comply with its regulatory capital requirements, these include:

- Worsening economic and market conditions and/or increasing interest rates and/or a fall in house prices could result in the Non-core assets suffering from more than expected impairments which would adversely impact on the Bank's operating results and retained earnings;
- The Bank needs the ongoing forbearance of the PRA regarding its ICG deficit in accepting and moving forwards with its plan. To the extent this is not forthcoming or to the extent that the Bank does not perform in line with its Plan, additional capital may be required over and above that included in the Plan. This could also be the case if there are increases in regulatory capital requirements as a result of changes to international regulations (eg Basel III) or other changes to legislation or other market wide regulatory requirements or a change in regulatory risk appetite. The Plan assumes additional non-CET1 capital will be raised within the Plan period; and
- The inability of the Bank to deleverage its Non-core assets in a controlled and capital efficient manner may have a negative impact on the Bank's operating results and financial position and its regulatory capital position. In addition, any greater than expected costs or delays in deleveraging the Non-core assets may divert funding from and adversely impact the longer term development and growth of the Core business.

Reflecting the relatively depressed economic conditions, the Bank's risk appetite includes the requirement to hold sufficient capital to meet a mild downturn in activity such as is experienced once in every ten years; a '1-in-10' stress. The Bank submitted its most recent ICAAP in July 2014. When the ICAAP was prepared, based on 31 December 2013 data, the Bank forecast remaining above the 4.5% CET1 minimum requirement in a 1-in-10 stressed scenario and would be above 7% at the end of the forecast period. On the same December data, the Board also ran a more severe stress than its risk appetite, a 1-in-25 stress aligned to the PRA anchor stress. In this scenario, the Bank forecast it would fall below the 4.5% CET1 minimum requirement during the plan period. These tests did not include the financial results of the first half of 2014.

In the December 2013 PS7/13 Policy Statement the PRA announced that, with the exception of available-for-sale unrealised gains, CRD IV deductions and filters would be implemented in full from 1 January 2014 and there would be no transition to full implementation. All CRD IV disclosures above are shown on a transitional and fully loaded basis except for Leverage ratio which is only calculated on a fully loaded basis.

1 Following the restatement discussed in note 3 CET1 ratio would be 7.3% as at 31 December 2013. This restatement will be part of the regulatory capital calculation only once formally audited.

For the period ended 30 June 2014 (unaudited)

All the amounts are stated in £m unless otherwise indicated

Capital resources CRD IV

Capital resources CRD IV 2013/2014

	30 June 2014		31 December 2013	
	Year 1 CRD IV transitional rules	**CRD IV fully loaded rules**	Year 1 CRD IV transitional rules	CRD IV fully loaded rules
Common Equity Tier 1 Capital: instruments and reserves				
Permanent share capital and the related share premium account	**1,596.5**	**1,596.5**	1,059.3	1,059.3
Retained earnings	**380.4**	**380.4**	1,119.5	1,119.5
Available for sale and cash flow hedge reserves	**(1.1)**	**(1.1)**	0.8	0.8
Minority interest[3]	**6.9**	**12.1**	6.9	12.1
Independently reviewed interim profits net of any foreseeable charge or dividend	**–**	**–**	–	–
Common Equity Tier 1 (CET1) Capital before regulatory adjustments	**1,982.7**	**1,987.9**	2,186.5	2,191.7
Common Equity Tier 1 (CET1) Capital: regulatory adjustments				
Prudential valuation in trading book	**(2.0)**	**(2.0)**	(2.1)	(2.1)
Intangible assets (net of related tax liability)	**(93.6)**	**(93.6)**	(110.7)	(110.7)
Deferred tax assets not arising from temporary differences	**–**	**–**	–	–
Cash flow hedge reserves	**(8.7)**	**(8.7)**	(14.9)	(14.9)
Expected loss shortfall	**(230.5)**	**(230.5)**	(238.3)	(238.3)
Securitisation positions treated as deduction	**–**	**–**	–	–
Regulatory losses for the period[2]	**(53.1)**	**(53.1)**	(738.2)	(738.2)
Filter for unrealised gains on debt instruments held in the available for sale category	**–**	**–**	–	–
Unrealised gains or losses on available for sale assets (revaluation reserve)	**(2.0)**	**–**	(2.0)	–
Qualifying AT1 deductions that exceed AT1 Capital	**–**	**–**	–	–
Total regulatory adjustments to Common Equity Tier 1 (CET1)	**(389.9)**	**(387.9)**	(1,106.2)	(1,104.2)
Common Equity Tier 1 (CET1) Capital	**1,592.8**	**1,600.0**	1,080.3	1,087.5

For the period ended 30 June 2014 (unaudited)

All the amounts are stated in £m unless otherwise indicated

Capital resources CRD IV continued

	30 June 2014		31 December 2013[1]	
	Year 1 CRD IV transitional rules	**CRD IV fully loaded rules**	Year 1 CRD IV transitional rules	CRD IV fully loaded rules
Additional Tier 1 (AT1) Capital: instruments				
Perpetual non-cumulative preference shares	**–**	**–**	–	–
Minority interest[3]	**21.7**	**2.6**	21.7	2.6
Additional Tier 1 (AT1) Capital before regulatory adjustments	**21.7**	**2.6**	21.7	2.6
Additional Tier 1 (AT1) Capital: regulatory adjustments				
Intangible assets	**–**	**–**	–	–
Expected loss shortfall (half)	**–**	**–**	–	–
Total regulatory adjustments to Additional Tier 1 (AT1) Capital	**–**	**–**	–	–
AT1 adjustments in excess of AT1 Capital	**–**	**–**	–	–
Additional Tier 1 (AT1) Capital	**21.7**	**2.6**	21.7	2.6
Tier 1 Capital (T1 = CET1 + AT1)	**1,614.5**	**1,602.6**	1,102.0	1,090.1
Tier 2 (T2) Capital: instruments and provisions				
Capital instruments	**196.3**	**196.3**	196.3	196.3
Minority interest[3]	**0.9**	**3.5**	0.9	3.5
Credit risk adjustments	**64.4**	**64.4**	63.9	63.9
Tier 2 (T2) Capital before regulatory adjustments	**261.6**	**264.2**	261.1	263.7
Tier 2 (T2) Capital: regulatory adjustments				
Revaluation reserves	**2.0**	**–**	2.0	–
Total regulatory adjustments to Tier 2 (T2) Capital	**2.0**	**–**	2.0	–
Tier 2 (T2) Capital	**263.6**	**264.2**	263.1	263.7
Total Capital (TC = T1 + T2)	**1,878.1**	**1,866.8**	1,365.1	1,353.8

1 Following the full implementation of CRD IV reporting in 2014, the December 2013 capital resources have been reported in line with the Bank's 2014 CRD IV interpretation. The previously reported Tier 2 credit risk adjustment for 2013 has been revised to £63.9m. The total capital ratio for 2013 has correspondingly been revised from 8.6% to 9.0%, all other capital ratios are unchanged from that reported.

2 December 2013 retained earnings included in the regulatory capital position have not been amended for the restatement of FSCS levy and changes to hedge accounting. The overall change results in a decreased loss, and the change in position has not been audited, this will not be included in regulatory capital retained earnings until the 31 December 2014 results have been audited. In addition, in order to be consistent with profit recognition, other changes arising from the hedging restatement, including recognition of deferred tax assets and changes to the balance sheet, have not been reflected in the December 2013 capital position or leverage ratio. A reconciliation of statutory to regulatory loss for the period is included on page 48.

3 Regulatory retained earnings include the £410m capital redemption reserve created as a result of the Bank's Liability Management Exercise in 2013.

4 Minority interest represents the share of the capital and reserves of Unity Trust Bank that is attributable to third party investors. Under CRD IV the amount of minority interest which can be recognised by the Bank is reduced, and then allocated between the different tiers of capital.

For the period ended 30 June 2014 (unaudited)

All the amounts are stated in £m unless otherwise indicated

Reconciliation of equity per balance sheet to Common Equity Tier 1 capital

	30 June 2014		31 December 2013	
	Year 1 CRD IV transitional rules	**CRD IV fully loaded rules**	Year 1 CRD IV transitional rules	CRD IV fully loaded rules
Total equity per balance sheet	**2,115.2**	**2,115.2**	1,792.5	1,792.5
Loss for the period attributable to equity shareholders	**57.6**	**57.6**	739.2	739.2
Regulatory adjustments	**0.2**	**0.2**	(5.5)	(5.5)
Ordinary shares not recognised until cash consideration paid in 2014	**(163.0)**	**(163.0)**	(313.0)	(313.0)
Minority Interest	**(27.3)**	**(22.1)**	(26.7)	(21.5)
Retained earnings	**–**	**–**	–	–
Available for sale reserve	**–**	**–**	–	–
Cashflow hedging reserve	**–**	**–**	–	–
Common Equity Tier 1 (CET1) Capital before regulatory adjustments	**1,982.7**	**1,987.9**	2,186.5	2,191.7

A reconciliation of the statutory to regulatory loss for the period is included below. Further details on restatements can be found in note 3.

Reconciliation of statutory to regulatory loss for the period

	30 June 2014	31 December 2013
Statutory loss for the period	**(56.7)**	(738.3)
FSCS levy	**26.3**	(26.3)
Hedge accounting	**(16.6)**	16.6
Discounted cash flows for ordinary shares not recognised until cash consideration paid	**(6.1)**	9.8
Regulatory loss for the period	**(53.1)**	(738.2)

For the period ended 30 June 2014 (unaudited)

All the amounts are stated in £m unless otherwise indicated

Capital ratios and risk-weighted assets

	30 June 2014		31 December 2013	
	Year 1 CRD IV transitional rules	**CRD IV fully loaded rules**	Year 1 CRD IV transitional rules	CRD IV fully loaded rules
Capital ratios				
Common Equity Tier 1 ratio	**11.5%**	**11.5%**	7.2%	7.2%
Tier 1 ratio	**11.6%**	**11.5%**	7.3%	7.2%
Total Capital ratio	**13.5%**	**13.4%**	9.1%	9.0%
Risk-weighted assets				
Credit risk	**12,768.5**	**12,768.5**	13,818.5	13,818.5
Market risk	**0.8**	**0.8**	2.4	2.4
Operational risk	**1,131.8**	**1,131.8**	1,255.2	1,255.2
Total risk-weighted assets	**13,901.1**	**13,901.1**	15,076.1	15,076.1
Segmental analysis of credit risk risk-weighted assets				
Core				
Retail	**2,004.1**	**2,004.1**	2,268.1	2,268.1
BaCB	**1,019.7**	**1,019.7**	990.3	990.3
Treasury/other	**1,697.7**	**1,697.7**	1,989.2	1,989.2
	4,721.5	**4,721.5**	5,247.6	5,247.6
Non-core				
Corporate CoAM	**4,203.3**	**4,203.3**	4,758.0	4,758.0
Optimum	**3,687.7**	**3,687.7**	3,661.6	3,661.6
Illius	**156.0**	**156.0**	151.3	151.3
	8,047.0	**8,047.0**	8,570.9	8,570.9
Total credit risk risk-weighted assets	**12,768.5**	**12,768.5**	13,818.5	13,818.5

CET1% has increased to 11.5% from 7.2% as at 31 December 2013. This reflects an increase in CET1 of £513m and a decrease in risk-weighted assets of £1.2bn.

The increase in CET1 reflects:

£150.0m injection from the Co-operative Banking Group as part of the 2014 Commitment;

£10.1m increase in permanent share capital and £377.1m increase in share premium account relating to the £400m capital raising (net of £12.8m of associated costs);

£53.1m regulatory losses for the period; and

£17.1m reduction in intangibles.

The reduction in risk-weighted assets is primarily due to a £555m reduction in Corporate CoAM (Non-core) and a £264m reduction in Retail (Core). The change in Corporate CoAM is driven by ongoing asset sales and deleveraging activity of the Non-core business. The reduction in the Retail risk-weighted assets has been driven by the unsecured portfolios following a gradual decline in exposure across the 6 month period.

Risk-weighted assets in relation to BaCB (Core), Optimum (Non-core) and Illius (Non-core) have remained relatively flat since 2013 year end.

Operational risk risk-weighted assets have decreased by £123m following the annual recalculation of the Pillar 1 Operational Risk requirement following the 2013 year end results.

For the period ended 30 June 2014 (unaudited)

All the amounts are stated in £m unless otherwise indicated

CRD IV leverage ratio

	30 June 2014	31 December 2013
Tier 1 Capital	**1,602.6**	1,090.1
Total assets as per balance sheet	**41,076.6**	43,396.1
Less derivatives accounting value	**(440.5)**	(555.8)
Plus derivatives (Netting and PFE)	**420.3**	517.7
Less SFT accounting value	**–**	–
Plus SFT (Basel III netting and collateral)	**–**	–
Off-balance sheet using credit conversion factor	**2,082.9**	2,354.6
Less Regulatory adjustments to Tier 1 Capital	**(334.8)**	(366.0)
Regulatory leverage exposure	**42,804.5**	45,346.6
Leverage ratio	**3.7%**	2.4%

The leverage ratio has increased to 3.7% from 2.4% as at 31 December 2013. The leverage ratio is calculated as CRD IV Tier 1 capital divided by adjusted balance sheet exposures. The improvement in the ratio reflects a £513m increase in total Tier 1 capital and a £2.5bn decrease in regulatory leverage exposure reflecting the overall deleveraging strategy. The 30 June 2014 leverage ratio has been calculated using the Basel Committee January 2014 definition, with the 31 December 2013 leverage ratio remaining on a CRD IV basis. This is in line with guidance provided to the Bank by the PRA. The ratio has not been restated for the prior year adjustment as detailed in note 3.

Independent review report to The Co-operative Bank plc

Introduction

We have been engaged by the Bank to review the condensed set of financial statements in the Interim Financial Report for the six months ended 30 June 2014 which comprises the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of financial position, the consolidated statement of cash flows, the consolidated statement of changes in equity and the related explanatory notes 1 to 20. We have read the other information contained in the Interim Financial Report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Bank in accordance with guidance contained in International Standard on Review Engagements 2410 (UK and Ireland) 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank, for our work, for this report, or for the conclusions we have formed.

Directors' Responsibilities

The Interim Financial Report is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the Interim Financial Report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

As disclosed in note 1, the annual financial statements of the Bank are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this Interim Financial Report has been prepared in accordance with International Accounting Standard 34, 'Interim Financial Reporting', as adopted by the European Union.

Our Responsibility

Our responsibility is to express to the Bank a conclusion on the condensed set of financial statements in the Interim Financial Report based on our review.

Scope of Review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the Interim Financial Report for the six months ended 30 June 2014 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Emphasis of matter – Going concern

In forming our conclusion on the Interim Financial Report, which is not modified, we have considered the adequacy of the disclosure made in note 1.3 to the Interim Financial Report concerning the Bank's ability to continue as a going concern. The matters explained in note 1.3 to the Interim Financial Report, represent a material uncertainty which may cast significant doubt upon the Bank's ability to continue as a going concern. The condensed set of financial statements does not include the adjustments that would result if the Bank was unable to continue as a going concern.

Ernst & Young LLP
London, United Kingdom

Date: 21 August 2014

The Bank Interim Financial Report

The Bank income statement

For the period ended 30 June 2014 (unaudited)

All amounts are stated in £m unless otherwise indicated

	Notes	Period to 30 June 2014	Restated Period to 30 June 2013
Interest receivable and similar income	5	**566.3**	707.6
Provision for potential customer redress claims	5	**(25.0)**	(39.0)
		541.3	668.6
Interest expense and similar charges	5	**(363.4)**	(470.8)
Net interest income		**177.9**	197.8
Fee and commission income	6	**104.9**	116.2
Provision for potential customer redress claims	6	**(5.0)**	(94.0)
		99.9	22.2
Fee and commission expense	6	**(36.9)**	(36.2)
Net fee and commission income/(expense)		**63.0**	(14.0)
Net trading income		**0.2**	1.1
Other operating (costs)/income		**(1.6)**	25.6
Operating income		**239.5**	210.5
Operating expenses			
Operating expenses	7	**(401.9)**	(411.0)
Intangible asset impairment		**–**	(148.4)
Total operating expenses		**(401.9)**	(559.4)
Operating loss before impairment losses		**(162.4)**	(348.9)
Impairment gains/(losses) on loans and advances	10	**86.7**	(496.0)
Operating loss		**(75.7)**	(844.9)
Share of post tax (losses)/profits from joint ventures		**(0.1)**	0.3
Loss before taxation		**(75.8)**	(844.6)
Income tax	9	**19.1**	39.4
Loss for the financial period		**(56.7)**	(805.2)
Attributable to:			
Equity shareholders		**(57.6)**	(805.5)
Non-controlling interests		**0.9**	0.3
		(56.7)	(805.2)
Earnings per share (basic and fully diluted)		**(20.35)p**	(9.82)p

In total £38.6m (2013: £163.0m) of conduct and legal provisions have been incurred during the period. This includes £25.0m (2013: £39.0m) reported within interest receivable and similar income, £5.0m (2013: £94.0m) reported within fee and commission income and £8.6m (2013: £30.0m) reported within operating expenses, further details can be found in note 13.

The change in earnings per share (EPS) is largely due to the cancellation of 8.2bn ordinary shares as part of the Bank's Liability Management Exercise on 20 December 2013. Had the EPS been calculated based on the number of outstanding shares as at 30 June 2014, the EPS would have been (12.8)p (2013 restated: (178.4)p). This transaction was described in the 2013 Annual Report and Accounts and the effect on share capital can be seen in note 18.

Comparative figures for the period to 30 June 2013 have been restated as described in note 3.

The notes on pages 59 to 100 form part of these financial statements.

The Bank statement of comprehensive income

For the period ended 30 June 2014 (unaudited)

All amounts are stated in £m unless otherwise indicated

	Period from 1 Jan 2014 to 30 June 2014			Restated Period from 1 Jan 2013 to 30 June 2013		
	Equity shareholders	**Non-controlling interests**	**Total**	Equity shareholders	Non-controlling interests	Total
(Loss)/Profit for the period	**(57.6)**	**0.9**	**(56.7)**	(805.5)	0.3	(805.2)
Other comprehensive (expense)/income that may be recycled to profit and loss:						
Changes in cashflow hedges						
Net changes in fair value recognised directly in equity	**(6.6)**	**(0.3)**	**(6.9)**	(34.4)	(0.5)	(34.9)
Income tax	**0.4**	**–**	**0.4**	9.2	0.1	9.3
Transfers from equity to income or expense	**(5.3)**	**–**	**(5.3)**	(10.6)	–	(10.6)
Income tax	**(0.3)**	**–**	**(0.3)**	2.4	–	2.4
Changes in available for sale assets						
Net changes in fair value recognised directly in equity	**18.0**	**–**	**18.0**	(44.4)	–	(44.4)
Income tax	**(3.9)**	**–**	**(3.9)**	10.0	–	10.0
Transfers from equity to income or expense	**(12.4)**	**–**	**(12.4)**	13.4	–	13.4
Income tax	**2.7**	**–**	**2.7**	(3.1)	–	(3.1)
Other comprehensive (expense)/income for the period, net of income tax	**(7.4)**	**(0.3)**	**(7.7)**	(57.5)	(0.4)	(57.9)
Total comprehensive (expense)/income for the period	**(65.0)**	**0.6**	**(64.4)**	(863.0)	(0.1)	(863.1)

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

The notes on pages 59 to 100 form part of these financial statements.

The Bank statement of financial position

At 30 June 2014 (unaudited)

All amounts are stated in £m unless otherwise indicated

	Notes	30 June 2014	Restated 31 December 2013	Restated 31 December 2012
Assets				
Cash and balances at central banks		**6,103.7**	5,418.8	5,433.0
Loans and advances to banks		**1,644.6**	1,594.4	1,904.1
Loans and advances to customers	10a	**27,836.4**	30,322.2	33,339.5
Fair value adjustments for hedged risk	10b	**58.0**	106.3	354.2
Investment securities – loans and receivables	11a	**16.0**	23.6	295.0
Investment securities – available for sale	11b	**2,925.2**	2,732.4	3,789.4
Investment securities – fair value through income or expense	11c	**1,256.7**	1,743.4	1,845.2
Investment securities – held for trading		**–**	–	960.2
Derivative financial instruments		**440.5**	555.8	818.8
Equity shares		**5.8**	5.8	5.7
Investments in joint ventures		**4.6**	4.7	3.9
Investment properties		**158.0**	164.1	173.0
Property, plant and equipment		**114.0**	115.2	113.4
Intangible fixed assets		**93.6**	110.7	263.2
Amounts owed by other Co-operative Group undertakings		**–**	–	56.8
Other assets		**400.3**	480.9	70.3
Prepayments and accrued income		**16.0**	16.5	14.9
Current tax assets		**–**	–	172.6
Deferred tax assets	14	**3.2**	2.5	159.6
Total assets		**41,076.6**	43,397.3	49,772.8
Liabilities				
Deposits by banks		**2,136.3**	2,757.5	3,612.0
Customer accounts		**31,070.1**	32,463.3	35,884.4
Customer accounts – capital bonds	12	**388.9**	538.1	888.1
Debt securities in issue		**3,880.8**	4,207.6	4,716.2
Derivative financial instruments		**481.1**	538.6	967.6
Other borrowed funds		**196.3**	196.3	1,258.6
Amounts owed to other Co-operative Group undertakings		**–**	–	190.0
Other liabilities		**166.7**	202.9	104.0
Accruals and deferred income		**17.4**	54.1	20.1
Provisions for liabilities and charges	13	**544.8**	549.7	137.9
Current tax liabilities		**1.2**	4.2	–
Deferred tax liabilities	14	**77.8**	92.5	121.4
Total liabilities		**38,961.4**	41,604.8	47,900.3
Capital and reserves attributable to the Bank's equity holders				
Ordinary share capital	18	**22.6**	12.5	410.0
Share premium account	18	**1,736.9**	1,359.8	8.8
Retained earnings		**(87.4)**	(29.7)	1,323.2
Available for sale reserve		**(9.7)**	(14.1)	30.0
Capital redemption reserve		**410.0**	410.0	–
Cashflow hedging reserve		**8.6**	20.4	67.1
		2,081.0	1,758.9	1,839.1
Non-controlling interests		**34.2**	33.6	33.4
Total equity		**2,115.2**	1,792.5	1,872.5
Total liabilities and equity		**41,076.6**	43,397.3	49,772.8

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

Approved by the Board on 21 August 2014:

Richard Pym, Chair
Niall Booker, Chief Executive

The notes on pages 59 to 100 form part of these financial statements.

The Bank statement of cash flows

For the period ended 30 June 2014 (unaudited)

All amounts are stated in £m unless otherwise indicated

	30 June 2014	Restated 30 June 2013
Cash flows used in operating activities		
Loss before taxation	**(75.8)**	(844.6)
Adjustments for:		
Decrease in prepayments and accrued income	**0.5**	(7.7)
(Decrease)/increase in accruals and deferred income	**(36.7)**	23.9
Interest payable in respect of other borrowed funds	**11.3**	45.3
Effect of exchange rate movements	**(0.4)**	(12.8)
Fair value movement on investment properties	**5.9**	18.9
Impairment (gains)/losses on loans and advances	**(86.7)**	495.8
Movements on investment impairments	**(1.1)**	(19.0)
Depreciation and amortisation	**19.9**	20.8
Impairment of intangible fixed assets	**0.4**	2.0
Interest amortisation	**(3.3)**	(0.2)
Fair value movements and amortisation of investment securities	**(45.8)**	53.9
Impairment of property, plant and equipment	**7.0**	9.9
Loss on disposal of property, plant and equipment	**0.2**	–
Unwind of fair value adjustments arising on transfer of engagements	**47.1**	8.2
Preference dividend	**–**	2.8
	(157.5)	(202.8)
Decrease in deposits by banks	**(617.6)**	(94.2)
Decrease in customer accounts and capital bonds	**(1,566.6)**	(1,850.1)
Decrease in debt securities in issue	**(361.6)**	(136.1)
Decrease/(increase) in loans and advances to banks	**20.0**	(41.4)
Decrease in loans and advances to customers	**2,644.0**	291.2
Decrease in amounts owed by other Co-operative Group undertakings	**–**	239.9
Increase in amounts owed to other Co-operative Group undertakings	**–**	11.9
Net movement of other assets and other liabilities	**(88.7)**	(213.7)
Income tax received	**5.3**	16.4
Net cash flows used in operating activities	**(122.7)**	(1,978.9)
Cash flows from investing activities		
Purchase of tangible and intangible fixed assets	**(11.4)**	(0.5)
Proceeds from sale of property, plant and equipment	**2.4**	–
Proceeds from sale of investment property	**–**	1.3
Purchase of investment securities	**(1,112.2)**	(2,033.8)
Proceeds from sale and maturity of investment securities	**1,526.9**	3,875.2
Net cash flows from investing activities	**405.7**	1,842.2
Cash flows from/(used in) financing activities		
Interest paid on other borrowed funds	**(11.4)**	(44.3)
Dividends paid to non-controlling interests	**–**	(0.1)
Preference share dividends paid	**–**	(2.8)
Capital Commitment received from the Co-operative Group	**150.0**	–
Costs incurred relating to the May 2014 Capital Raising	**(12.8)**	–
Cash proceeds relating to the May 2014 Capital Raising	**400.0**	–
Net cash flows from/(used in) financing activities	**525.8**	(47.2)

The Bank statement of cash flows continued

For the period ended 30 June 2014 (unaudited)

All amounts are stated in £m unless otherwise indicated

	30 June 2014	Restated 30 June 2013
Increase/(decrease) in cash and cash equivalents	**808.8**	(183.9)
Cash and cash equivalents at the beginning of the period	**6,092.2**	6,314.2
Cash and cash equivalents at the end of the period	**6,901.0**	6,130.3
Cash and balances with central banks	**6,041.2**	5,331.7
Loans and advances to banks	**704.8**	673.6
Short term investments (note 11)	**155.0**	125.0
	6,901.0	6,130.3

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

Following the change in the ownership of the Bank, amounts owed to and by Co-operative Group undertakings are classified as at 30 June 2014 as third party balances.

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

The notes on pages 59 to 100 form part of these financial statements.

The Bank statement of changes in equity

For the period ended 30 June 2014 (unaudited)

All amounts are stated in £m unless otherwise indicated

	Attributable to equity holders of the Bank								
	Share capital	Share premium	Available for sale reserve	Cashflow hedging reserve	Capital redemption reserve	Retained earnings	Total	Non-controlling interest	Total equity
Period from 1 January 2014 to 30 June 2014									
Balance at the beginning of the period (as restated)	**12.5**	**1,359.8**	**(14.1)**	**20.4**	**410.0**	**(29.7)**	**1,758.9**	**33.6**	**1,792.5**
Total comprehensive (expense)/income for the period	**–**	**–**	**4.4**	**(11.8)**	**–**	**(57.6)**	**(65.0)**	**0.6**	**(64.4)**
Transactions with owners recorded directly in equity:									
Issuance of new share capital	**10.1**	**389.9**	**–**	**–**	**–**	**–**	**400.0**	**–**	**400.0**
Transaction costs	**–**	**(12.8)**	**–**	**–**	**–**	**–**	**(12.8)**	**–**	**(12.8)**
Dividend	**–**	**–**	**–**	**–**	**–**	**(0.1)**	**(0.1)**	**–**	**(0.1)**
Balance at the end of the period	**22.6**	**1,736.9**	**(9.7)**	**8.6**	**410.0**	**(87.4)**	**2,081.0**	**34.2**	**2,115.2**
Period from 1 July 2013 to 31 December 2013									
Balance at the beginning of the period (as restated)	410.0	8.8	5.9	33.7	–	517.7	976.1	33.2	1,009.3
Total comprehensive (expense)/income for the period	–	–	(20.0)	(13.3)	–	47.4	14.1	0.5	14.6
Transactions with owners recorded directly in equity:									
Liability Management Exercise									
Cancellation of share capital	(410.0)	–	–	–	410.0	–	–	–	–
Issuance of new share capital	12.5	777.5	–	–	–	–	790.0	–	790.0
Transfer of retained earnings to share premium	–	594.8	–	–	–	(594.8)	–	–	–
Transaction costs	–	(21.3)	–	–	–	–	(21.3)	–	(21.3)
Dividend	–	–	–	–	–	–	–	(0.1)	(0.1)
Balance at the end of the period (as restated)	12.5	1,359.8	(14.1)	20.4	410.0	(29.7)	1,758.9	33.6	1,792.5
Period from 1 January 2013 to 30 June 2013									
Balance at the beginning of the period (as restated)	410.0	8.8	30.0	67.1	–	1,323.2	1,839.1	33.4	1,872.5
Total comprehensive (expense)/income for the period (as restated)	–	–	(24.1)	(33.4)	–	(805.5)	(863.0)	(0.1)	(863.1)
Transactions with owners recorded directly in equity:									
Dividend	–	–	–	–	–	–	–	(0.1)	(0.1)
Balance at the end of the period (as restated)	410.0	8.8	5.9	33.7	–	517.7	976.1	33.2	1,009.3

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

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

The notes on pages 59 to 100 form part of these financial statements.

Notes to the Bank Interim Financial Report

For the period ended 30 June 2014 (unaudited)

All amounts are stated in £m unless otherwise indicated

1. Basis of preparation and significant accounting policies

1.1 Basis of preparation

This condensed consolidated Interim Financial Report for the half year ended 30 June 2014 has been prepared in accordance with the Disclosure and Transparency Rules of the Financial Conduct Authority and with IAS 34 'Interim Financial Reporting', as adopted by the European Union. The Interim Financial Report should be read in conjunction with the Bank's 2013 financial statements, which have been prepared in accordance with IFRS as adopted by the European Union.

The information contained within this report for the year ended 31 December 2013 does not constitute statutory accounts as defined by Section 434 of the Companies Act 2006. A copy of the statutory accounts for that year has been delivered to the Registrar of Companies. The auditor's report on those accounts was unqualified, did not contain a statement under section 498(2) or (3) of the Companies Act 2006, but did make reference to an emphasis of matter in relation to going concern (see note 1.3 for further detail).

The comparative information presented within the Interim Financial Report 2014 reflects the information disclosed within the Prospectus prepared to support the Liability Management Exercise dated 4 November 2013 (restated as explained in note 3) and not the information presented within the Interim Financial Report 2013.

The Interim Financial Report 2014 was approved by the Board of Directors on 21 August 2014.

1.2 Significant accounting policies

In the current period, the Bank has adopted IFRIC 21 – Levies, resulting in a prior period adjustment being made within the Interim Financial Report 2014 (see note 3). The following additional pronouncements were applicable in the current period but did not have a significant impact on the Bank:

- IFRS 10 Consolidated Financial Statements – Amendments for investment entities
- IFRS 11 Joint arrangements
- IFRS 12 Disclosure of Interests in Other Entities – Annual periods beginning on or after 1 January 2014
- IAS 27 Separate Financial Statements – Amendments for investment entities
- IAS 32 Financial Instruments: Presentation – Amendments relating to the offsetting of assets and liabilities
- IAS 36 Impairment of Assets – Amendments arising from Recoverable Amount Disclosures for Non-Financial Assets
- IAS 39 Financial Instruments: Recognition and Measurement – Amendments for novations of derivatives

Otherwise, with exception to the matters disclosed in note 3, the same accounting policies and presentation are followed in the interim financial statements 2014 as applied in the 2013 Annual Report and Accounts. Significant additions and changes to underlying methodologies are discussed within the critical judgements and estimates section.

An overview of pronouncements that will be relevant to the Bank in future periods is provided in the 2013 Annual Report and Accounts. The IASB has issued further pronouncements; however, the Bank does not expect adoption of any of the new guidance to have a significant impact on its results with the exception of IFRS 9 and IFRS 15.

IFRS 9 Financial Instruments was issued in July 2014 and supersedes IAS 39 Financial Instruments: Recognition and Measurement. The standard includes requirements for recognition and measurement, impairment, derecognition and general hedge accounting. Due to the short period of time which has elapsed since the issue of the standard, the Bank has not yet estimated the financial effects, although it is expected that IFRS 9 will have a significant impact for the Bank, in line with the wider industry. The standard is mandatory for periods beginning on or after 1 January 2018 but is available for early adoption subject to EU endorsement.

IFRS 15 Revenue From Contracts With Customers was issued in May 2014 and supersedes IAS 18 'Revenue', IAS 11 'Construction Contracts' and a number of revenue-related interpretations. Due to the short period of time which has elapsed since the issue of the standard, the Bank has not yet estimated the financial effects of the standard. The standard will be effective for annual reporting periods beginning on or after 1 January 2017 subject to EU endorsement.

1.3 Going concern

a. Introduction

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

The assessment of the appropriateness of using the going concern basis of accounting has been subject to a thorough process involving analysis and discussion by management, Executive and Board Committees and the Board, in line with our governance processes, and discussion with the PRA. This analysis included a particular focus on the 12 month period ending 31 August 2015. The forecasts included in the 2014-2018 Business Plan have been subjected to stressed scenarios which the Board considered to be reasonable and appropriate.

Following the capital shortfall identified in 2013, and the subsequent successful capital raising exercises, the Bank is now in the early stages of its Turnaround Plan (incorporated into the Business Plan discussed above). The completion of this Plan is expected to take 4-5 years and involves reshaping and restructuring the business as a core relationship bank.

1. Basis of preparation and significant accounting policies continued

The completion of the capital raising exercises removed major elements of uncertainty around the going concern status of the Bank. However, whilst important steps, these are not in themselves sufficient to recapitalise the Bank in the long term. There continue to be material uncertainties around the Bank's ability to continue as a going concern which relate to the implementation of the Turnaround Plan as discussed in (e) below. In particular, the Bank needs the ongoing forbearance of the PRA regarding its ICG deficit in accepting and moving forwards with its plan.

b. The Turnaround Plan–refocus on Core relationship banking proposition

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

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

c. Capital

In line with expectations, the Bank remains below the Individual Capital Guidance (ICG) for total capital set by the PRA and it is forecast to remain so for most of the duration of the 2014 – 2018 planning period. The PRA has reviewed and accepted the 2014-2018 Business Plan. The Bank needs the ongoing forbearance of the PRA regarding its ICG deficit in accepting and moving forwards with its plan.

Total CROIV capital resources as at 30 June 2014 are £1.6bn (31 December 2013: £1.1bn). The Bank's CET1 ratio stands at 11.5% (31 December 2013: 7.2%[1]) on a CROIV end point basis.

d. Liquidity

Since 31 December 2013, the liquid asset ratio has increased to 18.5% as at 30 June 2014 (31 December 2013: 16.0%). This liquid asset ratio improvement is due to a reduction in total assets, and an increase in primary liquidity. The Bank continues to maintain a liquidity position above regulatory minima.

During the period to 30 June 2014, the Bank has actively managed a reduction in customer deposits of £1.5bn with a reduction in customer assets of £2.5bn. Within the aggregate £1.5bn customer deposit reduction in the six months to 30 June 2014, Retail customer deposits decreased by £0.7bn

e. Risks and uncertainties

Key risks associated with successful execution of the Turnaround Plan include:

i) The Bank needs the ongoing forbearance of the PRA regarding its ICG deficit in accepting and moving forwards with its plan. To the extent this is not forthcoming or to the extent that the Bank does not perform in line with its 2014-2018 Business Plan or regulatory capital requirements are increased for any reason, additional CET1 capital may be required over and above that included in that plan in order for the Bank to remain a going concern, and the PRA could exercise its powers under the Banking Act of 2009;

ii) As referred to above, the continued ability of the Co-operative Group (via the Co-operative Banking Group Limited) to make the remaining 2014 contribution of £163m and to meet its other commitments to the Bank as they fall due. To date, all payments have been paid when due. Based on all the information provided by the Co-operative Group, and on investigations made by and on behalf of the Bank, the Bank believes that the incorporation of this contribution into its plans is appropriate;

iii) On 20 December 2013, the Bank began the process of separating its operations from its former parent, the Co-operative Banking Group Limited, and its ultimate former parent, the Co-operative Group, with both of which it shares premises, systems and services. The work is complex and time consuming and there remains a risk that the costs of executing these separation plans may increase. The potential misalignment of Group and Bank's objectives may also make separation slower and more costly than anticipated;

iv) The Bank participates in the Co-operative Group's defined benefit pension scheme (Pace). A material difference to current estimates of the funding of the pension scheme, or the Bank being forced to pay for a greater proportion than currently envisaged, could cause the Bank to require further capital in addition to that referred to above; and

v) More generally the ability of the Bank to achieve the results set out in the 2014-2018 Business Plan. In this respect particular challenges include (but are not limited to): ability to achieve the targeted cost savings; ability to retain customers and deposits; the timing and quantum of impacts to capital from the asset reduction exercise; meeting its planned improvements in net interest margin; the ability of the Bank to generate sufficient asset growth; a possible further deterioration in the quality of the Bank's asset portfolio; unplanned costs from (for example) conduct risk matters, regulatory investigations, IT investment and the ability to maintain the Bank's access at an appropriate cost to liquidity and funding.

f. Conclusion

The Directors have concluded that despite delivering lower than expected losses and higher CET1 for the half year ended 30 June 2014, the risks set out above, and their consequential effects, represent a material uncertainty which may cast significant doubt upon the Bank's ability to continue as a going concern. Nevertheless, after making enquiries and considering the current forecasts, in particular those for the period up to and including 31 August 2015, the Directors have a reasonable expectation that the Bank will have adequate resources to continue in business over this period. For these reasons, they continue to adopt the going concern basis in preparing these financial statements. This set of financial statements does not include the adjustments that would result if the Bank was unable to continue as a going concern.

1 Following the restatement discussed in note 3 CETI ratio would be 7.3% as at 31 December 2013. This restatement will be part of the regulatory capital calculation only once formally audited.

2. Critical judgements and estimates

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

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

The judgements and assumptions that are considered to be the most important to the portrayal of the Bank's financial condition are those relating to loan impairment provisions, conduct risk and legal provisions, deferred tax, pensions and hedge accounting.

a. Loan impairment provisions

i. Overview

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

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

The changes in impairment provisions for all books of business result from management review of assumptions, with respect to the determination and operational alignment of: The probability of the possession of collateral given default (PPD); treatment of forbearance; length of loss emergence periods; timing of impairment recognition and the formalising of charge off policy. Where required, management also periodically adjust collective provisions for additional risk parameters upon existing individual and collective impairment models.

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

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

ii. Collective provisions

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

a) Core

i) Unsecured and secured residential

The Bank's collective provision for unsecured and secured retail personal advances is £198.0m (31 December 2013: £167.8m). Loans are identified as impaired by taking account of the stage of the debt's delinquency, the product type and the regularity of payments made whilst in arrears. The provision is calculated by applying a percentage rate to different categories and ages of impairment debt.

The provision rates reflect the likelihood that the debt in that category/age will be written off or charged off at some point in the future. The rates are based on historical experience and current trends, which incorporate the effects of discounting at the customer interest rate and are subject to regular review. The provision is the product of the rate and the balance for the relevant arrears segment.

The unsecured provisions rely heavily on assumed probabilities of default.

A key estimate within the provisioning model is the discounted percentage provision rates applied to all personal loans subject to impairment. The most significant risk resides with credit card loans. A 5% (percentage point) change across these provision rates would change the collective provision by £24.6m.

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

b) Non-core

i) Corporate

The Bank's collective provision against corporate loans in the Non-core division has decreased to £26.8m (31 December 2013: £40.0m).

The collective provision is calculated using factors such as observed default rates and loss given default. An assessment is made of the likelihood of the assets becoming recognised as impaired in the loss emergence period.

The formula underpinning this methodology relies heavily on assumed probabilities of default:

Drawn Balance (£) x Probability of Default (%) x Loss Given Default (%) x Loss emergence period six months (as a fraction of 12 months). The Probability of Default and Loss Given Default are based on observed default propensities and loss events in this portfolio.

2. Critical judgements and estimates continued

The reduction in the collective provision is primarily due to the planned deleveraging of Non-core assets of the Bank and the write off of loans in 2014. There were no significant changes made to the collective provision methodology in 2014 with the exception of the reduction in the Loss Emergence Period (LEP) from 9 to 6 months. The reduction in the LEP resulted in a decrease in the provision of £2.8m. The LEP was calculated with reference to recently experienced data.

A key estimate within the corporate collective model is the LEP. A movement of one month in this estimate would change the provision by £1.0m. There is a linear relationship between the change in LEP and the change in provision.

ii) Optimum collective

In addition to the above, collective provisions of £11.2m (31 December 2013: £9.4m) are held in the Optimum segment of the Non-core business.

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

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

iii. Individual provisions

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

a) Core

i) Unsecured and secured residential

Individual provisions for unsecured and secured residential lending total £8.5m (31 December 2013: £10.7m). There were no significant changes made to the provision methodology in 2014.

b) Non-core

i) Corporate

The Bank's impairment provision on corporate loans totals £504.3m (31 December 2013: £698.4m). The provision has decreased reflecting improving macro economic factors and the Bank's strategy of reduction of its Non-core assets.

Each corporate account is assessed and allocated a 'risk grade' to enable the Bank to monitor the overall quality of its lending assets. Those of lesser quality, where the lending is potentially at risk and loss provisions may be required, are centrally monitored. Provisions represent the likely net loss after realisation of any security.

There were no significant changes made to the provision methodology in 2014 reflecting comparable macro economic factors with the 2013 year end.

A key estimate within the corporate individual impairment model is collateral valuation. A 10% movement in this estimate would change the provision by £77.2m.

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

ii) Optimum individual

The Bank's individual impairment provision on Optimum mortgages is £13.0m (31 December 2013: £26.1m). Mortgage accounts are identified as impaired and provided for on an individual basis by taking account of the stage of the debt's delinquency.

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

b. Conduct risk and legal provisions

i. Overview

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

Significant components of the conduct risk and legal provision are potential customer redress in relation to Payment Protection Insurance (PPI), interest rate swaps and technical breaches of the Consumer Credit Act. The Bank has also made provision for conduct provisions which are individually less significant. In total a charge of £38.6m (30 June 2013: £166.7m, including £3.7m redress costs included within operating expenditure) has been made during the period.

The calculation of these conduct and legal provisions requires significant judgement by management in determining appropriate assumptions. Key assumptions include basis of redress, operating costs of resolving redress, the level of complaints, uphold rates, proactive contact and response rates and Financial Ombudsman Service referral and uphold rates.

All amounts are stated in £m unless otherwise indicated

2. Critical judgements and estimates continued

ii. Payment Protection Insurance

A provision of £96.5m (31 December 2013: £133.8m) has been recorded in respect of potential customer redress relating to past sales of Payment Protection Insurance ('PPI'). The provision is in respect of the total expected cost to the Bank of carrying out this work and paying compensation, making total provisions raised to date of £352m (31 December 2013: £347m).

The additional provision recorded during the period of £5m results from a number of factors. The most significant factors include the calculation of single premium PPI redress based on full redress rather than redress based on an equivalent regular premium PPI and the application of further guidance from Financial Ombudsman Service in relation to late fees.

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

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

Bank PPI assumptions table

Description of estimate	Current position	Future expected	Sensitivity on current position
Number of inbound valid*[1] complaints	78,000	20,000	1,000 = £1.5m
Number of proactive mailings	36,000	12,000	1,000 = £1.9m
Response rate to proactive mailings	62%	63%	1% = £1.4m
Average uphold rate per valid*[1] complaint	63%	59%	1% = £0.7m
Average redress per upheld complaint	£3,237	£2,530	£100 = £1.6m

(Note*[1], valid complaints excludes those complaints for which no PPI policy exists).

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

iii. Interest rate swap mis-selling

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

A provision of £25.6m (31 December 2013: £33.0m) for potential interest rate swap mis-selling has been recorded at 30 June 2014. The decrease in the provision reflects the utilisation of the provision in the period.

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

There are a number of key assumptions within the calculation of the current provision. The key assumptions within the calculation of the current provision are the population of in scope swaps and the methodology to calculate redress provision.

Where redress methods change, the value will also change. It has also been assumed that customers who opted out of the initial review of interest rate hedging products will subsequently choose to be placed back in the review, as is their right. The provision assumes that no redress will be required for potential future claims for consequential losses.

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

An amount of £136.5m (31 December 2013: £109.5m) has been recognised regarding interest refunds following identification of a number of breaches of the highly technical requirements of the Consumer Credit Act.

The increase in the provision reflects the interest chargeable on the related loan in accordance with the relevant loan agreements in this six month period. The provision will increase in line with interest charged in the period every period until the issue is resolved.

Assumptions for provisioning purposes are that the payment profile of loans was as per those agreed at drawdown. The provision covers all interest accrued during non-compliance to the end of June 2014. Until loans are returned to a compliant state which is expected in H2 of 2014, the ongoing cost is up to £0.1m per day leading to a probable increase in the total provision of £18m in the second half of 2014.

Within the provision, operating costs of £11m are based upon the latest view of delivery timeframes.

2. Critical judgements and estimates continued

v. Other conduct/compliance related provisions

Other conduct/compliance related provisions include the following:

- £37.6m (31 December 2013: £29.0m) for potential customer redress relating to the processing of first payments on certain mortgages;
- £31.0m (31 December 2013: £31.0m) relating to potential customer redress in relation to mortgage fees;
- £26.1m (31 December 2013: £26.1m) for alleged failings in the introduction of third party sales of card and identification protection products;
- £22.0m (31 December 2013: £22.0m) relating to potential customer redress on secured arrears;
- £14.0m (31 December 2013: £15.0m) for potential customer redress in relation to arrears charges;
- £15.0m (31 December 2013: £15.0m) relating to provision for potential conduct issues incurred but not reported;
- £9.0m (31 December 2013: £13.0m) relating to potential customer redress and other costs in relation to mortgage documentation; and
- £9.9m (31 December 2013: £10.9m) of other conduct provisions.

Key assumptions include basis of redress, operating costs of resolving redress, the level of complaints, uphold rates, proactive contact and response rates and Financial Ombudsman Service referral and uphold rates.

The above provisions have a significant range of highly judgemental outcomes, the most significant of which reside within the provision for alleged failings in the introduction of third party sales of card and identification protection products. Given the Bank has relatively limited levels of actual experience for estimates within this provision, it carries the inherent risk of forecasting for subjective final outcomes. For example, customer response ratios to the proactive customer contact programme, or an extension to the time period, for which a proactive customer contact programme is required. A change in the overall estimates for outcomes could increase the provision by up to £52m.

c. Deferred tax

The Bank has recognised a deferred tax asset of £3.2m (31 December 2013: £2.5m restated) and a deferred tax liability of £77.8m (31 December 2013: £92.5m). The deferred tax liability has been calculated using a tax rate of 20%.

The deferred tax asset relates to temporary differences arising on consolidation adjustments and the taxation of SPEs in the securitisation regime. The deferred tax asset has been recognised on the basis that its recoverability is not dependent on the future performance of the Bank.

d. Pensions

i. Defined contribution accounting for the Pace scheme

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

ii. Defined benefit accounting for the Britannia scheme

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

Following the continued separation of the Bank from the wider Co-operative Group, the Britannia scheme is now accounted for on a defined benefit basis within the accounts of the Bank. Further information on the financial implications of accounting for the Britannia scheme on a defined benefit basis is disclosed in note 15.

e. Hedge accounting

The Bank reviewed its hedge accounting methodology in the period and concluded that the method for calculating hedge ineffectiveness should be revised to better align with industry practices under IAS 39 (Financial Instruments: Recognition and Measurement). This has resulted in the recognition of an accounting loss in the period and a restatement of prior periods.

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

All amounts are stated in £m unless otherwise indicated

3. Restatement

This note provides details of restatements for hedge accounting, IFRIC 21 levies and CFSMS assets.

The comparative information presented within the Interim Financial Report 2014 reflects the information disclosed within the Prospectus prepared to support the Liability Management Exercise dated 4 November 2013 (restated as explained below) and not the information presented within the Interim Financial Report 2013.

Hedge accounting

The Bank elects to make use of different hedge accounting techniques in order to eliminate (as far as possible) any profit or loss generated purely through the implementation of accounting standards (as opposed to actual economic losses).

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

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

IFRIC 21 Levies

This interpretation provides guidance on accounting for the liability to pay a government imposed levy and has resulted in a change in the timing of recognition of Financial Services Compensation Scheme (FSCS) levies that impact the Bank.

The Bank has an obligation to contribute to the FSCS to enable the scheme to meet interest, capital and administrative costs of safeguarding the protected deposits of savers in financial institutions that have failed. The scheme year is from 1 April to 31 March and levies are calculated on the proportion of the deposit taker's protected deposits at the preceding 31 December.

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

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

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

Statement of financial position

	Note	1 January 2013 (as reported)	Adjustment	1 January 2013 (restated)	31 December 2013 (as reported)	Adjustment	31 December 2013 (restated)
Assets							
Fair value adjustments for hedged risk	10b	354.2	–	354.2	107.6	(1.3)	106.3
Liabilities							
Debt securities in issue		4,713.7	2.5	4,716.2	4,195.3	12.3	4,207.6
Provisions for liabilities and charges	13	162.7	(24.8)	137.9	576.0	(26.3)	549.7
Reserves							
Retained earnings		1,304.3	–	–	(39.4)	–	–
Adjustment re FSCS levy		–	24.8	–	–	26.3	–
Adjustment for hedge accounting		–	(5.9)	1,323.2	–	(16.6)	(29.7)
		1,304.3	18.9	1,323.2	(39.4)	9.7	(29.7)
Cashflow hedging reserve		63.7	3.4	67.1	14.9	5.5	20.4

As part of the reserves restatement deferred tax assets have been recognised. Further details can be found in note 14.

All amounts are stated in £m unless otherwise indicated

3. Restatement continued

Income statement

The hedge accounting restatement gives rise to a restated presentation of items within net interest income. The IFRIC 21 levies restatement gives rise to a restated presentation of items within operating expenses. The impact of the restatements is shown below:

	Note	30 June 2013 (as reported)	Adjustment	30 June 2013 (restated)
Net interest income	5	(59.4)	(8.0)	(67.4)
Other operating income		26.0	(0.4)	25.6
FSCS Levies	13	0.1	(24.8)	(24.7)
Operating loss		(811.7)	(33.2)	(844.9)
Loss for the period before taxation		(811.4)	(33.2)	(844.6)

The impact on regulatory capital is described in the Capital Management section on page 45.

The total impact of the IFRIC 21 levy adjustment as at 31 December 2013 is to reduce the year end FSCS provision by £26.3m to £13.3m, for the charge to reduce by £1.5m and the cumulative impact on reserves is an increase of £24.8m.

CFSMS Assets

In 2013 the accounting treatment of assets held on the books of CFSMS was reviewed and the conclusion reached that, as the Bank was substantially exposed to the risks and rewards of these assets, they should be held on the Bank's balance sheet. The impact of this is a re-classification within note 7, whereby £11.8m of administrative expenses in the period to June 2013 are now recorded as depreciation and amortisation. This is referred to in more detail in the 2013 Annual Report and Accounts.

All amounts are stated in £m unless otherwise indicated

4. Segmental information

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

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

	Core					Non-core				
	Retail	BaCB	Treasury	Other[1]	Total Core	Corporate CoAM	Optimum	Illius	Total Non-core	Total
Period to 30 June 2014										
Net interest income	201.5	23.0	(9.3)	5.7	220.9	11.8	17.3	(2.1)	27.0	247.9
Non-interest income	55.9	7.9	(21.2)	3.1	45.7	14.5	2.4	(2.0)	14.9	60.6
Operating income	257.4	30.9	(30.5)	8.8	266.6	26.3	19.7	(4.1)	41.9	308.5
Direct costs	(78.4)	(8.7)	(7.2)	(4.2)	(98.5)	(9.3)	(2.6)	(2.3)	(14.2)	(112.7)
Impairment gains/(losses)	(1.3)	(1.4)	–	1.2	(1.5)	79.3	9.0	(0.1)	88.2	86.7
Contribution result	177.7	20.8	(37.7)	5.8	166.6	96.3	26.1	(6.5)	115.9	282.5
Operations and central costs					(174.5)				(9.8)	(184.3)
Project costs					(60.0)				(8.8)	(68.8)
Operating result					(67.9)				97.3	29.4
Intangible asset impairment										–
PPI provision and conduct and legal risk										(38.6)
Share of post tax losses from joint ventures										(0.1)
Financial Services Compensation Scheme Levies										(25.3)
Fair value amortisation										(41.2)
Loss before taxation										(75.8)
Income tax										19.1
Loss for the period										(56.7)

1 Included within 'Core – Other' is Unity Trust Bank. Unity Trust Bank operates in the corporate banking and social economy sectors and is consolidated into the Bank's results on the basis of control. On 14 January 2014, it was announced that the Bank is in discussions with the Board of Unity Trust Bank about a potential sale of its 26.7% shareholding. Discussions continue and any decision on a changed ownership structure would be subject to regulatory approval.

During 2014 the Bank changed the way it reports the Core and Non-core business costs by segment. The 2013 comparatives have been re-presented to reflect this change.

All amounts are stated in £m unless otherwise indicated

4. Segmental information continued

	Core					Non-core				
	Retail	BaCB	Treasury	Other	Total Core	Corporate CoAM	Optimum	Illius	Total Non-core	Restated Total
Period to 30 June 2013										
Net interest income	203.5	34.4	(5.7)	4.3	236.5	15.1	(7.5)	(3.1)	4.5	241.0
Non-interest income	65.0	7.7	26.9	0.9	100.5	17.1	3.3	(14.5)	5.9	106.4
Operating income	268.5	42.1	21.2	5.2	337.0	32.2	(4.2)	(17.6)	10.4	347.4
Direct costs	(90.4)	(11.5)	(4.8)	(3.3)	(110.0)	(5.5)	(1.2)	(1.9)	(8.6)	(118.6)
Impairment losses on loans and advances	(21.7)	(0.5)	(0.1)	(0.5)	(22.8)	(432.9)	(36.2)	–	(469.1)	(491.9)
Contribution result	156.4	30.1	16.3	1.4	204.2	(406.2)	(41.6)	(19.5)	(467.3)	(263.1)
Operations and central cost					(169.2)				(19.4)	(188.6)
Project costs					(45.2)				(3.7)	(48.9)
Operating result					(10.2)				(490.4)	(500.6)
Intangible asset impairment										(148.4)
PPI provision and conduct and legal risk										(163.0)
Share of post tax profits from joint ventures										0.3
Financial Services Compensation Scheme Levies										(24.7)
Fair value amortisation										(8.2)
Loss before taxation										(844.6)
Income tax										39.4
Loss for the period										(805.2)

All amounts are stated in £m unless otherwise indicated

4. Segmental information continued

Reconciliation to statutory income statement	Period to 30 June 2014	Restated Period to 30 June 2013
Net interest income		
Total interest margin for reportable segments	**247.9**	241.0
Interest fair value unwind	**(45.0)**	(4.2)
Provision for customer redress claims	**(25.0)**	(39.0)
Net interest income	**177.9**	197.8
Non-interest income		
Total non-interest income for reportable segments	**60.6**	106.4
Interest fair value unwind	**6.0**	0.3
Provision for customer redress claims	**(5.0)**	(94.0)
Non-interest income	**61.6**	12.7
Comprising:		
Net fee and commission income/(expense)	**63.0**	(14.0)
Net trading income	**0.2**	1.1
Other operating (expense)/income	**(1.6)**	25.6
	61.6	12.7
Operating expenses		
Total direct costs for reportable segments	**(112.7)**	(118.6)
Interest fair value unwind	**(2.2)**	(4.3)
Operations and central costs	**(184.3)**	(188.6)
Project costs	**(68.8)**	(48.9)
Provision for customer redress claims	**(8.6)**	(30.0)
Financial Services Compensation Scheme Levies	**(25.3)**	(24.7)
Re-presentation of fraud costs	**–**	4.1
Operating expenses	**(401.9)**	(411.0)
Interest fair value unwind		
Total interest unwind for reportable segments	**(41.2)**	(8.2)
Interest margin unwind	**45.0**	4.2
Non-interest income unwind	**(6.0)**	(0.3)
Operating expenses unwind	**2.2**	4.3
Interest fair value unwind	**–**	–
Impairment gains/(losses) on loans and advances		
Total impairment gains/(losses) on loans and advances for reportable segments	**86.7**	(491.9)
Re-presentation of fraud costs	**–**	(4.1)
Impairment gains/(losses) on loans and advances	**86.7**	(496.0)

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

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

All amounts are stated in £m unless otherwise indicated

4. Segmental information continued

	Core					Non-core				
	Retail	BaCB	Treasury	Other	Total Core	Corporate CoAM	Optimum	Illius	Total Non-core	Total
30 June 2014										
Segment assets	**15,335.5**	**778.8**	**10,892.7**	**495.0**	**27,502.0**	**4,867.9**	**7,117.4**	**156.0**	**12,141.3**	**39,643.3**
Unallocated assets										**1,151.9**
Total assets for reportable segments										**40,795.2**
Statutory adjustments										**281.4**
Bank total assets										**41,076.6**

	Core					Non-core				
	Retail	BaCB	Treasury	Other	Total Core	Corporate CoAM	Optimum	Illius	Total Non-core	Total
Segment liabilities	**27,249.1**	**2,594.6**	**6,438.5**	**448.0**	**36,730.2**	**809.3**	**–**	**–**	**809.3**	**37,539.5**
Unallocated liabilities										**807.9**
Total liabilities for reportable segments										**38,347.4**
Statutory adjustments										**614.0**
Bank total liabilities										**38,961.4**

	Core					Non-core				
	Retail	BaCB	Treasury	Other	Total Core	Corporate CoAM	Optimum	Illius	Total Non-core	Total
31 December 2013 (as restated)										
Segment assets	16,790.9	844.9	10,491.4	441.0	28,568.2	5,646.1	7,326.1	162.2	13,134.4	41,702.6
Unallocated assets										1,557.9
Total assets for reportable segments										43,260.5
Statutory adjustments										136.8
Bank total assets										43,397.3

	Core					Non-core				
	Retail	BaCB	Treasury	Other	Total Core	Corporate CoAM	Optimum	Illius	Total Non-core	Total
Segment liabilities	27,899.3	3,479.0	7,645.5	394.9	39,418.7	831.0	–	–	831.0	40,249.7
Unallocated liabilities										603.8
Total liabilities for reportable segments										40,853.5
Statutory adjustments										751.3
Bank total liabilities										41,604.8

Unallocated assets are non-customer assets and liabilities that are not allocated to a particular segment.

Statutory adjustments mainly relate to the reallocation of provisions, accruals and prepayments and the gross up of mark to market values.

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

All amounts are stated in £m unless otherwise indicated

5. Net interest income

	Period to 30 June 2014	Restated Period to 30 June 2013
Interest receivable and similar income		
On financial assets not at fair value through income or expense:		
On loans and advances to customers	**567.9**	643.1
On loans and advances to banks	**17.2**	15.4
On investment securities	**29.6**	75.3
	614.7	733.8
On financial assets at fair value through income or expense:		
Net interest expense on financial instruments hedging assets	**(54.9)**	(67.4)
Net interest income on financial instruments not in a hedging relationship	**6.5**	41.2
	566.3	707.6

Included within interest receivable is £3.9m (30 June 2013: £7.2m) relating to profit on sale of investment securities – available for sale.

The changes in provision for potential customer redress claims recorded against interest income consist of:

	Period to 30 June 2014	Period to 30 June 2013
Potential customer redress in relation to breaches of the Consumer Credit Act	**(29.0)**	(29.0)
Potential customer redress in relation to past sales of interest rate hedging products	**–**	(10.0)
Provision for potential customer redress and other costs in relation to mortgage documentation	**4.0**	–
	(25.0)	(39.0)

See note 13 for further details of the above provisions.

	Period to 30 June 2014	Period to 30 June 2013
Interest expense and similar charges		
On financial liabilities not at fair value through income or expense:		
On customer accounts	**(214.6)**	(255.3)
On bank and other deposits	**(118.8)**	(127.5)
On subordinated liabilities	**(11.3)**	(40.1)
On perpetual secured debt	**–**	(20.8)
	(344.7)	(443.7)
On financial liabilities at fair value through income or expense:		
Net interest expense on financial instruments hedging liabilities	**(8.4)**	(9.5)
Net interest expense on financial instruments not in a hedging relationship	**(10.3)**	(17.6)
	(363.4)	(470.8)
Net interest income	**177.9**	197.8

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

The Bank's perpetual secured debt was extinguished on 20 December 2013 as part of the Liability Management Exercise. The associated interest expense is therefore £nil during the period (30 June 2013: £20.8m).

Interest expense on bank and other deposits includes interest expense on deposits by banks and on debt securities in issue. It also includes fair value unwind on debt securities in issue of £53.8m (30 June 2013: £44.7m). Further details of which are provided in note 19.

All amounts are stated in £m unless otherwise indicated

6. Net fee and commission income/(expense)

	Period to 30 June 2014	Period to 30 June 2013
Fee and commission income		
On items not at fair value through income or expense	**104.8**	116.0
On trust or fiduciary activities that result from holding or investing in assets on behalf of others	**0.1**	0.2
	104.9	116.2

The changes in provision for potential customer redress claims recorded against net fee and commission income consist of:

	Period to 30 June 2014	Period to 30 June 2013
Potential customer redress in relation to past sales of Payment Protection Insurance	**(5.0)**	(53.0)
Potential customer redress in relation to alleged failings in the introduction of third party sales of card and identity protection products	**–**	(26.0)
Potential customer redress in relation to mortgage arrears fees and charges	**–**	(15.0)
	(5.0)	(94.0)

See note 13 for further details of the above provisions.

	Period to 30 June 2014	Period to 30 June 2013
Fee and commission expense		
On items not at fair value through income or expense	**(36.8)**	(34.3)
On items at fair value through income or expense	**(0.1)**	(1.9)
	(36.9)	(36.2)
Net fee and commission income/(expense)	**63.0**	(14.0)

7. Operating expenses

	Note	Period to 30 June 2014	Restated Period to 30 June 2013
Operating expense			
Staff costs	8	**146.5**	131.5
Administrative expenses		**143.9**	146.9
Depreciation of property, plant and equipment		**7.0**	8.8
Amortisation of intangible fixed assets		**12.9**	12.0
Impairment of brand intangible fixed assets		**–**	2.0
Operating lease rentals		**15.3**	15.6
Financial Services Compensation Scheme Levies	13	**25.3**	24.7
Property provisions for liabilities and charges provided in the period	13	**1.9**	3.6
Property provisions for liabilities and charges released during the period	13	**–**	(0.4)
Other provisions for liabilities and charges provided in the period	13	**2.7**	–
Other provisions for liabilities and charges released during the period	13	**(0.6)**	(0.1)
Direct expenses from investment properties that generated rental income in the period		**4.0**	1.7
Direct expenses from investment properties that did not generate rental income in the period		**0.1**	0.1
		359.0	346.4

All amounts are stated in £m unless otherwise indicated

7. Operating expenses continued

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

	Note	**Period to 30 June 2014**	Period to 30 June 2013
Investment costs		**20.6**	14.7
Bank separation costs	13	**6.7**	–
Provision for customer redress claims relating to processing of first payments on certain mortgages and other redress claims	13	**8.6**	30.0
Costs incurred in bid for Lloyds Banking Group branches		**–**	10.0
Impairment of property, plant and equipment		**7.0**	9.9
		42.9	64.6
Total operating expenses		**401.9**	411.0

No expenditure has been incurred in respect of the Government's Bank Levy since the relevant aggregate liabilities of the Bank are below the qualifying threshold.

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

8. Staff costs

	Note	**Period to 30 June 2014**	Period to 30 June 2013
Wages and salaries		**88.5**	93.7
Social security costs		**7.7**	7.2
Pension costs:			
Defined benefit plans	15	**3.3**	0.1
Defined contribution plans		**13.8**	13.6
Other staff costs		**33.2**	16.9
		146.5	131.5

Up until 20 December 2013, employee activities were undertaken across the Co-operative Banking Group and the figures above reflect the Bank's share of these services.

Employees of the Bank were employed by CFS Management Services Limited (CFSMS) during 2013 and staff costs recharged to the Bank. With effect from 23 January 2014, the majority of Bank employees had their employment contracts transferred from CFSMS to The Co-operative Bank plc. The transfer was required to support the legal separation of the Bank from the Co-operative Group. This transfer took place under the Transfer of Undertakings (Protection of Employment) Regulations 2006.

All amounts are stated in £m unless otherwise indicated

9. Income tax

	Note	Period to 30 June 2014	Period to 30 June 2013 (restated)
Current tax			
Current period		**(5.3)**	(103.1)
Prior period		**1.5**	–
Total current tax		**(3.8)**	(103.1)
Deferred tax			
Current period	14	**(15.3)**	7.6
Write off of prior period deferred tax asset	14	**–**	56.1
Total deferred tax		**(15.3)**	63.7
Total tax credit		**(19.1)**	(39.4)

In addition to the above, current tax of £1.2m has been charged to other comprehensive income and deferred tax of £0.1m has been credited to other comprehensive income.

Further information on deferred income tax is presented in note 14. The tax on the Bank's loss before taxation differs from the theoretical amount that would arise using the corporation tax rate in the UK as follows:

	Note	Period to 30 June 2014	Period to 30 June 2013 (restated)
Loss before taxation		**(75.8)**	(844.6)
Tax calculated at a rate of 21.49% (30 June 2013: 23.25%)		**(16.3)**	(196.4)
Effects of:			
Write off of prior year deferred tax asset	14	**–**	56.1
Non-taxable income		**(1.3)**	(0.7)
Unrecognised deferred tax		**(0.4)**	92.9
Discount of group relief debtor		**(4.9)**	–
Change in rate of deferred tax		**0.5**	2.1
Expenses not deductible for tax purposes		**2.4**	2.9
Adjustments to tax charge in respect of prior periods		**1.5**	–
Depreciation of capital expenditure qualifying for capital allowances		**0.2**	2.9
Other differences		**(0.8)**	0.8
		(19.1)	(39.4)

Expenses not deductible of £2.4m (30 June 2013: £2.9m) include costs resulting from the separation of the Bank from the Co-operative Group.

The comparatives for period 30 June 2013 have been restated for the FSCS levy provision and hedge accounting changes as described in note 3. This results in additional unrecognised deferred tax assets of £6.7m.

10. a) Loans and advances to customers

	30 June 2014	31 December 2013
Gross loans and advances	**28,598.2**	31,274.6
Less: allowance for losses	**(761.8)**	(952.4)
	27,836.4	30,322.2

The Bank's loans and advances to customers include £167.6m (31 December 2013: £134.2m) of financial assets at fair value through income or expense designated at initial recognition to eliminate or significantly reduce a measurement or recognition inconsistency. Of these, £86.9m (31 December 2013: £62.9m) are secured by real estate collateral.

All amounts are stated in £m unless otherwise indicated

10. a) Loans and advances to customers continued

Loans and advances to customers include £9,515.9m (31 December 2013: £10,111.9m) securitised under the Bank's securitisation and covered bond programmes. The Bank remains exposed to substantially all of the risks and rewards of ownership of these assets. Included within the Bank's deposits by banks are £500.2m (31 December 2013: £500.3m) of loans from external third parties and within the Bank's debt securities in issue are £3,338.9m (31 December 2013: £3,703.4m) of fixed and floating rate notes, all secured on these mortgage assets.

Concentration of exposure

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

Allowance for losses on loans and advances

	Core		Non-core		
	Individual	Collective	Individual	Collective	Total
Period to 30 June 2014					
At the beginning of the period	**10.7**	**167.8**	**724.5**	**49.4**	**952.4**
Balances with debt collection agencies	**–**	**39.6**	**–**	**–**	**39.6**
Charge/(release) against profits	**(0.3)**	**1.9**	**(109.1)**	**(11.4)**	**(118.9)**
Amounts written off	**(1.8)**	**(8.9)**	**(93.9)**	**–**	**(104.6)**
Unwind of discount allowance	**(0.1)**	**(2.4)**	**(4.2)**	**–**	**(6.7)**
At the end of the period	**8.5**	**198.0**	**517.3**	**38.0**	**761.8**

Core provisions are analysed in further detail below:

	Core						
	Retail		BaCB		Other[1]		
	Individual	Collective	Individual	Collective	Individual	Collective	Total Core
Period to 30 June 2014							
At the beginning of the period	**2.8**	**161.9**	**0.5**	**5.3**	**7.4**	**0.6**	**178.5**
Balances with debt collection agencies	**–**	**39.6**	**–**	**–**	**–**	**–**	**39.6**
Charge/(release) against profits	**0.3**	**1.2**	**0.5**	**0.8**	**(1.1)**	**(0.1)**	**1.6**
Amounts written off	**(0.3)**	**(8.9)**	**(0.1)**	**–**	**(1.4)**	**–**	**(10.7)**
Unwind of discount allowance	**–**	**(2.4)**	**–**	**–**	**(0.1)**	**–**	**(2.5)**
At the end of the period	**2.8**	**191.4**	**0.9**	**6.1**	**4.8**	**0.5**	**206.5**

Non-core provisions are analysed in further detail below:

	Non-core				
	Corporate		Optimum		
	Individual	Collective	Individual	Collective	Total Non-core
Period to 30 June 2014					
At the beginning of the period	**698.4**	**40.0**	**26.1**	**9.4**	**773.9**
Charge/(release) against profits	**(98.2)**	**(13.1)**	**(10.9)**	**1.7**	**(120.5)**
Amounts written off	**(91.7)**	**–**	**(2.2)**	**–**	**(93.9)**
Unwind of discount allowance	**(4.2)**	**–**	**–**	**–**	**(4.2)**
At the end of the period	**504.3**	**26.9**	**13.0**	**11.1**	**555.3**

All amounts are stated in £m unless otherwise indicated

10. a) Loans and advances to customers continued

	Core		Non-core		
	Individual	Collective	Individual	Collective	Total
Year to 31 December 2013					
At the beginning of the year	9.4	175.2	434.8	23.6	643.0
Charge against profits for the period to 30 June 2013	2.9	34.3	402.1	117.9	557.2
Charge/(release) against profits for the period to 31 December 2013	(0.5)	3.7	39.2	(92.1)	(49.7)
Amounts written off	(0.9)	(41.8)	(145.1)	–	(187.8)
Unwind of discount allowance	(0.2)	(3.6)	(6.9)	–	(10.7)
Interest charged on impaired loans	–	–	0.4	–	0.4
At the end of the year	10.7	167.8	724.5	49.4	952.4

Core provisions are analysed in further detail below:

	Core						
	Retail		BaCB		Other[1]		
	Individual	Collective	Individual	Collective	Individual	Collective	Total Core
Year to 31 December 2013							
At the beginning of the year	2.7	173.3	0.3	1.1	6.4	0.8	184.6
Charge against profits for the period to 30 June 2013	1.9	33.7	0.4	0.6	0.6	–	37.2
Charge/(release) against profits for the period to 31 December 2013	(1.3)	(0.8)	0.2	4.7	0.6	(0.2)	3.2
Amounts written off	(0.5)	(40.7)	(0.4)	(1.1)	–	–	(42.7)
Unwind of discount allowance	–	(3.6)	–	–	(0.2)	–	(3.8)
At the end of the year	2.8	161.9	0.5	5.3	7.4	0.6	178.5

Non-core provisions are analysed in further detail below:

	Non-core				
	Corporate		Optimum		
	Individual	Collective	Individual	Collective	Total Non-core
Year to 31 December 2013					
At the beginning of the year	426.9	20.5	7.9	3.1	458.4
Charge against profits for the period to 30 June 2013	407.4	49.4	(5.3)	68.5	520.0
Charge against profits for the period to 31 December 2013	10.4	(29.9)	28.8	(62.2)	(52.9)
Amounts written off	(139.8)	–	(5.3)	–	(145.1)
Unwind of discount allowance	(6.9)	–	–	–	(6.9)
Interest charged on impaired loans	0.4	–	–	–	0.4
At the end of the year	698.4	40.0	26.1	9.4	773.9

1. 'Core – Other' relates to Unity Trust Bank.

A review of the Bank's relationships with debt collection agencies in 2014 concluded that the Bank had substantially retained all the risks and rewards associated with such relationships. The related gross receivables of £41.4m and associated allowance of £39.6m have therefore been recognised as at 30 June 2014.
The comparative information has not been adjusted on the grounds of materiality. Had the comparative information been adjusted the net Loans and Advances to Customers balance and Total Equity would have increased by £1.8m and £1.8m respectively.

All amounts are stated in £m unless otherwise indicated

10. a) Loans and advances to customers continued

The net impairment credit in the Bank's income statement is £86.7m (30 June 2013: loss of £496.0m). This includes amounts recovered by the Bank of £0.4m (30 June 2013: £0.2m) against amounts previously written off.

The impairment charge also includes a provision of £32.6m (30 June 2013: £1.4m) made against fair value adjustments for hedged risk during the period (as shown in the fair value adjustments for hedged risk tables).

The overall write back of impairment is largely due to improved credit conditions, restructuring of assets, and the disposal of Non-core assets at favourable prices, as part of the Bank's strategy to exit these books.

10. b) Fair value adjustments for hedged risk

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

	30 June 2014	Restated 31 December 2013
Gross fair value adjustments for hedged risk	**137.4**	153.1
Less: impairment provision	**(79.4)**	(46.8)
	58.0	106.3

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

	30 June 2014	31 December 2013
At the beginning of the period	**46.8**	37.0
Charge against profits for the period to 30 June 2014 (30 June 2013)	**32.6**	1.4
Charge against profits for the period to 31 December 2013	**–**	8.4
At the end of the period	**79.4**	46.8

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

11. Investment securities

a) Loans and receivables

	30 June 2014	31 December 2013
Loans and receivables		
Listed	**16.0**	23.6
Unlisted	**–**	–
	16.0	23.6
Less: allowance for losses	**–**	–
	16.0	23.6

b) Available for sale

	30 June 2014	31 December 2013
Available for sale		
Listed	**2,729.9**	2,497.2
Unlisted	**195.3**	255.2
	2,925.2	2,752.4
Less: allowance for losses	**–**	(20.0)
	2,925.2	2,732.4
Included in cash and cash equivalents	**155.0**	105.0

All amounts are stated in £m unless otherwise indicated

11. Investment securities continued

Impairment analysis of investment securities – available for sale

	30 June 2014	31 December 2013
At the beginning of the period	**20.0**	39.0
Release for the period	**(1.1)**	–
Utilised during the period	**(18.9)**	(18.5)
Exchange adjustments	**–**	(0.5)
At the end of the period	**–**	20.0

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

c) Fair value through income or expense

	30 June 2014	31 December 2013
Fair value through income or expense		
Listed	**1,256.7**	1,743.4
	1,256.7	1,743.4

d) Analysis of investment securities by issuer

	30 June 2014	31 December 2013
Investment securities issued by public bodies:		
Government securities	**3,021.1**	3,064.3
Other public sector securities	**255.2**	580.5
	3,276.3	3,644.8
Investment securities issued by other issuers:		
Bank and building society certificates of deposits	**195.3**	235.2
Other debt securities:		
Other floating rate notes	**710.3**	595.8
Mortgage backed securities	**16.0**	23.6
	726.3	619.4
	4,197.9	4,499.4

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

All amounts are stated in £m unless otherwise indicated

12. Customer accounts – capital bonds

	30 June 2014	31 December 2013
Retail	**388.9**	538.1

Capital bonds are fixed term customer accounts with returns based on the movement in an index (eg FTSE100) over the term of the bond.

The capital bonds have been designated on initial recognition at fair value through income and expense and are carried at fair value.

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

The maximum amount the Bank would contractually be required to pay at maturity for all the capital bonds is £394.9m (31 December 2013: £539.2m).

The Bank uses swaps to create economic hedges against all of its capital bonds. The gain on capital bonds in the income statement for the period is £23.6m (30 June 2013: loss of £9.4m). However, taking into account changes in fair value of the associated swaps, the net impact to the income statement for the period is a loss of £0.3m (30 June 2013: gain of £0.3m).

13. Provisions for liabilities and charges

	Note	Property	FSCS levies	PPI	Conduct/ legal	Other	Total
Period to 30 June 2014							
At the beginning of the period		**23.1**	**13.3**	**133.8**	**304.6**	**74.9**	**549.7**
Provided/(released) in the period:							
– net interest income	5	**–**	**–**	**–**	**25.0**	**–**	**25.0**
– net fee and commission income	6	**–**	**–**	**5.0**	**–**	**1.0**	**6.0**
– operating expense	7	**1.9**	**25.3**	**–**	**–**	**2.1**	**29.3**
– operating expense – separation costs	7	**–**	**–**	**–**	**–**	**6.7**	**6.7**
– operating expense – other potential customer redress claims	7	**–**	**–**	**–**	**8.6**	**–**	**8.6**
Utilised during the period		**(0.9)**	**–**	**(42.3)**	**(10.5)**	**(26.8)**	**(80.5)**
At the end of the period		**24.1**	**38.6**	**96.5**	**327.7**	**57.9**	**544.8**
Provisions were analysed as follows:							
Amounts falling due within one year		**12.3**	**25.4**	**80.5**	**310.7**	**57.9**	**486.8**
Amounts falling due after one year		**11.8**	**13.2**	**16.0**	**17.0**	**–**	**58.0**
		24.1	**38.6**	**96.5**	**327.7**	**57.9**	**544.8**

All amounts are stated in £m unless otherwise indicated

13. Provisions for liabilities and charges continued

	Note	Property	FSCS levies	PPI	Conduct/ legal	Other	Total
Year to 31 December 2013							
At the beginning of the year (as restated)		7.3	13.8	116.0	0.2	0.6	137.9
Provided/(released) in the period to:							
– net interest income	5	–	–	–	194.5	–	194.5
– net fee and commission income	6	–	–	103.0	82.1	–	185.1
– operating expense (as restated)	7	16.3	24.1	–	–	35.0	75.4
– operating expense – separation costs	7	–	–	–	–	39.4	39.4
– operating expense – other potential customer redress claims	7	–	–	–	31.9	–	31.9
Utilised during the year		(0.5)	(24.6)	(85.2)	(4.1)	(0.1)	(114.5)
At the end of the year (as restated)		23.1	13.3	133.8	304.6	74.9	549.7
Provisions were analysed as follows:							
Amounts falling due within one year		10.2	13.3	113.8	304.6	74.9	516.8
Amounts falling due after one year		12.9	–	20.0	–	–	32.9
		23.1	13.3	133.8	304.6	74.9	549.7

Conduct and legal provisions of £25.0m (period to 30 June 2013: £39.0m) have been recorded as a charge against interest in the income statement. Details of these amounts are provided in the next section.

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

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

Property

The Bank has a number of leasehold properties available for rent. Provisions are made when either the sub-lease income does not cover the rental expense or the property is vacant. The provision is based on the expected outflows during the remaining periods of the leases using a discount rate of 3.5%. In addition, dilapidation provisions are recorded to the extent that the Bank has incurred dilapidations and/or the dilapidation clause within the contract has been invoked.

Financial Services Compensation Scheme (FSCS) levies

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

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

By virtue of it holding deposits protected under the FSCS scheme at 31 December 2012, the Bank has an obligation to pay levies in respect of the interest cost for 2013/14. From this scheme year, the FSCS had also started to repay the principal of the Treasury loans and a further levy had been raised in 2013/14 for the expected capital shortfall for these loans, so that they are fully repaid by March 2016. The total levy to be raised is £961m over three years, with the first instalment of £363m collected in the previous year.

The Bank has provided £38.6m as at 30 June 2014 (2013 restated: £13.3m) for its share of the levies raised by the FSCS. The provision includes £14.3m in respect of the 2013/14 interest levy and £13.1m for the 2014/15 interest levy. The Bank's interest levy provision calculation includes estimates of the total FSCS levy in each levy year and estimates of the Bank's market participation in each levy year. The Bank has also provided £11.2m in respect of its share of the capital levy.

All amounts are stated in £m unless otherwise indicated

13. Provisions for liabilities and charges continued

Payment Protection Insurance (PPI)

Provisions have been made in respect of potential customer compensation claims relating to past sales of PPI. Claims are investigated on an individual basis and, where appropriate, compensation payments are made.

The FSA issued a policy statement in August 2010, which amended the 'Disputes Resolution: Complaints' section of the FSA Handbook, setting out new rules for handling complaints, including complaints of PPI mis-selling. The Bank must comply with the policy statement which requires complainants to receive adequate redress and the Bank to deliver fair outcomes and treat customers fairly including non-complainants. An additional provision of £5.0m (30 June 2013: £53.0m) has been recognised in the period (note 6), in respect of the total expected cost to the Bank of carrying out this work and paying compensation, making total provisions raised of £352.0m (31 December 2013: £347.0m). This is discussed in more detail in note 2.

Conduct/legal provisions

During the period £25.0m (30 June 2013: £39.0m) was charged to net interest income. This consists of: potential customer redress following identification of breaches of the highly technical requirements of the Consumer Credit Act £29.0m (30 June 2013: £29.0m); potential interest rate swap mis-selling £nil (30 June 2013: £10.0m); and potential customer redress and other costs in relation to mortgage documentation £4.0m release (30 June 2013: £nil).

£8.6m (30 June 2013: £30.0m) was charged through operating expenses relating to potential customer redress for the processing of first payments on certain mortgages.

Other

£6.7m (30 June 2013: £nil) has been provided through operating expenses for additional costs associated with the separation of the Bank from the Co-operative Group.

14. Deferred tax

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

The movements on the deferred tax accounts are as follows:

		30 June 2014			31 December 2013 (restated)		
	Note	**Deferred tax asset**	**Deferred tax liability**	**Total**	Deferred tax asset	Deferred tax liability	Total
Deferred tax at the beginning of the period		**2.5**	**(92.5)**	**(90.0)**	159.6	(121.4)	38.2
(Credited)/charged to the income statement:							
Current period		**0.6**	**14.7**	**15.3**	(20.4)	28.9	8.5
Write off of prior period deferred tax asset	9	**–**	**–**	**–**	(157.5)	–	(157.5)
Prior period		**–**	**–**	**–**	3.3	–	3.3
		0.6	**14.7**	**15.3**	(174.6)	28.9	(145.7)
Credited/(charged) to other comprehensive income:							
Cashflow hedges		**0.1**	**–**	**0.1**	17.4	–	17.4
Available for sale		**–**	**–**	**–**	0.1	–	0.1
		0.1	**–**	**0.1**	17.5	–	17.5
Deferred tax at the end of the period		**3.2**	**(77.8)**	**(74.6)**	2.5	(92.5)	(90.0)

All amounts are stated in £m unless otherwise indicated

14. Deferred tax continued

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

	30 June 2014		31 December 2013 (restated)	
	Deferred tax asset	Deferred tax liability	Deferred tax asset	Deferred tax liability
Deferred tax comprises:				
Capital allowances on fixed assets and assets leased to customers	**2.2**	**–**	6.6	–
Fair value adjustments – The Co-operative Bank plc	**–**	**–**	–	–
Fair value adjustments – The Co-operative Bank subsidiaries	**–**	**(82.6)**	–	(92.5)
Other temporary differences	**3.2**	**4.8**	2.5	–
Tax losses carried forward	**–**	**–**	–	–
Pensions and other post-retirement benefits	**–**	**–**	–	–
Cashflow hedges	**(1.6)**	**–**	(0.8)	–
Unrealised appreciation on investments	**(0.6)**	**–**	(0.6)	–
FSCS levy provision	**–**	**–**	(5.2)	–
	3.2	**(77.8)**	2.5	(92.5)

Net deferred tax assets expected to be recoverable after one year are £3.2m (30 June 2013: £103.5m, 31 December 2013: £2.5m restated).

Other temporary differences for the Bank totalling £8.0m (30 June 2013: £27.0m, 31 December 2013: £2.5m restated) relate to temporary differences arising on consolidation adjustments and the taxation of special purpose entities under the securitisation regime.

The Directors consider the recoverability of deferred tax to be a critical accounting judgement. Further detail is provided in note 2.

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

	Period to 30 June 2014	Period to 30 June 2013 (restated)
Capital allowances on fixed assets and assets leased to customers	**4.4**	(0.1)
Fair value adjustments	**(9.9)**	8.6
Other temporary differences	**(9.8)**	(0.9)
Write off of prior year deferred tax asset	**–**	56.1
	(15.3)	63.7

Deferred tax assets totalling £270.1m (31 December 2013: £270.5m restated) have not been recognised where doubt exists over the availability of sufficient future taxable profits. Deferred tax assets from the prior year of £nil (31 December 2013: £157.5m) have been written off in the period. Deferred tax assets of £0.4m (31 December 2013: £113.9m) in respect of the current period have not been recognised.

Reductions in the UK corporation tax rate from 23% to 21% (effective from 1 April 2014) and 20% (effective from 1 April 2015) were substantively enacted on 2 July 2013. This will reduce the Bank's future current tax charge accordingly. The deferred tax liabilities at 30 June 2014 have been calculated based on the rate of 20% substantively enacted at the balance sheet date.

All amounts are stated in £m unless otherwise indicated

15. Pensions

The Bank participates in two hybrid multi-employer pension schemes, consisting of defined benefit and defined contribution sections, and also operates a small unfunded scheme; only the Pace scheme is open to further contributions. Full details of the schemes are disclosed within the Bank's Annual Report and Accounts 2013.

The Co-operative Pension Scheme (Pace)

The Bank continues to account for this multi-employer scheme on a defined contribution basis as detailed within the Bank's Annual Report and Accounts 2013. The Pace scheme triennial valuation as at 4 April 2013 was completed on 21 July 2014. The funding shortfall for the entire scheme had increased from £248m per the previous triennial valuation as at 6 April 2010 to £600m as at 4 April 2013. The latest funding shortfall position calculated by the scheme actuary on an approximate basis as at 31 May 2014 was £104m.

Britannia Pension Scheme

The Bank accounted for the Britannia Pension Scheme ('the Britannia Scheme') on a defined contribution basis in the Bank's Annual Report and Accounts 2013 for the reasons explained therein. Following increased separation of the Bank from the wider Co-operative Group, the Britannia Scheme is now accounted for on a defined benefit basis in the Interim Financial Report 2014.

Whilst the Britannia Scheme is in accounting surplus, this has not been recognised on the balance sheet in accordance with IFRIC 14. The Bank has however recognised a £3.2m liability (31 December 2013 – unrecognised £3.1m) in relation to the unfunded element of the Britannia Scheme.

The pension scheme liabilities on the balance sheet comprise:

	Assets 30 June 2014	Assets not recognised 31 December 2013	**Liabilities 30 June 2014**	Liabilities not recognised 31 December 2013	**Net 30 June 2014**	Net not recognised 31 December 2013
Britannia Pension Scheme	**637.9**	630.7	**(610.8)**	(604.2)	**27.1**	26.5
Less asset limitation (IFRIC 14)	**(27.1)**	(26.5)	**–**	–	**(27.1)**	(26.5)
	610.8	604.2	**(610.8)**	(604.2)	**–**	–
Britannia unfunded obligations	**–**	–	**(3.2)**	(3.1)	**(3.2)**	(3.1)
	610.8	604.2	**(614.0)**	(607.3)	**(3.2)**	(3.1)

The amounts recorded in the balance sheet are as follows:

	30 June 2014	Not recognised 31 December 2013
Present value of funded obligations	**(610.8)**	(604.2)
Present value of unfunded obligations	**(3.2)**	(3.1)
Asset limitation (IFRIC 14)	**(27.1)**	(26.5)
Fair value of plan assets	**637.9**	630.7
Net retirement plan liability	**(3.2)**	(3.1)

The amounts recognised in the income statement are as follows:

	30 June 2014	Not recognised 31 December 2013
Current service cost	**–**	–
Interest expense on Defined Benefit Obligation	**(13.6)**	(26.6)
Interest income on plan assets	**14.2**	26.7
Administrative expenses and taxes	**(0.5)**	(1.1)
	0.1	(1.0)

All amounts are stated in £m unless otherwise indicated

15. Pensions continued

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

31 December 2013 – Not recognised	(604.2)
Benefit payments from plan	7.0
Changes in asset ceiling/onerous liability	(13.6)
30 June 2014	(610.8)

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

31 December 2013 – Not recognised	630.7
Interest income	14.2
Contributions by the employer	0.5
Benefit payments from plan	(7.0)
Administrative expenses paid from plan assets	(0.5)
30 June 2014	637.9

The statutory deadline for the 5 April 2014 Britannia Scheme triennial valuation is 5 July 2015.

16. Contingent liabilities and commitments

Details of contingent liabilities and commitments at December 2013 were disclosed in the 2013 Annual Report and Accounts. These included the following key areas: CFSMS indemnification agreement; conduct and Consumer Credit Act issues; regulatory and other investigations; legal proceedings; mortgage securitisation representations and warranties; pensions and tax treatment of Bank separation.

The items disclosed remain broadly unchanged, except in the following key areas:

Breaches of the technical requirements of the Consumer Credit Act

An amount of £138.5m (2013: £109.5m) has been recognised to refund interest following identification of a number of breaches of the highly technical requirements of the Consumer Credit Act. As part of this process of identification, detailed and technical legal analysis has been carried out to determine whether breaches of the technical requirements have in fact occurred, the nature of those breaches and the consequences which follow (which differ according to the precise nature of the breach). Such legal analysis by its nature involves judgement and assessment of the facts of particular circumstances. In the event that such legal analysis and judgements are determined to be wrong, the Bank could be exposed to a material additional liability. The amount of £138.5m which has been provided is the best estimate of the liability based on the legal analysis.

17. Related party transactions

Related party transactions and transactions with key management personnel in the half year to 30 June 2014 are similar in nature to those for the year ended 31 December 2013. Details of these transactions can be found in the 2013 Annual Report and Accounts.

Significant changes to those relationships and transactions from December 2013 are as follows:

Parent, subsidiary and ultimate controlling party

As at 31 December 2013 the Bank was an associate of, and therefore a related party of the Co-operative Group as the Co-operative Group owned 30% of the Bank's ordinary shares, had Bank Board representation and there were material transactions between the two companies.

On 30 May 2014 there was a further £400m share capital issuance to existing investors. This resulted in the Co-operative Group ownership reducing to 20% of the ordinary share capital of the Bank.

At 30 June 2014, due to the Co-operative Group's ownership of 20% of the Bank's ordinary shares and the material transactions between the two companies, the Bank is deemed an associate of, and therefore a related party of, the Co-operative Group.

Details of the Relationship Agreement, Co-existence Principles and 2014 Commitment Agreement can be found in the 2013 Annual Report and Accounts.

Variation and Director Appointment Deed

At the time of the Capital Raising in May 2014, the Bank, the Co-operative Group Limited and the Co-operative Banking Group entered into a Variation and Director Appointment Deed which provided that the Co-operative Group Limited would have a right, for so long as it remains a bona fide co-operative society and directly or indirectly controls 15% or more of the voting rights exercisable at general meetings of the Bank, to appoint one Director to the Board.

This Deed also makes certain amendments to the Relationship Agreement by deleting the provision whereby the Co-operative Group had agreed to provide the Company with reasonable assistance to obtain a listing on the premium segment of the Official List within 12 months following the Liability Management Exercise becoming unconditional and the lock-up restrictions on the Co-operative Group disposing of its Ordinary Shares in the Bank for five years from the effective date of the Liability Management Exercise. This Variation and Director Appointment Deed provides that if the Relationship Agreement has not previously terminated in accordance with its terms with effect from 30 September 2014, these lock-up restrictions shall cease to have effect and the Co-operative Group shall from that date be entitled to sell its interest in Ordinary Shares without the consent of the Bank, provided that the Co-operative Group shall pay or cause to be paid to the Bank following such sale the net proceeds of such sale, and such payment obligation shall continue until the Undertaking to Pay (as defined in the 2014 Commitment Agreement) has been discharged in full.

Shareholder Rights Agreement

At the time of the Capital Raising in May 2014, the Bank entered into a Shareholder Rights Agreement with four of its major shareholders being SP Coop Investment, Ltd (Cayman)("Silverpoint"), Perry Capital UK LLP ("Perry"), Invesco Asset Management Limited and York Capital Management Europe (UK) Advisors LLP (together the "Committed Shareholders") and the Co-operative Group.

Under the Shareholder Rights Agreement, the Bank has granted to each of Silver Point and Perry the right to nominate a Director for appointment to the Board for so long as Silver Point and Perry, as the case may be, directly or indirectly controls 5% or more of the voting rights exercisable at general meetings of the Bank. Such rights are not transferable, save that they will automatically transfer and be exercisable by another Committed Shareholder if Silver Point or Perry ceases to control such level of voting rights in the Bank, provided that such other Committed Shareholder itself directly or indirectly controls 5% or more of such voting rights.

The Directors appointed under the Shareholder Rights Agreement may be, but are not required to be, independent. Under the Shareholder Rights Agreement, the Bank has agreed to establish a sub-committee of the Board that will assess the feasibility of the Bank listing its ordinary shares on the Official List and make recommendations to the Board with regards to the timing of such a listing. That subcommittee will be comprised of four Directors, being one Director appointed pursuant to the Relationship Agreement, one Director appointed pursuant to the Shareholder Rights Agreement, one executive Director and one independent non-executive Director who is not a Director appointed pursuant to the Relationship Agreement or the Shareholder Rights Agreement.

In addition, any of the Committed Shareholders and the Co-operative Group who together hold 25% or more of the Bank's issued Ordinary Share capital, will have the right, not to be exercised before 30 September 2014, to require the Bank to assist in the launch of a secondary offering of Ordinary Shares, provided that the exercising Shareholders have committed to sell Ordinary Shares valued at not less than £100 million. The Committed Shareholders may only exercise this right once in any 12 month period and three times in total.

More information on both the Variation and Director Appointment Deed and the Shareholder Rights Agreement can be found in the circular for the capital raising in May 2014 at http://www.co-operativebank.co.uk/assets/pdf/bank/news/placing-and-open-offer-circular.pdf

17. Related party transactions continued

Intra-group Loan

As detailed in the 2013 Annual Report and Accounts, the Bank, the Co-operative Banking Group and the Co-operative Group entered into an intra-group loan facility. Under this agreement, the Co-operative Group will make available to the Co-operative Banking Group during 2014 a term loan facility of up to £313m. This will be utilised to support the Co-operative Banking Group's undertaking to pay the Bank the 2014 capital commitment agreed as part of the December 2013 Liability Management Exercise. During the period, the Bank has received £150m in line with the 2014 Commitment Agreement.

The Co-operative Banking Group has assigned to the Bank its rights against the Co-operative Group in the event that the Co-operative Group fails to provide the Co-operative Banking Group with a loan. A security assignment in respect of the Insurance Proceeds has been entered into between the Co-operative Banking Group and the Co-operative Group as security trustee for itself and the Bank to secure the Co-operative Banking Group's Undertaking to Pay and the Co-operative Banking Group's obligations as borrower under the Intra-group Loan.

Pensions undertaking

As detailed in the 2013 Annual Report and Accounts, the Bank and the Co-operative Group have entered into an undertaking, whereby the Bank is not required to cease to participate in Pace. The parties, at the request of one of the parties, have entered into good faith discussions to reach agreement on the separation of Pace and agree the Bank's proportion of employer contributions in Pace (and if not agreed, the matter will be referred to an independent third party). These discussions are ongoing.

CFSMS transactions

Details of the CFSMS-Bank 2006 services agreement were disclosed in the 2013 Annual Report and Accounts along with the fact that the Bank and CFSMS were negotiating to replace the CFSMS-Bank 2006 Agreement with appropriate arm's length revised arrangements.

It is not now planned that this agreement will be replaced by an arm's length framework agreement until the position on CFSMS pensions liabilities in respect of Bank employees is finalised. Accordingly, the CFSMS-Bank 2006 services agreement will continue, under its terms, in the meantime.

CFSMS employees

The employment contracts of the majority of CFSMS employees who performed services to the Bank have been transferred during the first half of 2014, with a small number remaining employed by CFSMS.

Tangible and intangible assets

A number of assets were originally purchased by CFSMS using funds advanced by the Bank and then provided to the Bank by CFSMS under the 2006 CFSMS-Bank services agreement referred to above. In 2013, the Directors of the Bank concluded these assets met the accounting criteria to be shown as assets for the Bank, and therefore reported them on the balance sheet. This is referred to in more detail in the 2013 Annual Report and Accounts. The carrying value of these assets on the balance sheet at 30 June 2014 is £114.4m (31 December 2013: £127.8m).

17. Related party transactions continued

IT and other services

Pending the outcome of discussions regarding the sourcing of IT services, the Bank is not progressing the proposed revised IT Service Agreement (ITSA) and Professional Services Master Service Agreement (PSMSA) which were described in the 2013 Annual Report and Accounts. A number of service contracts under the PSMSA have now been terminated and services repatriated to the Bank, with the plan that all except pensions will be terminated by the end of 2014.

Balances with the Co-operative Group

The tables below provide an analysis of balances with the Co-operative Group and its undertakings at 30 June 2014 and 31 December 2013 and their location within the Bank's balance sheet.

	30 June 2014			
	Loans and advances to customers	**Other assets**	**Customer accounts**	**Other liabilities**
The Co-operative Group	**152.9**	**126.5**	**(130.4)**	**–**
The Co-operative Banking Group Ltd	**–**	**159.3**	**(30.4)**	**–**
Subsidiaries of the Co-operative Banking Group Ltd	**–**	**0.5**	**(77.7)**	**(71.4)**
	152.9	**286.3**	**(238.5)**	**(71.4)**

	31 December 2013			
	Loans and advances to customers	Other assets	Customer accounts	Other liabilities
The Co-operative Group	110.1	126.6	(26.7)	–
The Co-operative Banking Group Ltd	–	303.2	(49.6)	–
Subsidiaries of the Co-operative Banking Group Ltd	–	–	(16.0)	(156.5)
	110.1	429.8	(92.3)	(156.5)

18. Share capital

	Period to 30 June 2014		Period to 31 December 2013	
	No. of shares (millions)	**Share capital**	No. of shares (millions)	Share capital
Allotted, called up and fully paid (ordinary shares of 5p each)				
At the beginning of the period	**250**	**12.5**	8,200	410.0
Shares cancelled	**–**	**–**	(8,200)	(410.0)
Issue of new ordinary shares	**200**	**10.0**	250	12.5
Issue of new bonus shares	**1**	**0.1**	–	–
At the end of the period	**451**	**22.6**	250	12.5
Share premium account				
At the beginning of the period		**1,359.8**		8.8
Issue of new ordinary shares		**377.2**		1,351.0
Issue of new bonus shares		**(0.1)**		–
At the end of the period		**1,736.9**		1,359.8

In March 2014, the Bank announced a £400.0m capital raising which was completed in May 2014. This resulted in an issuance of new ordinary share capital of £10.0m and a gross increase in share premium of £390.0m. Bonus shares of £0.1m were also issued. As part of the capital raising the Bank incurred transaction costs of £12.8m. These were offset against the gross share premium amount, giving a net increase in capital of £387.2m, of which £377.1m was recorded as share premium.

The number of ordinary shares in issue at 30 June 2014 was 451,456,510 (31 December 2013: 250,000,000).

The ordinary shareholders have one vote for every share held.

All amounts are stated in £m unless otherwise indicated

19. Fair values of financial assets and liabilities

The fair values in this note are stated at a specific date and may be significantly different from the amounts which will actually be paid on the maturity or settlement dates of the instruments.

The tables below analyse the balance sheet carrying values of financial assets and liabilities by classification.

Balance sheet categories	Held for trading	Designated at fair value	Loans and receivables	Available for sale	Liabilities at amortised cost	Derivatives in a hedging relationship	Total
30 June 2014							
Assets							
Cash and balances at central banks	–	–	6,103.7	–	–	–	6,103.7
Loans and advances to banks	–	–	1,644.6	–	–	–	1,644.6
Loans and advances to customers	–	167.6	27,668.8	–	–	–	27,836.4
Fair value adjustments for hedged risk	–	–	58.0	–	–	–	58.0
Investment securities	–	1,256.7	16.0	2,925.2	–	–	4,197.9
Derivative financial instruments	365.4	–	–	–	–	75.1	440.5
Equity shares	–	–	–	5.8	–	–	5.8
Other assets	–	–	400.3	–	–	–	400.3
Total financial assets	365.4	1,424.3	35,891.4	2,931.0	–	75.1	40,687.2
Non-financial assets							389.4
Total assets							41,076.6
Liabilities							
Deposits by banks	–	–	–	–	2,136.3	–	2,136.3
Customer accounts	–	–	–	–	31,070.1	–	31,070.1
Customer accounts – capital bonds	–	388.9	–	–	–	–	388.9
Debt securities in issue	–	–	–	–	3,880.8	–	3,880.8
Derivative financial instruments	188.7	–	–	–	–	292.4	481.1
Other borrowed funds	–	–	–	–	196.3	–	196.3
Other liabilities	–	–	–	–	166.7	–	166.7
Total financial liabilities	188.7	388.9	–	–	37,450.2	292.4	38,320.2
Non-financial liabilities							641.2
Total liabilities							38,961.4
Capital and reserves							2,115.2
Total liabilities and equity							41,076.6

IAS 39 requires derivative financial instruments that are not in a hedging relationship to be classified as 'held for trading'; this definition differs from the definition of 'derivatives held for trading purposes' as shown in the Bank's 2013 Annual Report and Accounts.

All amounts are stated in £m unless otherwise indicated

19. Fair values of financial assets and liabilities continued

Balance sheet categories	Held for trading	Designated at fair value	Loans and receivables	Available for sale	Liabilities at amortised cost	Derivatives in a hedging relationship	Total
31 December 2013 (restated)							
Assets							
Cash and balances at central banks	–	–	5,418.8	–	–	–	5,418.8
Loans and advances to banks	–	–	1,594.4	–	–	–	1,594.4
Loans and advances to customers	–	134.2	30,188.0	–	–	–	30,322.2
Fair value adjustments for hedged risk	–	–	106.3	–	–	–	106.3
Investment securities	–	1,743.4	23.6	2,732.4	–	–	4,499.4
Derivative financial instruments	465.4	–	–	–	–	90.4	555.8
Equity shares	–	–	–	5.8	–	–	5.8
Other assets	–	–	480.9	–	–	–	480.9
Total financial assets	465.4	1,877.6	37,812.0	2,738.2	–	90.4	42,983.6
Non-financial assets							413.7
Total assets							43,397.3
Liabilities							
Deposits by banks	–	–	–	–	2,757.5	–	2,757.5
Customer accounts	–	–	–	–	32,463.3	–	32,463.3
Customer accounts – capital bonds	–	538.1	–	–	–	–	538.1
Debt securities in issue	–	–	–	–	4,207.6	–	4,207.6
Derivative financial instruments	191.7	–	–	–	–	346.9	538.6
Other borrowed funds	–	–	–	–	196.3	–	196.3
Other liabilities	–	–	–	–	202.9	–	202.9
Total financial liabilities	191.7	538.1	–	–	39,827.6	346.9	40,904.3
Non-financial liabilities							700.5
Total liabilities							41,604.8
Capital and reserves							1,792.5
Total liabilities and equity							43,397.3

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

19. Fair values of financial assets and liabilities continued

a) Use of financial instruments

The use of financial instruments is essential to the Bank's business activities, and financial instruments constitute a significant proportion of the Bank's assets and liabilities. The main financial instruments used by the Bank, and the purposes for which they are held, are outlined below:

Loans and advances to customers and customer accounts

The provision of banking facilities to customers is the primary activity of the Bank, and loans and advances to customers and customer accounts are major constituents of the balance sheet. Loans and advances to customers include retail mortgages, corporate loans, credit cards, unsecured retail lending and overdrafts. Customer accounts include retail and corporate current and savings accounts.

Loans and advances to banks and investment securities

Loans and advances to banks and investment securities underpin the Bank's liquidity requirements and generate incremental net interest and trading income. Held for trading investments are traded solely for short term profit.

Deposits by banks and debt securities in issue

The Bank issues medium term notes within an established Euro medium term note programme and also issues certificates of deposit and commercial paper as part of its normal treasury activities. These sources of funds, alongside other borrowed funds, are invested in marketable investment grade debt securities and short term wholesale market placements and are used to fund customer loans.

Other borrowed funds

The Bank issues unsecured and secured notes from time to time as part of its treasury activity. These sources of funds may be invested, held in cash, or used to fund customer deposits.

Derivatives

A derivative is a financial instrument that derives its value from an underlying rate or price such as interest rates, exchange rates and other market prices. Derivatives are an efficient means of managing market risk and limiting counterparty exposure. The Bank uses them mainly for hedging purposes and to meet the needs of customers.

The most frequently used derivative contracts are interest rate swaps, exchange traded futures and options, caps and floors, currency swaps and forward currency transactions.

Foreign exchange

The Bank undertakes foreign exchange dealing to facilitate customer requirements and to generate incremental income from short term trading in the major currencies.

All amounts are stated in £m unless otherwise indicated

19. Fair values of financial assets and liabilities continued

b) Valuation of financial assets and liabilities at fair value

The following tables analyse financial assets and liabilities carried at fair value by the three level fair value hierarchy defined as follows:

- Level 1 – Quoted market prices in active markets
- Level 2 – Valuation techniques using observable inputs
- Level 3 – Valuation techniques using unobservable inputs

	Fair value at end of the reporting period using:			
30 June 2014	**Level 1**	**Level 2**	**Level 3**	**Total**
Non-derivative financial assets				
Designated at fair value:				
Loans and advances to customers	**–**	**160.1**	**7.5**	**167.6**
Investment securities	**1,256.7**	**–**	**–**	**1,256.7**
Available for sale financial assets:				
Investment securities	**2,729.8**	**195.4**	**–**	**2,925.2**
Equity shares	**0.1**	**5.7**	**–**	**5.8**
Derivative financial instruments	**–**	**411.1**	**29.4**	**440.5**
Non-financial instruments				
Investment properties	**–**	**156.0**	**2.0**	**158.0**
Total assets carried at fair value	**3,986.6**	**928.3**	**38.9**	**4,953.8**
Non-derivative financial liabilities				
Designated at fair value:				
Customer accounts – capital bonds	**–**	**388.9**	**–**	**388.9**
Derivative financial instruments	**–**	**432.5**	**48.6**	**481.1**
Total liabilities carried at fair value	**–**	**821.4**	**48.6**	**870.0**

	Fair value at end of the reporting period using:			
31 December 2013	Level 1	Level 2	Level 3	Total
Non-derivative financial assets				
Designated at fair value:				
Loans and advances to customers	–	125.5	8.7	134.2
Investment securities	1,743.4	–	–	1,743.4
Available for sale financial assets:				
Investment securities	2,497.2	235.2	–	2,732.4
Equity shares	0.1	5.7	–	5.8
Derivative financial instruments	–	525.3	30.5	555.8
Non-financial instruments				
Investment properties	–	157.9	6.2	164.1
Total assets carried at fair value	4,240.7	1,049.6	45.4	5,335.7
Non-derivative financial liabilities				
Designated at fair value:				
Customer accounts – capital bonds	–	538.1	–	538.1
Derivative financial instruments	–	477.4	61.2	538.6
Total liabilities carried at fair value	–	1,015.5	61.2	1,076.7

19. Fair values of financial assets and liabilities continued

The carrying values of financial assets and liabilities measured at fair value are determined in compliance with the accounting policies in note 1 and according to the following hierarchy:

Level 1 – Quoted market prices in active markets

Financial instruments with quoted prices for identical instruments in active markets. The best evidence of fair value is a quoted market price in an actively traded market.

Level 2 – Valuation techniques using observable inputs

Financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.

The valuation techniques used to value these instruments employ only observable market data and relate to the following assets and liabilities:

Loans and advances to customers

Loans and advances to customers include corporate loans of £160.1m (31 December 2013: £125.5m) which are fair valued through income or expense using observable inputs. Loans held at fair value are valued at the sum of all future expected cash flows, discounted using a yield curve based on observable market inputs.

Investment securities – available for sale

Fair value is based on available market prices. Where this information is not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

Derivative financial instruments

Over-the-counter (ie non-exchange traded) derivatives are valued using valuation models which are based on observable market data. Valuation models calculate the present value of expected future cash flows, based upon 'no arbitrage' principles. The Bank enters into vanilla foreign exchange and interest rate swap derivatives, for which modelling techniques are standard across the industry. Examples of inputs that are generally observable include foreign exchange spot and forward rates, and benchmark interest rate curves.

Investment properties

Investment properties are carried at fair value. For those within level 2, fair value is calculated by using a mid-point of a range of valuations for the entire portfolio, index linked to the balance sheet date using the relevant regional house price index where appropriate.

Customer accounts – capital bonds

The estimated fair value of customer accounts – capital bonds is based on independent third party valuations using forecast future movements in the appropriate indices.

Equity shares

Equity shares primarily relate to investments held in Vocalink Limited which are unquoted shares. The valuation of these shares is based on the Bank's percentage shareholding and the net asset value of the company according to its most recently published financial statements.

Level 3 – Valuation techniques using unobservable inputs

This is used for financial instruments valued using models where one or more significant inputs are not observable.

The small proportion of financial assets valued based on significant unobservable inputs are analysed as follows:

Loans and advances to customers

Loans and advances to customers include 25 year fixed rate mortgages of £7.5m (31 December 2013: £8.7m) which are fair valued through income or expense using unobservable inputs. 25 year fixed rate mortgages are valued using future interest cash flows at the fixed customer rate and estimated schedule of customer repayments. Cash flows are discounted at a credit adjusted discount rate; the credit adjustment is based on the average margin of new long dated (five years or greater) fixed rate business written in the last six months, and subject to quarterly review. The eventual timing of future cash flows may be different from that forecast due to unpredictable customer behaviour, particularly on a 25 year product. The valuation methodology takes account of credit risk and has increased the valuation by £nil in 2014 (31 December 2013: £0.8m increase). A reasonable change in the assumptions would not result in any material change in the valuation.

All amounts are stated in £m unless otherwise indicated

19. Fair values of financial assets and liabilities continued

Derivative financial instruments

Derivative financial instruments in the form of interest rate swaps have been entered into between the Bank and its subsidiaries, and external counterparties.

The purpose of the swaps is to convert the SVR and base rate linked revenue receipts of the pool of mortgage assets to the same LIBOR linked basis as the intercompany loan. Under this swap arrangement the Bank's subsidiaries pay to the swap counterparty, the monthly SVR and base rate linked revenue receipts of the pool of assets and receives from the swap counterparty LIBOR plus a contractual spread on the same notional balance. The Bank has a 'back to back' swap that is the mirror image of the subsidiaries' swaps.

The swaps are valued based on an assumed amortisation profile of the pool of assets to the bond maturity date (assuming some annual prepayment), an assumed profile of customer receipts over this period, and LIBOR prediction using forward rates. Swap cash flows are discounted to present value using mid-yield curve zero coupon rates.

Investment properties

Investment properties within level 3 are valued by taking the original price, index linked to the balance sheet date using the relevant house price index.

Movements in fair values of instruments with significant unobservable inputs (level 3) were:

	Fair value at the beginning of the year	Purchases and transfers in	Sales and transfers out	Income or expense including impairment	Fair value at the end of the period
30 June 2014					
Loans and advances to customers	**8.7**	**–**	**(1.0)**	**(0.2)**	**7.5**
Derivative assets	**30.5**	**0.7**	**(0.1)**	**(1.7)**	**29.4**
Derivative liabilities	**(61.2)**	**(0.7)**	**0.1**	**13.2**	**(48.6)**
Investment properties	**6.2**	**–**	**(4.3)**	**0.1**	**2.0**
	(15.8)	**–**	**(5.3)**	**11.4**	**(9.7)**
31 December 2013					
Loans and advances to customers	11.2	–	(1.7)	(0.8)	8.7
Derivative assets	35.4	12.6	(22.6)	5.1	30.5
Derivative liabilities	(12.4)	(52.0)	0.6	2.6	(61.2)
Investment properties	173.0	–	(166.6)	(0.2)	6.2
	207.2	(39.4)	(190.3)	6.7	(15.8)

During the prior period, the methodology for calculating the fair value of investment properties was amended as explained in the Bank's 2013 Annual Report and Accounts. During the current period, investment properties totalling £4.3m were transferred from level 3 to level 2. The transfer was made following identification of third party pricing information. The majority of investment property meets the level 2 fair value hierarchy.

All amounts are stated in £m unless otherwise indicated

19. Fair values of financial assets and liabilities continued

c) Fair values of financial assets and liabilities not carried at fair value

The carrying values of financial instruments measured at amortised cost are determined in compliance with the accounting policies in note 1.

The table below sets out a summary of the carrying and fair values of:

- financial assets classified as loans and receivables; and
- financial liabilities classified as held at amortised cost,

unless there is no significant difference between carrying and fair values.

	Carrying value	Fair value	Difference
30 June 2014			
Financial assets			
Loans and receivables			
Loans and advances to banks	**1,644.6**	**1,643.7**	**(0.9)**
Loans and advances to customers	**27,668.8**	**25,836.0**	**(1,832.8)**
Fair value adjustments for hedged risk	**58.0**	**58.0**	**–**
Investment securities	**16.0**	**15.6**	**(0.4)**
Other assets	**400.3**	**400.3**	**–**
Financial liabilities			
Financial liabilities at amortised cost			
Deposits by banks	**2,136.3**	**2,136.2**	**(0.1)**
Customer accounts	**31,070.1**	**31,065.7**	**(4.4)**
Debt securities in issue	**3,880.8**	**4,319.0**	**438.2**
Other borrowed funds	**196.3**	**243.3**	**47.0**
Other liabilities	**166.7**	**166.7**	**–**

	Carrying value	Fair value	Difference
31 December 2013 (as restated)			
Financial assets			
Loans and receivables			
Loans and advances to banks	1,594.4	1,594.4	–
Loans and advances to customers	30,188.0	27,813.0	(2,375.0)
Fair value adjustments for hedged risk	106.3	106.3	–
Investment securities	23.6	21.4	(2.2)
Other assets	480.9	480.9	–
Financial liabilities			
Financial liabilities at amortised cost			
Deposits by banks	2,757.5	2,757.4	(0.1)
Customer accounts	32,463.3	32,488.3	25.0
Debt securities in issue	4,207.6	4,714.9	507.3
Other borrowed funds	196.3	234.2	37.9
Other liabilities	202.9	202.9	–

19. Fair values of financial assets and liabilities continued

Key considerations in the calculation of fair values for loans and receivables and financial liabilities at amortised cost are as follows:

Loans and advances to banks/deposits by banks

Loans and advances to banks include interbank placements and items in the course of collection.

The amortised cost value of all loans and advances to banks are deemed to be a close approximation of their fair value due to their short maturity. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money market interest rates for debts with similar credit risk and remaining maturity.

Loans and advances to customers

The fair value of loans and advances to customers is calculated by segmenting the overall balance into Retail, Optimum and Corporate.

i. Retail and Optimum

Fair values have been calculated using an origination spread income approach. Under this approach, value is measured by determining discounted expected cashflows, derived using redemption profiles, from the portfolio and applying an origination spread which reflects the difference between current market rates for products with similar characteristics and risk profiles and the actual rates the portfolio is generating. The discount rates applied to the expected cash flows reflect the underlying risk of the portfolios.

ii. Corporate

As part of the implementation of the Bank's strategy for Non-core assets, certain assets have either already been sold after the period end or plans to sell are well advanced. For these assets, the fair value can therefore be determined from the actual sale price achieved or expected to be received.

For other corporate assets an expected cashflow income approach has been used. Under this approach, value is measured by determining expected cashflows, derived using redemption profiles from the portfolio and then considering credit costs, funding costs and tax to derive cash flows which are discounted at an appropriate blended cost of capital. The discount rates applied to the expected cash flows reflect the underlying risk of the portfolios.

The fair value of loans and advances to customers is 93% of the carrying value as at 30 June 2014 (31 December 2013: 92%). The overall fair values are less than par primarily due to two main factors for Non-core loans in particular:

1. Customer interest rates are below the market rate at the balance sheet date until expected maturity or the repricing date, if earlier; and

2. Credit risk adjustments due to incurred and expected future credit losses.

Investment securities

Fair value is based on available market prices. Where this information is not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

Customer accounts

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest bearing deposits and other borrowings without quoted market prices is based on future interest cash flows (at funding rates) and principal cash flows, discounted using an appropriate market rate.

All amounts are stated in £m unless otherwise indicated

19. Fair values of financial assets and liabilities continued

Debt securities in issue and other borrowed funds

The aggregate fair values are calculated based on quoted market prices. For those notes where quoted market prices are not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics. Quoted prices may be from inactive markets.

The fair value of debt securities in issue is significantly above the carrying value as a result of the carrying value being net of merger fair value adjustments. The carrying values of debt securities in issue are expected to increase as the merger fair value adjustments continue to unwind, as shown in the following section.

Unwind of merger fair value adjustments

On the merger of the Bank and Britannia Building Society in August 2009 an exercise was undertaken to fair value the respective assets and liabilities of Britannia Building Society. These fair value adjustments are unwound on an EIR basis over the effective lives of the assets and liabilities. As at 30 June 2014, the remaining merger fair value unwinds and the forecast unwind profiles can be summarised as follows:

				Forecast Unwind			
	Carrying amount at period end	Remaining merger fair value to be unwound at period end	Actual unwind for the 6 month period to 30 June 2014	2014	2015	2016	2017+
Assets							
Loans and advances to customers	27,836.4	(34.2)	(8.5)	(2.1)	(3.1)	(2.9)	(22.7)
Fair value adjustment for hedged risk	58.0	(30.3)	(7.3)	(3.0)	(4.4)	(3.6)	(19.3)
Other	13,182.2	20.4	2.6	2.3	4.6	4.6	17.6
Total assets	**41,076.6**	**(44.1)**	**(13.2)**	**(2.8)**	**(2.9)**	**(1.9)**	**(24.4)**
Liabilities							
Debt securities in issue	3,880.8	447.3	53.8	60.0	148.7	179.6	58.9
Deferred tax liabilities	77.8	(82.6)	–	–	–	–	–
Other	35,002.8	(9.0)	0.4	–	–	–	–
Total liabilities	**38,961.4**	**355.7**	**54.2**	**60.0**	**148.7**	**179.6**	**58.9**

A breakdown of the unwind on debt securities in issue held at merger is as follows:

							Forecast Unwind			
Issue Name	Issue Date	Contractural Maturity Date	Carrying amount at period end	Fair value at period end	Remaining merger fair value to be unwound at period end	Actual unwind for the 6 month period to 30 June 2014	2014	2015	2016	2017
Leek Finance Number Seventeen plc	April 2006	June 2016	597.2	599.1	98.8	17.3	19.8	48.7	30.3	–
Leek Finance Number Eighteen plc	October 2006	December 2016	729.0	724.5	147.8	19.0	21.4	52.6	73.8	–
Leek Finance Number Nineteen plc	April 2007	June 2017	717.4	715.4	210.7	16.8	19.6	50.9	79.9	60.3
Total Leek Notes			**2,043.6**	**2,039.0**	**457.3**	**53.1**	**60.8**	**152.2**	**184.0**	**60.3**

Of which liabilities held internally within the Bank are as follows:

							Forecast Unwind			
Issue Name	Issue Date	Contractural Maturity Date	Carrying amount at period end	Fair value at period end	Remaining merger fair value to be unwound at period end	Actual unwind for the 6 month period to 30 June 2014	2014	2015	2016	2017
Internally Held Leek Notes			557.8	539.9	10.7	2.1	2.1	4.1	3.6	0.9

All amounts are stated in £m unless otherwise indicated

19. Fair values of financial assets and liabilities continued

Fair values of financial assets and liabilities which are not carried at fair value and bases of valuation

Fair values are determined according to the hierarchy set out on page 91.

	Carrying value	Level 1	Level 2	Level 3
30 June 2014				
Financial assets				
Loans and receivables				
Loans and advances to customers	**27,668.8**	**–**	**–**	**25,836.0**
Fair value adjustment for hedged risk	**58.0**	**–**	**–**	**58.0**
Investment securities	**16.0**	**15.6**	**–**	**–**
Financial liabilities				
Financial Liabilities at amortised cost				
Customer accounts	**31,070.1**	**–**	**31,065.7**	**–**
Debt securities in issue	**3,880.8**	**844.4**	**3,474.6**	**–**
Other borrowed funds	**196.3**	**–**	**243.3**	**–**

	Carrying value	Level 1	Level 2	Level 3
31 December 2013 (as restated)				
Financial assets				
Loans and receivables				
Loans and advances to customers	30,188.0	–	–	27,813.0
Fair value adjustment for hedged risk	106.3	–	–	106.3
Investment securities	23.6	21.4	–	–
Financial liabilities				
Financial liabilities at amortised cost				
Customer accounts	32,463.3	–	32,488.3	–
Debt securities in issue	4,207.6	892.5	3,810.1	–
Other borrowed funds	196.3	–	234.2	–

The carrying amount is a reasonable approximation of fair value for the following assets and liabilities; loans and advances to banks, fair value adjustments for hedged risk, other assets, deposits by banks and other liabilities.

All amounts are stated in £m unless otherwise indicated

19. Fair values of financial assets and liabilities continued

d) Fair value of transferred assets and associated liabilities

Securitisation vehicles

The beneficial ownership of the loans and advances to customers sold to securitisation vehicles by the subsidiaries of the Bank fail the derecognition criteria, and consequently, these loans remain on the balance sheets of the sellers. Each seller therefore recognises a deemed loan financial liability on its balance sheet and an equivalent deemed loan asset is held on each securitisation company's balance sheet. The deemed loans are repaid as and when principal repayments are made by customers against these transferred loans and advances.

The securitisation vehicles have issued fixed and floating rate notes which are secured on the loans and advances to customers. The notes are redeemable in part from time to time, such redemptions being limited to the net capital received from mortgagers in respect of the underlying mortgages.

The Bank retains substantially all of the risks and rewards of ownership. The Bank benefits to the extent to which surplus income generated by the transferred mortgage portfolios exceeds the administration costs of those mortgages. The Bank continues to bear the credit risk of the underlying mortgages.

The results of the securitisation vehicles are consolidated into the results of the Bank. The table below shows the carrying values and fair values of the assets transferred to securitisation vehicles and their associated liabilities. The carrying values presented below are the carrying amounts as recorded in the books of the subsidiary companies, some of these issued notes are held internally by the Company and as such are not shown in the consolidated balance sheet of the Bank.

	Carrying amount of transferred assets not derecognised	Carrying amount of associated liabilities	Fair value of transferred assets not derecognised	Fair value of associated liabilities	Net position
30 June 2014					
Leek Finance Number Seventeen plc	**570.9**	**597.2**	**502.2**	**599.1**	**(96.9)**
Leek Finance Number Eighteen plc	**684.7**	**729.0**	**603.8**	**724.5**	**(120.7)**
Leek Finance Number Nineteen plc	**662.0**	**717.4**	**583.8**	**715.4**	**(131.6)**
Leek Finance Number Twenty plc	**1,394.8**	**1,369.8**	**1,171.0**	**1,338.4**	**(167.4)**
Leek Finance Number Twenty One plc	**806.3**	**818.4**	**735.1**	**764.5**	**(29.4)**
Leek Finance Number Twenty Two plc	**364.4**	**380.3**	**300.7**	**358.1**	**(57.4)**
Silk Road Finance Number One plc	**1,304.8**	**1,314.6**	**1,226.6**	**1,315.3**	**(88.7)**
Silk Road Finance Number Two plc	**473.8**	**482.3**	**470.0**	**457.1**	**12.9**
Silk Road Finance Number Three plc	**514.5**	**526.9**	**499.0**	**533.8**	**(34.8)**
Cambric Finance Number One plc	**1,056.2**	**1,097.7**	**1,145.4**	**1,070.0**	**75.4**
Meerbrook Finance Number Eight Ltd	**636.3**	**640.6**	**604.2**	**608.0**	**(3.8)**
	8,468.7	**8,674.2**	**7,841.8**	**8,484.2**	**(642.4)**

The above carrying amount of associated liabilities can be reconciled to debt securities in issue, as follows:

	Carrying value
Carrying amount of associated liabilities as given above	**8,674.2**
Internally held fixed and floating rate notes	**(5,296.9)**
Loan facilities and subdebt not included in debt securities in issue	**(606.4)**
Non securitised debt securities	**1,586.4**
Merger fair value adjustment	**(447.3)**
Other adjustments	**(29.2)**
Debt securities in issue per financial liabilities	**3,880.8**

All amounts are stated in £m unless otherwise indicated

19. Fair values of financial assets and liabilities continued

Of the notes listed above, those held by the Bank are as follows:

	Carrying amount of transferred assets not derecognised	Carrying amount of associated liabilities	Fair value of transferred assets not derecognised	Fair value of associated liabilities	Net position
30 June 2014					
Leek Finance Number Seventeen plc	**151.7**	**158.7**	**133.5**	**154.4**	**(20.9)**
Leek Finance Number Eighteen plc	**186.7**	**198.8**	**164.7**	**189.1**	**(24.4)**
Leek Finance Number Nineteen plc	**184.8**	**200.3**	**163.0**	**196.4**	**(33.4)**
Leek Finance Number Twenty plc	**1,394.8**	**1,369.8**	**1,171.0**	**1,338.4**	**(167.4)**
Leek Finance Number Twenty One plc	**806.3**	**818.4**	**735.1**	**764.5**	**(29.4)**
Leek Finance Number Twenty Two plc	**364.4**	**380.3**	**300.7**	**358.1**	**(57.4)**
Silk Road Finance Number One plc	**809.3**	**815.4**	**760.8**	**812.8**	**(52.0)**
Silk Road Finance Number Two plc	**154.6**	**149.6**	**153.3**	**147.2**	**6.1**
Silk Road Finance Number Three plc	**105.5**	**108.0**	**102.3**	**107.7**	**(5.4)**
Cambric Finance Number One plc	**1,056.2**	**1,097.7**	**1,145.4**	**1,070.0**	**75.4**
Meerbrook Finance Number Eight Ltd	**–**	**–**	**–**	**–**	**–**
	5,214.3	**5,297.0**	**4,829.8**	**5,138.6**	**(308.8)**

The above carrying value and fair value of assets held for each entity have been determined by applying the proportion of internally held liabilities.

Transferred assets include securitised gilts and loans and advances to customers that have not been derecognised by the seller. The associated liabilities include the fixed and floating rate notes, bank loans and intercompany loans that specifically relate to the funding for the assets securitised.

The difference between the fair value and carrying value of the mortgage assets that have been securitised within Leek 17, 18, and 19 is significantly higher than the fair value to carrying value difference for the associated liabilities. This is because it is expected that the note liabilities will be repaid before most of the underlying mortgages – which will continue to be held on the Bank's balance sheet for a significant period after the notes have repaid. These mortgages typically have an interest rate which is below the equivalent market rate at the balance sheet date for loans of similar nature.

The securitisation vehicles receive cash daily in relation to the transferred loans and advances and semi-annually for the transferred gilts. These amounts are held within loans and advances to banks until the associated liabilities' payments are due. Payments are made quarterly for all associated liabilities except for the variable funding notes associated with the transferred gilts, which are paid semi-annually. The amounts held within loans and advances to banks are not included in the table above but will be used in part to cover the repayments made on the associated liabilities.

	Carrying amount of transferred assets not derecognised	Carrying amount of associated liabilities	Fair value of transferred assets not derecognised	Fair value of associated liabilities	Net position
31 December 2013					
Leek Finance Number Seventeen plc	588.8	624.6	490.9	619.4	(128.5)
Leek Finance Number Eighteen plc	703.1	762.5	592.3	748.1	(155.8)
Leek Finance Number Nineteen plc	680.5	749.6	573.0	737.1	(164.1)
Leek Finance Number Twenty plc	1,438.2	1,413.3	1,135.1	1,364.0	(228.9)
Leek Finance Number Twenty One plc	850.1	864.1	770.1	784.6	(14.5)
Leek Finance Number Twenty Two plc	372.6	389.0	309.1	356.0	(46.9)
Silk Road Finance Number One plc	1,466.4	1,481.2	1,466.4	1,486.3	(19.9)
Silk Road Finance Number Two plc	562.0	561.1	562.5	563.4	(0.9)
Silk Road Finance Number Three plc	583.1	597.9	584.2	604.6	(20.4)
Cambric Finance Number One plc	1,339.8	1,384.5	1,238.8	1,310.9	(72.1)
Meerbrook Finance Number Eight Ltd	625.9	635.8	616.1	601.4	14.7
	9,210.5	9,463.6	8,338.5	9,175.8	(837.3)

All amounts are stated in £m unless otherwise indicated

19. Fair values of financial assets and liabilities continued

Covered Bond Limited Liability Partnerships

Moorland Covered Bonds LLP was originally established to enable a £1.4bn retained covered bond issuance. Loans and advances to customers of £1.9bn were transferred to Moorland Covered Bonds LLP. The transfer was funded by a loan of £1.4bn and capital contribution of £0.5bn. Following the attainment of regulated covered bond status there was a public issuance of notes in November 2011 totalling £0.6bn. At the period end the Bank held a loan of £0.6bn (31 December 2013: £0.6bn) and a capital contribution of £0.7bn (31 December 2013: £0.9bn) with Moorland Covered Bonds LLP.

Moorland Covered Bonds LLP does not have ordinary share capital. The Bank's interest in Moorland Covered Bonds LLP is in substance no different from a wholly owned subsidiary and consequently it is fully consolidated in the Bank accounts. The table below shows the carrying values and fair values of the assets transferred to the covered bond and their associated liabilities:

	Carrying amount of transferred loans and advances to customers	**Carrying amount of fixed and floating rate notes**	**Fair value of transferred loans and advances to customers**	**Fair value of fixed and floating rate notes**	**Net position**
30 June 2014					
Moorland Covered Bonds LLP	**1,274.0**	**596.3**	**1,264.2**	**642.7**	**621.5**

	Carrying amount of transferred loans and advances to customers	Carrying amount of fixed and floating rate notes	Fair value of transferred loans and advances to customers	Fair value of fixed and floating rate notes	Net position
31 December 2013					
Moorland Covered Bonds LLP	1,448.8	596.1	1,417.9	628.4	789.5

Assets pledged

Assets are pledged as collateral under repurchase agreements with other banks. These deposits are not available to finance the Bank's day-to-day operations.

	Carrying amount of assets not derecognised	**Carrying amount of associated liabilities**	**Fair value of assets not derecognised**	**Fair value of associated liabilities**	**Net position**
30 June 2014					
Investment securities sold under repurchase agreements	**896.1**	**904.1**	**899.1**	**904.1**	**(5.0)**

	Carrying amount of assets not derecognised	Carrying amount of associated liabilities	Fair value of assets not derecognised	Fair value of associated liabilities	Net position
31 December 2013					
Investment securities sold under repurchase agreements	1,004.4	1,028.3	1,022.5	1,028.3	(5.8)

Associated liabilities are included within deposits by banks.

20. Post balance sheet events

It is a requirement of IAS 10 (Events after the balance sheet date) that these financial statements reflect events arising after the 30 June 2014. The following events have occurred between 30 June 2014 and 21 August 2014 (the date of approval of the Interim Financial Report 2014) and represent 'non adjusting' post balance sheet events:

On 25 July 2014 the Bank gave notice that Silk Road Finance Two Plc will redeem all outstanding notes at their then principal amount outstanding together with accrued interest on 22 September 2014. As at 23 June 2014, £0.3bn of 'Silk 2' class A notes were outstanding.

On 25 July 2014 the Bank announced the planned closure of a further 25 branches by the end of 2014. This would result in a further provision of £5.2m.

Glossary
For the period ended 30 June 2014

The following glossary defines terminology used within the Bank's Interim Financial Report to assist the reader and to facilitate comparison with publications by other financial institutions:

Terminology	Definition
Almost prime	Almost prime lending is lending to borrowers with very low levels of adverse credit history.
Arrears	Customers are said to be in arrears or non-performing when they are behind in fulfilling their obligations with the result that an outstanding loan is unpaid or overdue. Corporate customers may also be considered non-performing prior to being behind in fulfilling their obligations. This can happen when a significant restructuring exercise begins.
Automated Valuation Model (AVM)	A valuation model used specifically for low loan to value (LTV) remortgages. Performance of AVMs is monitored on a regular basis to ensure their ongoing accuracy.
Banking Group	The Co-operative Banking Group Ltd and its subsidiaries, which included the Bank until legal separation occurred on 20 December 2013.
Basel II	A statement of best practice issued by the Basel Committee on Banking Supervision, 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.
Basel III	A strengthening of the requirements laid out in Basel II, to be phased into the Bank from 2014 ahead of full implementation by 2022. Basel III is implemented within the European Union (including the UK) through CRD IV.
Basis points (bps)	One hundredth of a percent (0.01%), so 100 basis points is 1%. Used in quoting movements in interest rates or yields on securities.
BIPRU	The prudential sourcebook for banks, building societies and investment firms which sets out the PRA's requirements for capital and liquidity.
BaCB (Business and Commercial Banking)	The core segment of the Bank which specialises in lending to businesses.
Buy-to-let	A commercial practice of buying a property to let to tenants, rather than to live in.
Capital bonds	Fixed term customer accounts with returns based on the movement in an index (eg FTSE 100) over the term of the bond.
Capital ratio	Total of Tier 1 capital plus Tier 2 capital, all divided by risk weighted assets.
Capital Requirements Directive (CRD IV)	This encompasses both the Capital Requirements Directive and Capital Requirements Regulation (CRR) as well as the PRA's Policy Statement PS7/13: Strengthening capital standards. CRD IV implements Basel III within the European Union (including the UK) and is a strengthening of the requirements laid out in Basel II.
Capital resources	Capital held, allowable under regulatory rules, less certain regulatory adjustments and deductions that are required to be made. Capital includes retained earnings, share premium and minority interests.
Carrying value	The value of an asset or liability as it appears in the balance sheet. For each asset or liability, the value is based on either of the amortised cost or fair value principles.
Certificates of deposit (CDs)	Debt issued by banks, savings and loan associations to individual investors with terms ranging from a few months to several years. Longer term CDs tend to bear a higher interest rate. At the expiration of the term, investors may (subject to penalties) withdraw both the principal and the accrued interest.
CFS Management Services Ltd (CFSMS)	CFS Management Services Ltd (CFSMS) provides supplies and services on behalf of subsidiary undertakings within the Co-operative Banking Group.
Charged off	When all economical avenues to recover an unsecured debt have been exhausted, the Bank permanently closes the loan account, ie it is charged off. This final step sits at the end of a time frame within which the Bank attempts to manage the debt's recovery and differs from a 'write down' in terms of its fixed position in time (see Write down).
Collateral	A borrower's pledge, usually a property, which acts as security for repayment of the loan (see Secured lending).
Collateralised swap	A swap, whose volatility is secured (collateralised) by way of exchanging cash deposits (see Swaps).
Colleague engagement	An internal survey, measuring the level of the Bank's employees' engagement.
Collectively assessed for impairment	Impairment is measured collectively where a portfolio comprises assets with a homogenous risk and where appropriate statistical techniques are available.
Commercial Paper	An unsecured promissory note issued to finance short term credit needs. It specifies the face amount paid to investors on the maturity date.
Commercial real estate	Commercial real estate includes office buildings, industrial property, malls, retail stores, shopping centres, multifamily housing buildings, warehouses, and industrial properties.

For the period ended 30 June 2014

Terminology	Definition
Common Equity Tier 1	A CRD IV regulatory measure of financial (capital) strength. Common Equity Tier 1 capital is the highest quality of capital and comprises share capital and associated share premium, and general reserves from retained profits. The book values of goodwill and intangible assets as well as other regulatory adjustments, including the full amount of expected loss over provisions, are deducted from Common Equity Tier 1 capital for the purposes of capital adequacy.
Conduct risk	The risk that the Bank's behaviours, offerings or interactions will result in unfair outcomes for customers.
Contagion risk	An international financial market term which describes a corrupting or harmful influence, spreading effects of shocks from one counterparty to another.
Co-operative Asset Management (CoAM)	The segment that comprises Non-core assets managed for run down or exit.
Co-operative Banking Group (CBG)	The Co-operative Banking Group Ltd and its subsidiaries, which included the Bank until legal separation occurred on 20 December 2013.
Core business	Lines of business that are consistent with the Bank's strategy and risk appetite.
Corporate core segment	The segment that comprises corporate banking, business banking and business services in line with the Bank's strategy and risk appetite.
Cost of risk	Impairment charges (amounts provided for non-performing loans) expressed as a percentage of average loans during the year.
Cost to income ratio	Operating expenses divided by operating income.
Counterparty	In any financial contract, the person or institution entering the contract on the opposite side of the transaction is called a counterparty.
Covered bonds	Debt securities backed by a portfolio of mortgages that are segregated from the issuer's other assets solely for the benefit of the holders of the covered bonds. The Bank issues covered bonds as part of its funding activities.
Credit default swap	An arrangement whereby the credit risk of an asset (the reference asset) is transferred from the buyer to the seller of protection. A credit default swap is a contract where the protection seller receives premium or interest related payments in return for contracting to make payments to the protection buyer upon a defined credit event. Credit events normally include bankruptcy, payment default on a reference asset or assets, or downgrades by a credit rating agency.
Credit impairment	Impairment charges on loans and advances to customers.
Credit risk	The current or prospective risk 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.
Currency swap	An arrangement in which two parties exchange specific principal amounts of different currencies at inception and subsequently interest payments on the principal amounts. Often one party will pay a fixed rate of interest, while the other will pay a floating rate (though there are also fixed-fixed and floating-floating arrangements). At the maturity of the swap, the principal amounts are usually re-exchanged.
Credit valuation adjustments (CVAs)	Adjustments to the fair values of derivative assets to reflect the creditworthiness of the counterparty.
Customer deposits	Money deposited by all individuals and companies that are not credit institutions. Such funds are recorded as liabilities in the Bank's balance sheet under customer accounts or financial liabilities designated at fair value.
Customer funding ratio	Customer deposits divided by customer loans. This is the reverse equation of the customer loan to deposit ratio (see Customer loan to deposit ratio).
Customer loan to deposit ratio	Customer loans divided by customer deposits. This is the reverse equation of the customer funding ratio (see Customer funding ratio).
Debt securities in issue	Transferable certificates of indebtedness of the Bank to the bearer of the certificates. These are liabilities of the Bank and include certificates of deposit, commercial paper and fixed and floating rate notes.
Default	Circumstances in which the probability of default is taken at 100% for the purposes of the calculation of regulatory capital and compliance with Basel II. This is defined as when a borrower reaches a predefined arrears status where a borrower is considered unlikely to repay the credit obligation in full without the lender taking action.
Deleverage the balance sheet	Strategic reduction of the Bank's risk asset base leading to improved capital management.
Delinquency	A customer in arrears is also said to be in a state of delinquency. When a customer is in arrears, their entire outstanding balance is said to be delinquent, meaning that delinquent balances are the total outstanding loans on which payments are overdue (see Arrears).
Derivative	A financial instrument that has a value, based on the expected future price movements of the instrument to which it is linked, such as a share or a currency.

For the period ended 30 June 2014

Terminology	Definition
Effective interest rate method (EIR)	The method used to measure the carrying value of certain financial assets or liabilities and to allocate associated interest income or expense over the relevant period.
Encumbrance	Encumbrance is an impediment to use of assets, for example a claim against a property by another party. Encumbrance usually impacts the transferability of the asset and restrict its free use until the encumbrance is removed.
Ethical Policy	A method developed since 1992 by which the Bank engages with its customers in relation to ethics.
Eurozone	The geographical area containing countries whose economies function using the European single currency.
Expected charge off rate	The expected level of a portfolio's loans that may be written off as bad debt.
Expected loss	A measure of anticipated loss for exposures captured under an internal ratings based credit risk approach. The expected loss amount is the exposure from a potential default of a counterparty or dilution over a one year period to the amount outstanding at default.
Exposure at default (EAD)	A Basel II Pillar 1 parameter the amount estimated to be outstanding at the time of default – EAD calculated under the standardised approach is always reported post credit conversion factors and provisions. Under the IRB approach the EAD includes undrawn commitments after credit conversion factors.
External audit	An independent opinion, by an external firm, on the Bank and Company's financial statements.
External credit rating	A financial indicator of risk, assigned by credit rating agencies, to potential investors in the Bank.
Fair value adjustments	Fair value adjustments are the remaining balance sheet adjustments for the assets/liabilities acquired on the merger of the Bank and Britannia Building Society on 1 August 2009.
Fair value amortisation	The amortisation of the remaining interest risk related fair value adjustments for the assets/liabilities acquired on the merger of the Bank and Britannia Building Society on 1 August 2009 (see Interest rate risk).
Financial Conduct Authority (FCA)	The FSA was replaced as the UK's financial regulator on 1 April 2013 by two new regulatory bodies: the PRA and the FCA. The FCA is responsible for the regulation of conduct in retail, as well as wholesale, financial markets and the infrastructure that supports those markets.
Financial instruments	Any document with monetary value. Examples include cash and cash equivalents, but also securities such as bonds and stocks which have value and may be traded in exchange for money.
Financial Services Authority (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 Compensation Scheme (FSCS)	The UK's compensation fund of last resort for customers of authorised financial services firms. The FSCS may pay compensation to customers if a firm is unable, or likely to be unable, to pay claims against it, usually because it has stopped trading or has been declared in default. The FSCS is funded by the financial services industry. Every firm authorised by the PRA is obliged to pay an annual levy, which goes towards its running costs and compensation payments.
Floating rate notes (FRNs)	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.
Forbearance	The Bank, for reasons relating to the actual or apparent financial stress of a borrower, grants a concession whether temporarily or permanently to that borrower. A concession may involve restructuring the contractual terms of a debt (such as an extension of the maturity date or any weakening of the security structure or adjustment/non enforcement of covenants) or payment in some form other than cash, such as an equity interest in the borrower.
Foreclosure	The legal process by which a lender, eg the Bank, obtains a court order in order to terminate a borrower's equitable right of redemption. This legal action is required when a borrower has materially failed to comply with the agreed terms and conditions of the loan, eg by defaulting (see Forbearance).
Forward rate agreement	A legal contract, governing the terms and conditions of a forward or future, in which the buyer pays a fixed rate of interest to the seller in return for the seller's floating rate (see Forwards, Futures and Swaps).
Forwards	Non-standardised contracts, traded over the counter, between two parties to buy or sell financial instruments at a specified future time at a price agreed today (see Over The Counter).
Funding for Lending	The Bank of England and HM Treasury launched the Funding for Lending Scheme (FLS) on 13 July 2012. It is designed to boost lending to households and businesses. It works by allowing participating banks and building societies to borrow from the Bank of England for up to four years. As security against that lending, participating banks will provide assets, such as business or mortgage loans, to the Bank of England. Banks were able to borrow during the 18 months from 1 August 2012 until 31 January 2014.
Futures	Standardised contracts, traded on an exchange, between two parties to buy or sell financial instruments at a specified future time at a price agreed today.

For the period ended 30 June 2014

Terminology	Definition
Gap	The Bank's net exposure to variable elements being managed within its market risk, eg interest rate movements (see Market risk).
Hedging	A technique used by the Bank to offset risks on one instrument by purchasing a second instrument that is expected to perform in the opposite way.
Impaired loans	Loans where the Bank does not expect to collect all the contractual cash flows or expects to collect them later than they are contractually due.
Impairment allowance	A loss allowance held on the balance sheet as a result of the raising of a charge against profit for the incurred loss inherent in the lending book. An impairment loss allowance may be either individual or collective.
Individual Capital Guidance (ICG)	The PRA's statement as to the regulatory capital it expects the Bank to hold.
Individual Liquidity Adequacy Assessment (ILAA)	The Bank's assessment of its liquidity risks, controls and quantification of liquid assets required to survive severe financial shocks through the use of stress tests prescribed by the PRA (see Liquidity risk).
Individual Liquidity Guidance (ILG)	A PRA guidance on the required amount and composition of the liquid assets buffer that should be held by a firm. This guidance arises once the firm's Individual Liquidity Adequacy Assessment (ILAA) has been conducted.
Individually assessed for impairment	Impairment is measured individually for assets that are individually significant.
Individually significant	Large value loans that exceed a balance threshold established by the Bank, above which it is deemed appropriate to impair accounts on an individual basis.
Interest rate risk	The variability in value borne by an interest bearing asset, such as a loan or a bond, due to variability of interest rates. In general, as rates rise, the price of a fixed rate bond will fall, and vice versa.
Internal audit	The examination of the Company's records and reports by its employees. Internal audits are usually intended to prevent fraud and to ensure compliance with Board directives and management policies.
Internal Capital Adequacy Assessment Process (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.
Internal rating grade (IRG)	The grading of credit risk resulting from the internal ratings based approach (IRB).
Internal ratings based approach (IRB)	A Basel II approach for measuring exposure to credit risks. IRB approaches are more sophisticated and risk sensitive than the Standardised Approach and may be Foundation or Advanced. IRB approaches may only be used with PRA permission.
Investment grade	A debt security, treasury bill or similar instrument with a credit rating measured by external agencies of AAA to BBB.
Legal separation	The process by which the Bank was legally separated from the Co-operative Group.
Leverage ratio	A CRD IV measure, calculated as the ratio of Tier 1 capital to total exposures. Total exposures include on-balance sheet items, off-balance sheet items and derivatives. The leverage ratio is a supplementary measure to the risk-based capital requirements and is intended to constrain the build-up of excess leverage in the banking sector.
Liability Management Exercise (LME)	The process by which the Bank successfully raised c.£1.2bn of capital in 2013. This was effected by the transfer of preference shares and extinguishment of multiple subordinated liabilities, followed by the recognition of a single tranche of subordinated debt.
LIBOR (London Interbank Offered Rate)	The interest rate participating banks offer to other banks for loans on the London market.
Lifetime expected loss	The losses that the Bank expects to incur over the lifetime of portfolios of mortgage assets which were acquired on merger with Britannia Building Society. This is different from expected loss (see Expected loss) which is based on assets expected to default in the next 12 months.
Limited Liability Partnership (LLP)	An LLP provides each of its individual partners protection against personal liability for certain partnership liabilities.
Liquid Asset Buffer (LAB)	A range of assets from which the Bank can manage its liquidity risk. These assets have relatively short maturity dates.
Liquidity and funding risk	The risk that the Bank's resources will prove inadequate to meet its liabilities as they contractually fall due or as a result of any contingent or discretionary cash outflows that may occur in times of stress. It arises from mismatch of timings of cash flows generated from the Bank's assets and liabilities (including derivatives).
Loan to value (LTV)	A ratio which expresses the amount of a mortgage as a percentage of the value of the property. The Bank calculates residential mortgage LTV on an indexed basis (the value of the property is updated on a quarterly basis to reflect changes in the house price index (HPI)).
Loss emergence period	The time taken, expressed in months, for a loss event on a loan to become observed by the Bank.

For the period ended 30 June 2014

Terminology	Definition
Loss given default	An estimate of the actual loss that would occur in the event of default expressed as a percentage of the Exposure at Default (EAD).
Loss provisions	Provisions held against assets on the balance sheet as a result of the raising of a charge against profit for the incurred loss inherent in the lending book. The allowance represents management's best estimate of losses incurred in the loan portfolio at the balance sheet date.
Low to medium credit risk	Within not impaired, low to medium credit risk has been defined as exposures where the probability of default (PD) is 1% or below over a one year time horizon for exposures on an internal ratings based (IRB) approach under Basel II, and slotting category strong/good for specialised lending exposures under the slotting approach (see Slotting).
Lower Tier 2	Lower Tier 2 capital comprises the Bank's long term subordinated debt.
LSE	London Stock Exchange.
Malus	A facility whereby the Remuneration Committee may reduce the amount of any deferred bonus payable in the event that any of the underpins to the incentive plans are not met or where business and/or individual performance otherwise requires.
Management expenses and compensation cost	The specific elements of both operating and financing cost which form the basis of the Financial Services Compensation Scheme (see Financial Services Compensation Scheme (FSCS)).
Mandatory reserve deposits	Mandatory reserve deposits are deposited with the Bank of England and are not available for use in the Bank's day to day operations. They are non-interest bearing and are not included in cash and cash equivalents.
Market risk	Risk that the values of assets and liabilities, earnings and/or capital may change as a result of changes in market prices of financial instruments. The majority of the Bank's market risk arises from changes in interest rates.
Medium term notes (MTN)	Flexible medium term corporate debt instruments, offered by the Bank to investors through a dealer. Investors can choose from differing maturities, ranging from nine months to 30 years.
Medium to high credit risk	Within not impaired, medium to high credit risk has been defined as a probability of default (PD) of greater than 1% over a one year time horizon for exposure on internal ratings based (IRB) approach under Basel II, and slotting category weak/satisfactory for specialised lending exposures under the slotting approach (see Slotting).
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 (see Transfer of engagements).
Mortgage backed securities	Securities that represent interests in a group of mortgages. Investors in these securities have the right to cash received from future interest and/or principal mortgage payments.
Multilateral Development Banks (MDBs)	Supranational institutions which provide financial support and professional advice for economic and social development activities in developing countries. The term MDBs typically refers to the World Bank Group and Regional Development Banks.
Net interest income	The difference between interest received on assets and interest paid on liabilities after taking into account the effect of derivatives.
Net present value (NPV)	The present value of the expected future cash in and out flows on an asset or liability.
Non-conforming	Loans originated by Platform prior to 2009 and those acquired by Britannia Treasury Services, with similar risk profiles to Almost prime (see Almost prime).
Non-core business	Lines of business not congruent with the Bank's current strategy, are managed for value and are targeted for run down and exit, and contain the majority of impairment risk. Included in Non-core is Corporate Non-core business, Optimum (closed book of residential mortgages originated through intermediaries and previously purchased mortgage portfolios) and Illius (the residential property company).
Operational risk	The risk of loss resulting from inadequate or failed internal processes, people and systems or external events. This encompasses the effectiveness of risk management techniques and controls to minimise these losses.
Optimum	A sub-segment within CoAM which is a closed book of residential mortgages originated through intermediaries and previously purchased mortgage portfolios.
Options	Instruments which convey the rights, but not the obligations, to engage in future transactions.
Over The Counter (OTC)	Contracts that are traded (and privately negotiated) directly between two parties, without going through an exchange or other intermediary. They offer flexibility because, unlike standardised exchange traded products, they can be tailored to fit specific needs.
Overnight Indexed Swap (OIS)	A rate reflecting the overnight interest typically earned or paid on the Bank's collateralised swaps. The OIS rate is used for valuing the discounted cash flows of collateralised swaps.
Past due	When a counterparty has failed to make a payment when contractually due.

For the period ended 30 June 2014

Terminology	Definition
Pension risk	The risk to Bank capital and Company funds from exposure to pension scheme liabilities and risks inherent in the valuation of scheme liabilities and assets.
Preference shares	The preference shares have been cancelled as part of the LME. They were fixed interest shares, non-cumulative and irredeemable.
Prime	Prime mortgages are mainstream residential loans, which typically have a higher credit quality and fit standard underwriting processes. As such, they are likely to have a good credit history and pass a standard affordability assessment at the point of origination.
Probability of default (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.
Project Verde	The bid to purchase the Verde business from the Lloyds Banking Group. Also referred to as Project Mars.
Prudential Regulation Authority (PRA)	The FSA was replaced as the UK's financial regulator on 1 April 2013 with two new regulatory bodies: the PRA and the FCA. The PRA a subsidiary of the Bank of England, is responsible for promoting the stable and prudent operation of the financial system through regulation of all deposit-taking institutions, insurers and investment banks.
Recapitalisation Plan	The process by which the Bank is improving its capital position in line with regulatory guidance.
Recovery and Resolution Plan	The FSA required all UK deposit takers and large investment firms to draw up a Recovery and Resolution Plan by 31 December 2012. The Recovery Plan assesses and documents the recovery options available in situations of financial stress or negative financial shocks, either market-wide or idiosyncratic. The Resolution Plan will provide authorities with sufficient information to enable them to determine a detailed roadmap to resolve a failed financial institution, without resorting to government (effectively taxpayer) support.
Remuneration Code	The Remuneration Code, issued by the Financial Services Authority, sets out the standards that banks, building societies and other financial institutions have to meet when setting pay and bonus awards for their staff. It aims to ensure that firms' remuneration practices are consistent with effective risk management.
Repo/Reverse repo	A repurchase agreement that allows a borrower to use a financial security as collateral for a cash loan at a fixed rate of interest. In a repo, the borrower agrees to sell a security to the lender subject to a commitment to repurchase the asset at a specified price on a given date. For the party selling the security (and agreeing to repurchase it in the future) it is a repo; for the party on the other end of the transaction (buying the security and agreeing to sell in the future) it is a reverse repurchase agreement or reverse repo.
Reputational risk	The risk associated with an issue which could in some way be damaging to the brand of the Bank either through its strategic decisions, business performance, an operational failure or external perception.
Retail segments	The Core and Non-core segments that comprise customer focused products and services for individuals, sole traders and small partnerships. This includes mortgages, credit cards, consumer loans, current accounts and savings products.
Return on Equity	The ratio of profit for the year (after tax) to shareholders equity, expressed as a percentage.
Return on Risk Weighted Exposure Amount (RRWEA)	The return on Bank's assets and exposures weighted according to risk. The measure is one of the performance metrics set by the Remuneration and Appointments Committee when assessing targets in the long term incentive plan.
Risk appetite	The articulation of the level of risk that the Bank is willing to accept (or not accept) in order to safeguard the interests of the members whilst achieving its business objectives.
Risk weighted amount	Risk weightings are established in accordance with Basel II as implemented by the FSA. Risk weighted amounts are the carrying value of the Bank's assets, adjusted by the risk weightings, to reflect the degrees of risk they represent.
Risk weighted assets	A measure of a bank's assets adjusted for their associated risks. Risk weightings are established in accordance with Basel II.
Secondary sovereign exposure	Direct exposure to something other than sovereign debt that has itself a direct exposure to sovereign debt.
Secured lending	Lending in which the borrower pledges retail or commercial property as collateral for the loan, which then becomes a secured debt owed to the Bank. In the event that the borrower defaults, the Bank may take possession of the asset used as collateral and may sell it to regain some or the entire amount originally lent to the borrower.

Terminology	Definition
Securitisation	A process by which a portfolio of retail mortgages is used to back the issuance of new securities by an SPE. The Bank has established securitisation structures as part of its funding and capital management activities (see Special purpose entities (SPEs)).
Senior unsecured debt	Debt that has priority ahead of all other unsecured or subordinated debt for payment in the event of default.
Slotting	The regulatory defined approach used for rating the risk level of Corporate lending using a broad scope of financial, political and transactional factors. The regulatory slotting categories are listed as follows: • 'Standardised' businesses lack sufficient information upon which detailed credit analysis can be undertaken for which models have yet to be developed; • 'Strong' businesses have little competition, high demand, significant governmental support and enforceable collateral; • 'Good' businesses have limited competition, stable demand, good governmental support and enforceable collateral; • 'Satisfactory' businesses have a broad competition base with limited levels of demand, governmental support and collateral; • 'Weak' businesses operate at a disadvantage to competition, display a declining trend of demand, with no governmental support and no clear collateral; and • 'Default' businesses are considered unlikely to repay their credit obligations (see Impaired loans).
SME customers	Small and medium sized businesses engaging with the Bank as customers.
SONIA	Sterling OverNight Index Average (SONIA). Yield curves used by the Bank for swap arrangements. These are based on overnight indexed rates.
Sovereign debt	Bonds issued by and loans given to central banks and local governments, governmental bodies and other government-related bodies.
Sovereign exposure	The Bank's exposure to the total financial obligations incurred by all governmental bodies of any nation.
Special purpose entities (SPEs)	Entities that are created to accomplish a narrow and well defined objective. For the Bank this includes: • various securitisation transactions in which mortgages were sold to SPEs. The equity of these SPEs is not owned by the Bank; and • Covered Bond Limited Liability Partnerships created in order to act as guarantors for issues of covered bonds.
Specialised lending	Lending in which the primary source of repayment of the obligation is the income generated by the assets being financed, rather than the independent capacity of a broader commercial enterprise.
Standardised category	Customers who have not defaulted, and for the purposes of the capital calculations are not rated with the regulatory approved rating model.
Standard Variable Rate (SVR)	A variable and basic rate of interest charged on a mortgage. This may change in reaction to market conditions resulting in monthly repayments going up or down.
Statutory loss	The loss stated in accordance with the requirements of the UK Companies Act 2006, which incorporates the requirements of International Financial Reporting Standards (IFRS).
Strategic Asset Review	The process by which the Bank centrally monitors risk on its corporate loan assets in line with agreed strategy and governance parameters.
Strategic and business risk	Risk arising from changes to the Bank's business and the environment in which it operates, specifically the risk of not being able to carry out the Bank's business plan and desired strategy.
Subordinated debt/liabilities	Liabilities which, in the event of insolvency or liquidation of the Bank, are subordinated to the claims of depositors and other creditors of the Bank.
Swaps	An agreement between the Bank and a counterparty in which one stream of future payments is exchanged for another stream, based on a specified principal amount. For example, interest rate swaps often involve exchanging a fixed receipt for a floating receipt, which is linked to an interest rate (most often LIBOR). The Bank's use of swaps helps to manage periodic market risk on its financial instruments.
Term deposit	A deposit balance that cannot be withdrawn before a date specified at the time of deposit.
the Bank	The Co-operative Bank and its subsidiaries.
the Banking Group	See 'the Co-operative Banking Group'.

For the period ended 30 June 2014

Terminology	Definition
the Board	The Board of Directors. They manage the Bank's business performance in line with its purpose, givens, vision and values.
the Company	The Co-operative Bank as a standalone entity.
the Co-operative Banking Group	The Co-operative Banking Group Ltd and its subsidiaries, which included the Bank until legal separation occurred on 20 December 2013.
The Co-operative Group	The former ultimate parent company of the Bank, pre legal separation.
Tier 1	A regulatory measure of financial (capital) strength. Tier 1 is divided into Core Tier 1 and other Tier 1 capital. Core Tier 1 capital comprises share capital and associated share premium, and general reserves from retained profits. The book values of goodwill and intangible assets are deducted from Core Tier 1 capital and other regulatory adjustments may be made for the purposes of capital adequacy. Qualifying capital instruments such as perpetual subordinated bonds are included in other Tier 1 capital.
Tier 1 ratio	Tier 1 capital divided by risk weighted assets.
Tier 2	Tier 2 capital comprises the Bank's property valuation reserve, preference shares, qualifying subordinated notes and collective impairment allowance (for exposures treated on a Basel II standardised basis). Certain regulatory deductions may be made for the purposes of assessing capital adequacy.
Transfer of engagements	On 1 August 2009, Britannia Building Society merged with The Co-operative Bank plc by a transfer of engagements between the Building Society and the Bank under the Building Societies (Funding) and Mutual Societies (Transfers) Act 2007 (see Merger).
Treasury segment	The treasury segment's responsibilities usually include capital management, risk management, strategic planning and investor relations.
Turnaround Plan	The 4–5 year plan to reshape and restructure the business as a core relationship bank.
Unaudited	Financial information that has not been subjected to the audit procedures undertaken by the Bank's external auditor.
Unfunded pension scheme	Pension scheme which has liabilities and no assets. The Bank will pay the liabilities of the scheme as they fall due.
Unsecured lending	Lending for which there is no collateral for the loan.
Verde business	Separated part of the Retail business of the Lloyds Banking Group.
Value at risk (VaR)	VaR measures the daily maximum potential gain or loss due to market volatility within a statistical confidence level of 95% and a one day holding period. The VaR methodology employed is historical simulation using a time series of one year to latest day.
Watchlist	A list of counterparties, drawn up by the Bank once it has elected to closely monitor the performance of loans subject to significant credit risk.
Wholesale	Wholesale banking is the provision of loans to corporate customers and institutional customers and services to other banks and financial institutions.
Write down	After an advance has been identified as impaired and is subject to an impairment allowance, the stage may be reached whereby it is concluded that there is no realistic prospect of further recovery. Write downs will occur when, and to the extent that, the whole or part of a debt is considered irrecoverable. This action can occur at any time in the debt's life (see Charge off).

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