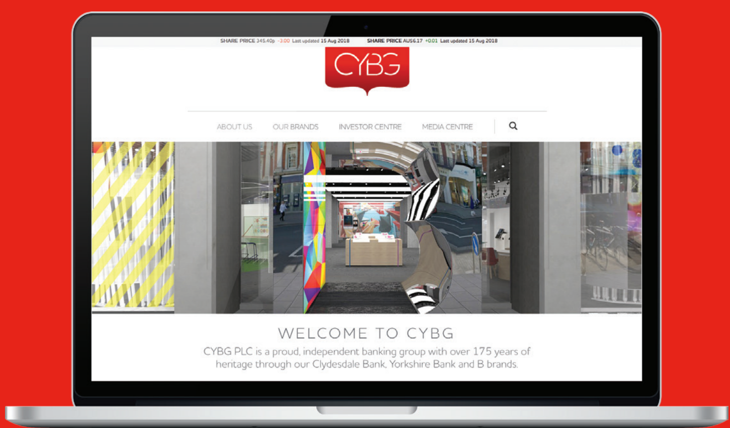
ANNUAL REPORT AND ACCOUNTS 2018

2018 has been another year of strong progress for CYBG, with the continued execution of its strategy and disciplined delivery against all of the strategic targets the Group has set.

The transformation CYBG has undertaken since IPO has positioned the Group well and culminated in the acquisition of Virgin Money to create the first true national competitor to the status quo in UK banking.

View our Annual Report and Accounts, Financial Results and Articles and other information about CYBG at **www.cybg.com/investor-centre/**



Reporting

Certain figures contained in this document, including financial information, may have been subject to rounding adjustments and foreign exchange conversions. Accordingly, in certain instances, the sum or percentage change of the numbers contained in this document may not conform exactly to the total figure given. The forward-looking statements disclaimer can be found on page 257.

Inside this year's report

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Strategic report

Group at a glance

Our significant scale (as at 30 September 2018)

£33.3bn
Customer loans

£28.9bn
Customer deposits

2.8m
Customers

159
Retail branches

Our business is delivered through our key brands

CYBG operates through the retail and commercial banks Clydesdale Bank, established in 1838 in Glasgow, Yorkshire Bank, founded in 1859 in Halifax and through the digital banking service B, created in 2016.

Underpinned by our three strategic priorities

Drive sustainable customer growth
by investing to broaden the franchise across our target segments and core regions, while enhancing the customer experience.

Improve efficiency
by making our network, operations and organisation more efficient and agile for colleagues and customers.

Capital optimisation
by securing internal ratings-based (IRB) accreditation across all of our lending book (with accreditation for mortgages and small and medium-sized enterprises (SMEs) lending achieved in October 2018) and deploying our capital to support our business ambitions while balancing risk and reward.

Distributed through our omni-channel model

Our omni-channel model enables our customers to interact with us in whichever way they choose and we remain focused on delivering an improved service across every channel where we serve and support our customers.

Our strong and growing digital offering, combined with the branch network, contact centre and extensive broker channel, provides an enviable position from which to grow our business.

To achieve our objectives, we are streamlining our front and back office, investing in our digital platform to accelerate the adoption of mobile and online tools and increasing in-branch automation.

2018 highlights

Delivering sustainable customer growth

+4.5% mortgage lending annual growth

+5.6% core SME lending annual growth

Improving efficiency

5.9% reduction in underlying costs with positive jaws achieved

63% underlying cost income ratio (2017: 67%)

Capital optimisation

IRB accreditation achieved

10.5% CET1 ratio

14.0% IRB pro forma CET1 ratio

Managing net interest margin (NIM)

2.17% (2017: 2.27%)

Increased underlying profit before tax

£331m up 13% year on year

Double-digit return

10.6% underlying return on tangible equity (RoTE)

Increased ordinary dividend

3.1 pence per share payable to all shareholders

Statutory loss in year

£145m statutory loss primarily due to PPI provision charges

Note: the key performance indicators (KPIs) used by management in monitoring the Group's performance and reflected throughout this section are determined on a combination of bases (including statutory, regulatory and alternative performance measures), as detailed in the Glossary on page 246. The results referred to in this Annual Report and Accounts relate to the 12 months up to 30 September 2018, which is a period prior to the acquisition of Virgin Money Holdings (UK) plc (Virgin Money) and therefore do not take into account the results of Virgin Money or its controlled entities.

Strategic report

Chairman’s statement

“2018 has been a landmark year for CYBG with the continued delivery of our strategy and the well-executed acquisition of Virgin Money. This sets us up for an exciting future that I believe will deliver real value for shareholders and create a powerful force in UK banking.”

2018 was another year of strong progress for CYBG, with the continued execution against our organic strategic pillars – sustainable customer growth, efficiency and capital optimisation – while at the same time delivering the Virgin Money acquisition. This was the Group’s first acquisition, not to mention the UK’s first major public bank acquisition since the financial crisis. The hard work and focus of the Board, Executive Leadership Team and all of our colleagues during this time has been impressive. It gives me great confidence that we have the right team in place to lead us through the next phase of our transformation.

The Group’s continued successful delivery means that I am pleased to announce that the Board is recommending the payment of an increased ordinary dividend of 3.1p per share. When we paid our inaugural dividend 12 months ago, I talked about how this represented a landmark event in the process of transforming CYBG into a bank that generates and distributes a sustainable return on its equity to shareholders. The payment of this year’s dividend, a trebling of last year’s, is true to this aspiration. The Group’s enhanced prospects following the acquisition means I am confident we can deliver on our progressive dividend ambitions going forward.

One of the key strengths of CYBG is our colleagues’ commitment to our customers and during the year I have seen a continued focus on doing the right thing for customers. Examples of this include initiatives such as our successful ‘B-Tox’ campaign which aimed to help our customers get their finances in order and the introduction of a new forum for embedding daily customer feedback into the wider Group. Like all organisations, there is always more we can do and improvements to be made, but I truly believe that CYBG has the customer at the heart of what we do and this can only be good for customer outcomes.

A value deeply ingrained in our heritage is our commitment to supporting the communities we serve. 2018 has seen another strong year of support provided by our colleagues with, for instance, 2,000 hours of volunteering time across our range of community projects; a further year of fundraising for Hospice UK with £6.5m now raised during our 10-year partnership; an impressive £500k raised by almost 300 colleagues sleeping out in aid of Social Bite’s campaign to end homelessness; and the much-needed support we provide for critical front-line services for the most remote areas with Scotland’s Charity Air Ambulance.

Given the contribution our colleagues make, it is only right that CYBG in turn does its utmost to take care of them. The introduction of our first ‘Well-being in the Workplace’ survey has shown our commitment to creating an inclusive, safe and healthy environment where people can excel. The relaunch of our mental health awareness training module and People Leader toolkit has also helped ensure colleagues feel supported and have the right tools available to them.

Inclusion is also very much at the heart of our culture and we continue to make great strides in developing a diverse and inclusive culture. We have five colleague network groups now in place for gender, age, disability, ethnicity and sexual orientation, all sponsored by members of our Executive Leadership Team.

Lack of clarity surrounding the terms of the UK’s departure from the EU has led to an uncertain economic outlook. However, the work undertaken by the Board suggests that CYBG is well-placed to manage any short-term volatility.

I would like to thank all of our colleagues, the Executive Leadership Team and the Board for their continued dedication to the transformation of CYBG in what has been a landmark year. I would also like to personally thank David Browne, who retired from the Board in June, for his contribution over the past six years.

Finally, I would like to extend a very warm welcome to our new colleagues and Board members who have joined us from Virgin Money. We look forward to working with and learning from you, and the clear alignment in our cultures means I am confident we will be able to leverage the strengths of both businesses to build something greater than the sum of the two parts.

Jim Pettigrew
Chairman

26 November 2018

Clear alignment in cultures provides opportunity to leverage the strengths of both businesses

- Brand / cultural alignment between businesses
- Balanced approach planned to integration strategy
- Building a ‘best of both’ model will leverage talent of both CYBG and Virgin Money colleagues

Strategic report

Chief Executive Officer's review

"2018 has been another transformational year for CYBG, in which we have continued to execute on our strategy and consistently delivered against the targets we have set. Our strong progress since the IPO has put in place the foundations that enabled us to acquire Virgin Money and to deliver on our ambition to create the first true national competitor to the status quo."

I am delighted to report that we have seen another year of significant progress in 2018. Our disciplined approach to executing on our strategic plan and delivering our commitments has translated into both improved financial performance and strong strategic positioning.

The UK economic outlook remains uncertain and while the economy has remained more resilient than expected, economic data through the year has pointed to a slightly weaker environment. In particular, consumer spending has slowed and businesses have been holding back investment. This has reduced demand for lending, although credit conditions remain benign. In the mortgage market, economic uncertainty has reduced customer demand while competition has remained intense, resulting in a challenging pricing environment, with swap rate increases not being fully passed on to customer pricing. There is still significant uncertainty as to the outcome of the UK's negotiations with the EU. However, the Group's outlook and 2019 guidance is based on our planning assumption of a transitional agreement between the UK and EU from March 2019.

Despite some of these uncertainties, our market position as the only full-service UK challenger bank of scale across both Retail and SME enabled us to deliver ahead of market growth in both mortgages and SME, prudently funded by our strong deposit franchise. Our performance in SME means we remain on track to deliver our commitment to provide at least £6bn of lending to SMEs by the end of 2019.

Our 2018 financial results show improved underlying profit and returns, sustainable loan growth and the payment of an increased ordinary dividend of 3.1p per share. Income was down slightly, with continued growth in net interest income more than offset by lower non-interest income. NIM declined 10bps in the year to 2.17% driven by the competitive front book pricing environment in mortgages. Our cost efficiency programme is ahead of plan, with underlying operating costs of £635m, while impairment charges remain low.

While the Group delivered a strong underlying performance, the significant action taken to manage the Group's legacy conduct issues means we have reported a statutory loss after tax of £145m. While the additional PPI provision charge required in 2018 is disappointing, the Group's strong capital position means we have been able to absorb this without any impact on our strategy and future ambitions.

Capital optimisation and, specifically, achieving IRB accreditation, was one of the Group's key strategic targets. Following another year of hard work across the Group, I am delighted that in October 2018 we received IRB accreditation from the PRA for both our mortgage and SME portfolios. It is a testament to the strength of our risk management approach, delivers a significantly more capital efficient bank and will enable us to compete in a broader range of products in the marketplace.

Our digital transformation also continued at pace, with the significant, multi-year investment made in our technology platforms enabling us to leverage the iB platform to deliver an enhanced digital customer experience. Key achievements include: the migration of our c.2m Retail customers onto our iB platform; beginning our first Fintech partnerships; and being the first challenger bank to offer an Open Banking enabled current account aggregation service.

While our Group NPS score of +10 is not at the level we aspire to, customer experience is very much a top priority for my leadership team. We are therefore encouraged by the strong +34 NPS score for our digital-only brand B.

Looking forward, I believe CYBG is truly differentiated from its UK banking peers through the genuinely unique combination of growth opportunities available to us. These include the ability to grow our SME business through the RBS Alternative Remedies Package schemes, the delivery of an enhanced customer experience by fully leveraging our digital platform in an Open Banking environment and, of course, the recently announced acquisition of Virgin Money. I believe our combination of scale and growth opportunities are unique in the UK marketplace.

The Virgin Money acquisition was clearly a landmark moment for the Group. The combination will create the first true national competitor to the status quo in UK banking in over a decade, offering a genuine alternative for consumers and small businesses. The following transaction overview section recaps the compelling strategic and financial rationale. We have already begun a comprehensive strategic planning process for the Group and I would expect us to be in a position to update the market on our strategy and targets at a Capital Markets Day event in June 2019.

I want to thank our Board and colleagues for their support and hard work, and I would also like to extend a very warm welcome to our new colleagues from Virgin Money. Together, we have a once-in-a-generation opportunity to change the competitive dynamic in UK banking and I am sure I speak for everyone when I say that we can't wait to get started!

David Duffy
Chief Executive Officer

26 November 2018

Strategic report

CYBG acquisition of Virgin Money

Creating the first true national competitor to the status quo

This will be achieved through:

ONE ICONIC NATIONAL BRAND

Virgin money

Virgin is one of the most powerful and iconic brands in the UK, with 99% brand awareness.

Use of the Virgin Money brand, combined with CYBG's customer-centric product range and service model, is expected to lead to higher consumer interest and advocacy across the UK over time, generating increased customer acquisition and greater customer retention.

Read more online at:
www.cybg.com/investor-centre

A COMPELLING RETAIL CUSTOMER EXPERIENCE

Delivers full product set
- Full banking product offering for customers post-transaction.
- Complementary blend of product expertise, driving product innovation for customers.

Strengthens omni-channel customer proposition
- Single platform customer service proposition across all channels.
- National coverage increases customer convenience and access.

New partnerships opportunities
- Potential to build partnerships with other Virgin companies to offer innovative products to our enlarged customer base.

A LEADING SME FRANCHISE

Strong SME capabilities
- 175 years' history and heritage.
- Full product suite and substantive business current account (BCA) capability.
- Relationship-manager led service model.
- Deep sector specialism and proven risk management capability.

Scale and strength in core regions
- £9bn of deposits and £7bn of lending.
- c.15% BCA market share in Scotland and Yorkshire.
- c.200k customers – 50% for >10 yrs.

Well-positioned to become a national SME competitor
- CYBG well-placed to compete for both RBS alternative remedies package schemes to scale our regional SME franchise nationally.

Underpinned by a leading digital capability
- c.6m customers will benefit from iB platform capabilities and customer experience.
- Greater scale will allow increased investment in platform, improving user experience.
- Developing our SME digital proposition using our iB platform.

EXPECTED 2019 REPORTING TIMELINE

JAN 2019
Q1 trading update
First Combined Group update
Pro forma financial comparatives

MAY 2019
Interim results
Combined Group financial results
RBS alternative remedies scheme update

JUN 2019
Capital Markets Day
Strategy deep-dive
Announce medium-term strategic and financial targets

INTEGRATION TIMELINE

FY2019

– Integration planning and project begins.
– Initial cost synergies delivered.
– RBS alternative remedies schemes commence.
– Customer experience and digital development continues.

FY2020-2021

– Virgin Money rebranding begins.
– Phased migration of systems and customers.
– Remaining cost synergies to be delivered.
– Strategic growth opportunities to be explored.

FIRST TRUE NATIONAL COMPETITOR TO THE STATUS QUO

FINANCIAL OUTCOMES

- c.£120m of annual run rate cost synergies
- Low risk asset portfolio, with diversified funding model
- Strong pro forma Combined Group CET1 ratio of 15.2%, with enhanced capital generation capability
- Materially earnings accretive, with opportunity for further shareholder value creation

AUG 2019
Q3 Trading Update
Combined Group Q3 update

NOV 2019
Full year results
Combined Group financial results

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Case study

Backing Britain's manufacturers and the Northern Powerhouse

Britain has long been heralded as a world leader in manufacturing and Clydesdale and Yorkshire Banks have a proud history of supporting businesses across the sector for more than a century. We're committed to fuelling business growth across the North of England in particular, where so many innovative manufacturing SMEs operate. Besides being a key member of the Northern Powerhouse Partnership, we have a commitment to make £6bn of lending available to the UK's SMEs through to 2019, with 90% of this lending focused outside London. Through the support we give to our manufacturing customers, our lending commitments and our backing of the Northern Powerhouse, Clydesdale and Yorkshire Banks are playing an active role in maintaining the UK's globally renowned strength in the manufacturing sector, boosting the industrial base of Britain's regional economies and helping the North to flourish.

Advanced Engineering Techniques Ltd (AET Ltd) is an established Sheffield-based manufacturing business which provides parts for a broad range of industries including the rail, construction, road transport, renewable energy and agricultural sectors.

Established in 1989, AET Ltd operates from a 65,000 square feet manufacturing facility on a 2.5 acre site and is one of the largest and fastest growing sub-contract engineering companies in the North of England. Yorkshire Bank first backed the business in 2002, and since then we have continued to support their acquisition of state-of-the-art automated laser cutting technology. In 2015, we provided £900,000 funding for new advanced laser cutting tools which used far less energy than previous equipment, ran three times faster and could run unmanned overnight.

Support continued and in the summer of 2018, Yorkshire Bank provided a £770,000 Asset Finance package to AET Ltd so they could acquire a further Bystronic laser BySprint & ByTrans, as well as a larger Panasonic Welding Cell. These new tools will allow the company to expand its production capacity and benefit from new market opportunities, maintain its competitive edge against rivals overseas and win more contracts, all of which will help to retain jobs for the local community and keep the North of England moving.

Strategic report

How we create value

OUR CORE BUSINESS STRENGTHS...

- Simple, low-risk banking model
- Scale and scope of larger players, with the agility of a smaller bank
- Long-established franchise in core regional and selected national markets
- Resilient and strongly capitalised balance sheet with a diverse range of funding sources available
- Cutting-edge, scalable and full-service digital operating platform positioned for the future
- Experienced Executive Leadership Team and dedicated colleagues

...MEANS WE CAN OFFER OUR CUSTOMERS...

- 2.8m retail and business customers
- Strong market shares in our core regions of Scotland and the North of England
- Perfectly positioned to support and benefit from the UK Government's 'Northern Powerhouse' initiative
- Customer proposition increasingly attracting new customers from our under-represented demographic segments (young and affluent)

...A FULL SERVICE BANKING PLATFORM...

We offer a range of simple banking products supported by great customer service

Retail

– Personal current accounts
– Savings accounts
– Term deposits
– Mortgages
– Personal loans
– Credit cards
– Overdrafts

SME

– Business current accounts
– Savings and deposits
– Term lending
– Overdrafts
– Working capital solutions
– Payment and transaction services

Telephony

Internet banking

Mobile

Intermediary

Branches and business centres

...IN WHICHEVER WAY OUR CUSTOMERS CHOOSE TO INTERACT WITH US...

...DELIVERING VALUE TO OUR STAKEHOLDERS

Customers
Read more pages 26 and 27

Colleagues
Read more pages 26 and 27

Communities
Read more pages 26 and 27

Environment
Read more page 30

Strategic report

Strategy and performance

Another year of consistent delivery against our strategic targets

	Drive sustainable customer growth	Improve efficiency	Capital optimisation
Our strategic priorities	**by investing to broaden the franchise across our target segments and regions, while enhancing the customer experience**	**by making our network, operations and organisation more efficient and agile**	**by securing IRB accreditation and exploring opportunities across the asset portfolio**
Our progress during FY2018	– Sustainable growth in the year with core lending up 4.7% and customer deposits up 4.2%. – Ahead-of-market mortgage growth driven by our differentiated proposition. – Consistent and disciplined focus on serving the SME market, with our specialist sector offerings resonating strongly. – Improved origination capability driving c.4% growth in unsecured personal lending. – Delivered targets in a muted economic environment.	– Project Sustain cost efficiency programme ahead of schedule with £141m of run rate cost savings delivered by the end of 2018. – 2018 run rate savings delivered primarily through central cost management optimisation. – Project Sustain has delivered higher gross cost savings than originally planned and, after reinvestment, our net savings target of £100m has been largely delivered a year ahead of target. The run rate for underlying operating expenses going into FY2019 is <£630m.	– In October 2018 we received IRB accreditation for our mortgages and SME portfolios from the Prudential Regulation Authority (PRA); a landmark achievement for the Group. – Good progress has also been made with IRB accreditation for retail unsecured lending, with all models now submitted to the PRA for review. – The Group achieved a double-digit underlying RoTE for 2018 in line with its target. – Development of our portfolio management capabilities during the year has driven improved capital efficiency.
Changes since FY2017	+4.5% Mortgage lending growth +5.6% SME core lending growth	-5.9% Underlying costs year on year -£40m reduction in operating costs	+3.1%pts Underlying RoTE year on year >£5bn pro forma reduction in RWAs from IRB
Our KPIs for FY2018	+4.7% Core loan growth 115% Loan to deposit ratio (LDR)	63% Underlying cost to income ratio (CIR) Positive jaws of 5% achieved	10.6% Underlying RoTE 10.5% Common Equity Tier 1 (CET1) ratio 14.0% IRB pro forma CET1 ratio

FY2019 Combined Group guidance

Note: all guidance is based on CYBG's current planning assumption of an orderly Brexit and a transitional agreement being in place between the UK and EU by March 2019.

Metric	FY2019 Combined Group guidance
Net interest margin (NIM)	160-170bps
Underlying costs	<£950m

Existing medium-term guidance – transaction impact

CYBG's acquisition of Virgin Money reinforces the delivery of our existing medium-term guidance, with material Earnings per share (EPS) accretion for all shareholders once full cost synergies are delivered.

Metric	Existing guidance	Expected transaction impact
Loan growth	Mid single-digit % CAGR to FY2019	✓ Sustainable growth ambition continues
LDR	<120%	✓ Diversified funding model continues
CIR	55-58% by FY2019	✓ CIR at lower end of target range, significant cost synergies over time
RoTE	Double-digit by FY2019	✓ Double digit returns target maintained
Dividend	50% pay out ratio over time	✓ Accelerates progressive dividend ambition

Strategic report

Risk overview

Effective management of risk is a key capability for a successful financial services provider and is fundamental to the Group's strategy

The Group has continued to advance and strengthen its risk management capabilities, evolving in line with industry developments and best practice.

The Group's approach to risk

Risk exists in every aspect of the Group's business, is an integral part of the operating environment, and is a core consideration inherent within the Strategic Plan.

The Group's approach to risk management is based on the principle that risk management capability must be embedded across all areas of the Group to be effective.

Risk strategy

The Group has a clearly defined strategy in place to monitor, manage and mitigate risk.

The risk strategy includes: ensuring all principal and emerging risks are identified and assessed; that risk appetite is clearly articulated and influences the Group's strategic plan; the maintenance of a clearly defined risk culture which emphasises risk management while maintaining independent oversight; the need for ongoing analysis of the environment in which the Group operates to proactively address potential risk issues as they arise; and a requirement to ensure that appropriate risk processes, systems and controls exist to support all colleagues in their decision making.

Risk culture

The Group promotes a risk culture that supports the safety and soundness of the Group as well as the consistent and fair treatment of customers, both of which are fundamental to the success of the Group's business model and strategy. The risk culture shapes behaviours and decision making at all levels of the Group. The interests of customers, colleagues, shareholders and the communities within which the Group operates are all aligned to deliver the Group's strategic aim of sustainable customer growth.

A strong risk culture is founded on a risk management accountability model and formal delegation framework where personal accountability empowers colleagues to take ownership. It is a consideration in all people management practices, supported by a formal whistle-blowing framework that allows colleagues, in confidence and anonymously, to raise concerns about matters of conduct, including inappropriate behaviour.

Risk management framework (RMF)

The Group identifies and manages risk using the RMF (see diagram below), which is the totality of systems, structures, policies, processes and people that identify, measure, evaluate, control, mitigate, monitor and report all material sources of internal and external risk. Key aspects include:

– the risk appetite statement (RAS) that defines the level and types of risk the Group is willing to assume, within the boundaries of its risk capacity, to achieve its strategic objectives;

– the policy framework which provides structure and governance for the effective management of risks; and

– the Group adopts a 'Three Lines of Defence' risk model comprised of: operational Business Units, the Risk Management function and Internal Audit.

Top and emerging risks

The Group monitors the environment in which it operates to identify both top and emerging risks that may have an impact on its operations and strategy. The Group currently considers those to be (see page 124 for details):

– geopolitical and macroeconomic environment, including the impact of the UK's vote to leave the EU (Brexit);

– competition;

– consumer credit;

– cybersecurity, IT and financial crime;

– regulatory change;

– risks arising from the acquisition of Virgin Money;

– continued risk of customer detriment;

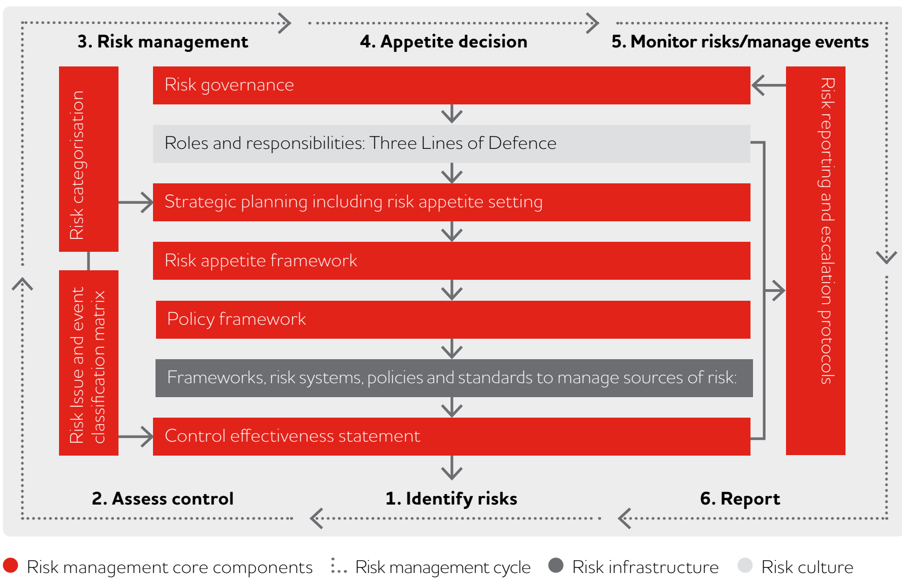
– service interruption;

– use of third party suppliers.

The Group continues to monitor and mitigate these risks through the RMF.

Risk capability

As discussed earlier in the report, in October 2018 the Group obtained approval for the use of IRB models for its mortgage and SME/corporate portfolios. This represents a significant milestone in the further development of the Group's risk capability.



The principal risk categories listed below reflect the Group's inherent risks, and are expanded upon within the Risk Report on page 121.

Principal Risk category	How this risk is managed
Credit risk is the risk of loss of principal or interest stemming from a borrower's failure to meet contracted obligations to the Group in accordance with the terms agreed. Credit risk is evident at both a portfolio and transactional level.	– Significant credit risk strategies, credit risk appetite and tolerances for credit risk are approved and reviewed by the Board and Boards' Risk Committee. – The credit portfolio is closely monitored with actions initiated where required.
Balance sheet and prudential regulation risk covers a number of categories of risk, which affect the manner in which the Group can support its customers in a safe and sound manner. The risks include the need to withstand times of stress for the loss of funding (liquidity), the impact of restricted access to future sources of deposits (funding), the impact of providing a defined benefit (DB) scheme to colleagues (pension) and the need to withstand severe unexpected losses (capital).	– Funding and Liquidity is managed in accordance with standards that are approved by the Board, including the annual ILAAP, Funding and Contingency Funding Plans. These standards maintain appropriate controls on the flow of new lending, deposits and refinancing of existing transactions and also consider the outcomes of stress testing. – The Group completes a formal assessment of capital through an ICAAP which includes the impact of severe, yet plausible, stress events to ensure that appropriate levels and types of capital underpin the strength of the balance sheet in both normal and stressed conditions. – The Group has implemented a range of pension reforms to reduce its exposure to pension risk including the closure of the DB scheme to future accrual for the majority of members from August 2017.
Regulatory and compliance risk is the risk of failing to identify, understand, monitor and comply with relevant laws, regulations, licence conditions, supervisory requirements, self-regulatory industry codes of conduct and voluntary initiatives. In doing so, the Group risks damaging its relationship with its regulators. It is also the failure of not keeping regulators informed of relevant issues and not responding effectively to information requests and regulatory reviews.	– Continued and significant Board and senior management focus is directed towards maintaining regulatory compliance. The Board or Executive Risk Committee approves all material changes to regulatory policy and protocols.
Conduct risk is the risk of undertaking business in a way which is contrary to the interests of our customers, resulting in the delivery of inappropriate customer outcomes, customer detriment, regulatory censure, redress costs and/or reputational damage.	– The Group has an overarching Conduct Framework in place with supporting target outcomes and operating principles, and processes to put things right for customers where they have been impacted by historic issues. Governance, oversight and reporting are in place to ensure those objectives are met.
Operational risk (including resilience and information security) is the risk of loss resulting from inadequate or failed internal processes and systems or from external events. It includes legal risk, and operational risks associated with the execution of strategy.	– The Group has an established Operational Risk Framework to enable identification, management and mitigation of operational risks. Risk categories are used to facilitate the consistent identification, assessment, mitigation, monitoring and reporting of risks and events. – The Group also has an operational resilience framework that is being enhanced to reflect the changing digital environment and work is underway to ensure compliance with the new Operational Continuity in Resolution regulations that come into effect from January 2019.
Financial crime risk is the risk that the Group's products and services will be used to facilitate financial crime against the Group, its customers or third parties.	– The Group has an established Financial Crime Framework supporting ongoing management, monitoring and mitigation of financial crime risk. The Group operates zero tolerance for financial crime risk.
Strategic, business and financial performance risk is the risk of significant loss, loss of earnings and/or damage arising from business decisions that impact the long-term interests of stakeholders or from an inability to adapt to external developments.	– The Board approves and oversees the execution of the Strategic Plan and associated strategic risk following the recommendations of the CEO and Executive Leadership Team. The Group's RAS sets out the risks it is able and willing to take to achieve its strategic objectives.
People risk is the risk of not having sufficiently skilled and motivated colleagues who are clear on their responsibilities and accountabilities and who behave in an ethical way.	– Roles, responsibilities and performance expectations are defined in role profiles and expanded through objective setting and ongoing performance management. – The quality and continuity of the Group's leadership is reviewed and assessed through succession planning and talent management activity.

Case study

Supporting communities where we live and work

A decade of difference

This year, CYBG celebrated ten years of supporting Hospice UK. Over the last decade we have raised over £6m and dedicated more than 40,000 hours in colleague time to the charity. Much of this support has been direct with colleagues using their two days of volunteering leave per year to help out with everything from garden makeovers to helping with Hospice marketing, Christmas fairs, to marshalling at events.

Ali O'Reilly, Head of Corporate Partnerships said: "We are truly grateful to everyone at Clydesdale and Yorkshire Banks for every bake sale organised, every marathon run, every mountain climbed and every collection tin filled. Every pound raised makes a difference and helps to ensure that hospices across the country continue to provide vital end-of-life care to those in need."

Spirit of the Community Awards

Since its inception in 2013, the YCB Foundation has made grants of over £1m to 173 local charities through the Spirit of the Community Awards. In 2018, the Foundation introduced an additional £5,000 of funding for the winner that demonstrated exceptional innovation in their approach. This year it was awarded to Emerge 3Rs, one of the successful applicants in the employment category.

Emerge 3Rs aims to promote self-confidence and achievement to create routes into further training and employment; alongside a social enterprise matching community inclusion with waste prevention with the wider purpose of improving local, social, economic and environmental conditions.

Sleep in the Park

In December 2017, 300 CYBG staff took part in Sleep in the Park, an event run by Glasgow based charity, Social Bite to raise funds for and awareness of homelessness. Together we raised £500,000 – a major contribution towards the building of a 'village' creating temporary housing for 20 rough sleepers. The village will provide a home for 12-18 months to help transition residents into permanent accommodation and provide pathways to mainstream employers, supporting their journey back into society. After 12-18 months another 20 residents will be welcomed into the village. Gerry Magee, Head of Marketing for CYBG presents a cheque for £500,000 to Josh Littlejohn, Founder of Social Bite.

Strategic report

Operational review

Deposits

We are a full service UK clearing bank offering a wide range of current accounts, savings accounts and term deposit products for personal and business customers. Our loyal personal current account customer base represents a stable source of funding and sets us apart from most other challenger banks.

Customer deposit growth

+4.2%

to £28.9bn

B current accounts

>190,000

2017: c.100,000

BCA acquisition

c.30,000

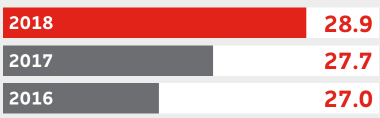
new accounts opened

BCA accounts originated digitally

c.65%

in 2018

Customer deposit balances (£bn)



CYBG adopts a prudent approach to its balance sheet management, ensuring that deposits are raised well in advance of lending commitments. The development of our deposit business is a key enabler of our overall growth strategy and 2018 saw another year of strong performance as we steadily increased the size of our deposit base, while maintaining the quality and stability of our funding.

At 30 September 2018, the Group had £28.9bn of customer deposits consisting of £14.2bn of current account balances, £8.4bn of savings account balances and £6.2bn of term deposit balances.

Progress against strategic priorities

Drive sustainable customer growth

- To support our sustainable growth in lending, deposits grew by £1.2bn (4.2%) year on year with notable increases in:
  - total B current account and linked savings, which grew by 96% to £2.1bn during the year; and
  - business notice and access accounts, which increased to £1.9bn at year end, a 6% increase year on year.
- We made improvements to our PCA proposition during the year, including enhancements to the digital account opening and maturity processes across our deposit range. These improvements mean that over two-thirds of customers receive an end-to-end digital account opening experience; this helped to support increased balances.
- In SME, our market leading offering of 25 months fee-free for new BCA customers has supported growth in balances.

Improve efficiency

- We have a continuous programme of enhancements to our core current account and savings propositions:
  - in May, we launched our first Open Banking feature, 'Connect accounts', enabling personal current account customers to connect their current accounts held with other banks;
  - our online account opening journeys for both Retail and SME have been enhanced – making it easier for customers to find the right account for them and progress their application; and
  - we have invested in our online maturity process for fixed term accounts, making it significantly easier for customers to reinvest.
- Since the launch of the new Cheque Imaging Clearing scheme in October 2017, we were the first UK bank to give customers the option to deposit cheques using a mobile app – reducing the cheque clearance time from six to two business days.
- We have made improvements to the Cash ISA transfer-in customer journey with >90% of customers transferring within seven days compared to the industry target of 85%.

Other highlights

- Since its launch in May 2016, B has attracted over 190,000 accounts and deposit balances of c.£2.1bn. During the year there was growth of 96,000 accounts year on year.
- We were pleased to be recognised as the 'Best Current Account Provider' for the second year running at the 2018 Moneyfacts awards.
- In total, 57% of our balances are now held in current accounts and linked savings accounts, demonstrating the quality and stability of our deposit business.
- In the Business Developments Research Consultants (BDRC) 'Moments of Truth' study published in August, B was ranked 5th out of 32 tested providers for net promoter score (NPS).

Mortgages

We have a strong and growing UK mortgage business. We offer mortgages through a select broker network with national coverage, while our strong regional branch network supports the natural markets in our heartlands. We operate a differentiated broker mortgage proposition, which supports a broad range of professional customers including those with complex income, underpinned by our strong underwriting capability.

Customer lending growth

+4.5%

to £24.5bn

Customer retention

84%

in 2018

Market share

1.8%

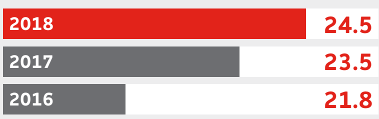
in 2018

Product transfers

27%

increase vs. 2017

Mortgage customer balances (£bn)



The mortgage market in 2018 has seen low growth, with increased remortgage activity, but lower levels of new lending and the strong competition has continued to exert pressure on front book pricing. Despite this, our differentiated proposition has delivered another strong performance.

Progress against strategic priorities

Drive sustainable customer growth

– The mortgage book increased by 4.5% in the year to £24.5bn, compared with market growth of 2.5%. We advanced £5.2bn of mortgages in 2018 with c.80% of this coming through our broker network with our proprietary mortgage business delivering c.20%.

– Strong customer retention of 84% supported balance growth, with a 27% increase in the number of product transfers through our broker channel demonstrating the strength of our proposition and offering. This reflects our focus on retention balances with customers and brokers now able to switch to a new rate through an online portal up to three months before the end of a fixed rate term without incurring an early repayment charge.

– Residential mortgage pricing remains highly competitive, with the home mover market flat and growth stemming from first time buyers and remortgaging. The BTL market remains subdued following the taxation changes, and is predominantly remortgage. With base rate having increased, the market remains a fixed rate market with five year fixed rates growing in popularity.

Improve efficiency

– New online tools and calculators have been launched to make it easier for brokers to do business with us and reducing their need to contact us.

– An enhanced online application form has improved the customer and broker experience.

– Our mortgage adviser process has had multiple improvements, making it quicker and easier for customers to get the mortgage they want with us.

Capital optimisation

– In October 2018 we received IRB accreditation for mortgages from the PRA, a major achievement for the Group. This resulted in a c.£4.5bn reduction in RWAs as at 30 June 2018.

– Going forward, IRB accreditation will enable the Group to be more competitive across a broader range of products and further strengthen our risk management approach.

Other highlights

– Mortgage offering enhancements in 2018 include the introduction of a new Qualified Professional product, allowing enhanced income multiples for a targeted, high quality customer segment, while our First Time Buyer Products were awarded an outstanding rating from Moneyfacts.

– In autumn 2017, we brought our mortgage processing operation back onshore as part of our customer journey improvement initiatives. The process of embedding the changes led to some servicing and fulfilment challenges and as a result we slowed new business volumes to protect customer service levels. Now fully embedded, the onshored operation will deliver an enhanced experience for customers in future.

– While the digital mortgage market remains a very small part of the market overall, we plan to launch our execution only digital remortgage proposition in 2019. In addition, we are enhancing our proposition through the use of digital tools allowing customers to focus on what's important to them, including speed of decision and certainty of offer.

Strategic report

Operational review

Unsecured personal lending

We have a strong unsecured lending proposition and offer a range of competitive personal loans, credit cards and overdraft products. These are available across our digital, telephone and branch channels to both new and existing customers.

Customer lending growth

+3.5%

to £1.2bn

Average loan drawdown time

1.4 days

2017: 9.7 days

Digital loans approved

£209m

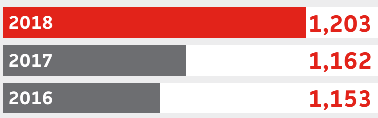
up 12%

Approved loans drawndown

79%

in 2018

Unsecured lending balances (£m)



The UK personal loans and credit card markets remain extremely competitive and unsecured lending has not been a target growth area for the Group. However, the improvement in our personal loans capability has supported origination and enabled the business to deliver a strong 2018 performance.

Progress against strategic priorities

Drive sustainable customer growth

- Unsecured lending growth continued, with an increase of 3.5% to £1.2bn.
- Unsecured fixed rate personal loans balances increased 12.9% primarily driven by digital acquisition. We have invested heavily in providing our new and existing customers with a seamless, paperless and simplified in-app digital journey including pre-assessed and pre-filled application forms and same day drawdowns. Since deploying, 67% of customers using our new app now receive funds on the day they apply.
- We have worked closely with third-party technology providers to improve product visibility and increase applicant quality on unsecured personal loan acquisition sites, helping drive volume within the risk profile.
- The focus in our cards business has been managing value in a highly competitive market. For acquisition, we have focused on features and functionality rather than solely price, as evidenced by the growth in our new B Credit card with its innovative payment managing capabilities. Accordingly, we have held book margins flat with a small reduction in balances of 3.7%.

Improve efficiency

- New unsecured personal loan origination system developments reduced application questions by half and delivered improved fraud detection tools, digital signatures and same day funds. The changes will allow increased acquisition of good quality business via improved conversion across the journey due to the enhanced systems and controls.
- For existing customers we launched secure site sales within our mobile app with pre-filled application and/or pre-assessment, significantly reducing the customer journey and time to apply to just a few clicks.

Capital optimisation

- We continue to proactively manage our cards portfolio as part of ongoing prudent risk management and in anticipation of the greater sensitivity of capital weighting to credit risk under IRB, which for Retail unsecured products is expected in 2019. This has included taking steps to optimise credit limits and we anticipate broadening this programme as we move towards IRB accreditation.

Other highlights

- We have continued our focus on regulatory changes and being a responsible lender, providing increased transparency and tackling persistent debt for customers facilitated by the FCA Credit Card Market Study remedies. Enhancements implemented include payment date changes, unsolicited credit limit increase opt-out, digital notification of approaching end of promotional terms, text alerts for approaching credit limit and additional support to manage credit card debt.
- We have rationalised our credit card issuing schemes by migrating all customers to Mastercard and signed a new exclusivity deal with Mastercard across debit and credit portfolios.
- Prudent risk management strategies have included strengthening criteria for personal loans to continue to protect asset quality in light of wider economic uncertainty.

Digital

A digital bank with a human touch, providing an intuitive, value add experience for our customers by harnessing our digital capabilities and supporting our colleagues to grow their own digital know-how.

Growth in digitally active customers

13%

since 2017

Growth in mobile app users

32%

since 2017

Mobile banking logins

191m

2017: 137m

Number of digital payments made

61m

2017: 41m

Digital sales

21% increase

vs. 2017

We have continued investing to transform our business, with a significant amount focused on enhancing our digital capabilities for our customers and colleagues. This investment has completed the refresh of our mobile and web capabilities, covering all segments and customer groups.

We have continued to build out our core iB platform at pace, extending the power of the platform, launching new mobile banking applications to all Clydesdale Bank and Yorkshire Bank customers. Every customer in CYBG now has access to our leading mobile app and over 300k customers were seamlessly migrated from an older legacy mobile app. Following this we upgraded our Internet Banking system and now 1.1m customers can transact at a time and a place that suits them using iB.

New functionality increased usage exponentially, for instance, average mobile daily logins increased to c.520k compared to c.375k last year. We have also taken the iB platform to a position where it supports, on average, c.630k logins per day, which is a 28% increase from 2017.

As the industry continues to evolve we have innovated at pace on our iB platform. iB allows us to deliver enhancements to customers faster and more efficiently than ever before as well as bringing an opportunity to open up a seam of innovation. An example of this is our leading position in aggregation, where in April 2018 we became the first challenger bank to offer an aggregation service 'Connect accounts', despite not being a CMA9 bank. Now 1.1m of our customers have Open Banking functionality which enables them to use their app to connect to accounts from other banks.

In addition to this our agile team, Accelerator, is now utilising new ways of working to develop our B store strategy.

Launching innovative technology is also helping drive efficiencies

- c.300k customers have opted for digital statements compared with over 18,000 in 2017, driven by the ability to turn on digital statements via the app.
- We streamlined the personal loans application process allowing customers to apply with just a few taps on their phone.
- 2018 saw a 27% year on year increase in completed mortgage product transfers, with 64% of applications being fulfilled through our digital channels (both direct and broker).
- We were the first UK bank to offer cheque clearing through our mobile app; over 60,000 cheques have been cleared via our mobile app in 2018.
- We have deployed a number of robotics capabilities within processes to either remove repeatable manual effort or drive straight through processing. For example, the Cash ISA 'transfer in' and 'transfer out' process is now a fully automated end to end service enabled by automation tools.
- We are delivering iB Advisor, which will transform colleagues' ability to serve customers by bringing a single customer view of all transactions and servicing history across all accounts, through one system.

Digital inside and out

We have upgraded our entire network capability, paving the way to deliver a step change for our business with new modern enterprise applications while driving additional benefits to our colleagues. The introduction of Office 365 with a user base now at c.2,300, virtual desktops and the launch of Service Now ensure that not only our customers benefit from the transformation, but our colleagues experience working in a modern digital bank.

Strategic report

Operational review

SME lending

We provide small and medium-sized enterprises (SME) customers with a complete set of lending products and services comprising term lending, overdrafts, revolving credit facilities, working capital, trade and treasury solutions.

Core SME lending growth

+5.6%

to £7.2bn

SME lending commitment 2016-19

£6bn

c.70% of pledge now met with £4.1bn lent

Drawdowns

£2.0bn

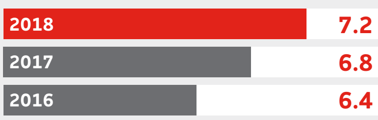
in 2018

RBS incentivised switching scheme readiness investment

c.£16m

in 2018

Core SME lending balances (£bn)



Despite persistent concerns around the uncertainty of Brexit negotiations impacting the confidence of UK companies, our SME business continued to perform strongly in 2018 with both loan and deposit balances growing. Activity was broadly spread across all sectors and loan purposes but demand for asset finance and acquisition finance was particularly strong. Loan losses are at very low levels reflecting not only disciplined loan origination over a period of years but also a very stable economic environment.

Progress against strategic priorities

Drive sustainable customer growth

- 2018 has seen continued momentum in our SME lending business, with a strong pipeline and drawdowns of £2.0bn.
- Origination flows remained broadly consistent with a strong prior year and we remain on track to achieve our £6bn lending commitment by 2019.
- Our core SME lending portfolio therefore increased by c.£400m to £7.2bn, up 5.6%, and ahead of system growth of 2.1%. This is due to a consistent and disciplined focus on serving the SME market, with our specialist sector offerings resonating particularly strongly with customers.

Capital optimisation

- Our SME IRB application progressed ahead of expectations during the year and in October 2018 the Group announced that it had received IRB accreditation for its SME portfolio – a year ahead of target.
- The Group has also continued to enhance its portfolio management capabilities during 2018 to ensure that it can target an optimal mix of capital and risk return for its SME lending.

Other highlights

- Our approach to specialisms continued to resonate with customers, with strong growth experienced across the portfolio particularly in acquisition finance for business services and lending to health and real estate, with the latter being driven in part by a strong demand for student accommodation.
- We maintained a robust approach to credit decisions on new lending in the year, reflective of the continued reduction in the impaired asset portfolio to £83m (2017: £126m). The underlying credit quality of the portfolio has remained broadly stable.

RBS alternative remedies package

- We are committed to supporting the RBS alternative remedies package where, given our existing SME banking capabilities, we believe we are well placed to compete for both schemes.
- We intend to fully participate in the Incentivised Switching Scheme and offer an attractive home to SME customers leaving RBS. In advance of this, we have invested c.£12m in building a bespoke switching and support team in Leeds and have also recruited a further c.50 relationship managers during 2018. This positions us well to effectively and efficiently switch RBS customers at scale when the scheme begins.
- We will also submit an application to 'Pool A' of the Capability & Innovation Fund which, if successful, would enable us to further enhance our competitive edge in SME banking and accelerate our growth plans. With a c.3.5% market share of BCAs today, we believe we are uniquely positioned to break through the Competition and Markets Authority's (CMA's) 5% market share competition barrier (the definition of a credible market competitor) to deliver effective competition in the marketplace.

Case study

Our commitment to supporting SMEs

As part of our commitment to supporting SMEs, we launched our SME Health Check Index – an in-depth report designed to 'take the temperature' of SMEs operating within the UK economy.

The study, which is published in partnership with The Centre for Economics and Business Research Limited (Cebr), creates a quarterly industry report that measures business performance and the macroeconomic environment affecting SMEs.

The SME Health Check Index combines various statistics and indicators to evaluate the health of the UK's SMEs, including business costs, employment, lending, revenue and capacity. In the fourth quarter of 2017, the Index fell to its lowest level since it began in 2014, driven by declines in business confidence, GDP growth and the rate of business creation. The index has recovered somewhat in the subsequent two quarters, although it remains well below the levels observed in previous years.

Each report is supported by a comprehensive media plan, stakeholder engagement activity with key industry contacts and organisations, as well as national and regional events. The Q1 2018 report was launched at the Houses of Parliament. The report is also widely shared and used by the Group's Relationship Managers through their own networks.

Strategic report

Delivering to our stakeholders

Delivering sustainable value for our customers, colleagues and communities is an integral part of our overall business model and key to our future success. Continuing to address our broader responsibility to society and managing the environmental impact from our day-to-day operations remains fundamental to our strategy and long-term ambitions.

Stakeholder groups	Interest and concerns	How CYBG responds
Customers	Understanding our customers and anticipating their needs has been our main focus in marketing and innovation this year. To stand out in a competitive landscape, where banks have to work increasingly hard to earn consumer trust, we shifted our focus in FY2018 to start a movement around getting the UK financially fit and launched a year-long campaign called B-Tox. We support and value information which allows customers to compare services by different account providers and strive to deliver the best possible customer service experience, so we were disappointed with our rankings in the CMA's first Service Quality Indicators Survey and the fall in our NPS. Other surveys, including BDRC's Moments of Truth study, show a more positive picture. To turn this around we continue to invest in our digital offering and are increasing staff training across our branches and in our contact centres. In addition, we recognise that tapping into customer sentiment needs to occur with increased frequency to build a holistic view. To assist with this, we introduced a new way of obtaining daily customer feedback via PACE – The Programme for the Acceleration of Customer Experience.	B is geared towards liberating people from money management worries. Our B-Tox themed quarterly campaigns are driving awareness of how the B app's features can help people get financially fit. We delivered active campaigns to enable customers to 'live where they love' through a series of cash-back schemes across our network. We now also provide same day mortgage appointments. A brand-wide upgrade of our mobile banking apps introduced new technology, including digital cheque imaging. The customer-focused designs delivered a more efficient money management platform, improving accessibility for our customers.
Colleagues	Our colleagues are integral to our ongoing success, and the overall business performance is dependent on their engagement and advocacy. Over the past year we have made great strides in accelerating the cultural transformation of CYBG on multiple fronts. Our goal is to foster a culture which attracts, retains, motivates and rewards people who consistently deliver ambitious, customer-focused-outcomes, regardless of their role. Valuing diversity among our colleagues has been fundamental to our positive cultural shift. We are striving to embed an inclusive culture, where every colleague can reach their full potential. We will continue to develop an open and transparent workplace, where respect, dignity, fair treatment, equality, tolerance and understanding are at the core of how people behave and interact.	Our culture is brought to life by our refreshed 'values and behaviours', which describe what is important at CYBG. Our new performance management framework reflects a forward-looking, team-based approach, allowing colleagues to be ambitious. Our colleague well-being strategy, as well as the new employee benefits platform, have become integral parts of our cultural transformation journey this year.
Communities	Boasting a proud heritage spanning more than 300 years combined, we have very strong roots in both Scotland and Yorkshire and are committed to supporting the communities we serve. We work in partnership with community organisations to tackle issues that are important to our customers and their local areas. We support critical front-line services for the most remote areas with Scotland's Charity Air Ambulance, as well as having brought environmental education to schoolchildren with the Wild about Scotland education bus. In Yorkshire, we help people who don't have access to a bike to borrow one for free through the Yorkshire Bank Bike Libraries. The financial education programmes we offer help support and augment our position as a responsible bank. To support Social Bite's campaign to end homelessness in Scotland, 300 staff took part in Sleep in the Park 2017. We are also proud to support the Yorkshire and Clydesdale Bank Charitable Foundation, which supports employee charitable giving, as well as providing grants to local charities, through the annual Spirit of the Community Awards.	Financial education – 650 hours invested by our employees and 'count me in 123' available to download free. Fundraising for Hospice UK – raising over £6.5m during the 10 years of our partnership. Spirit of the Community Awards – £160,000 of grants awarded. Yorkshire Bank Bike Libraries – delivering more than 60,000 opportunities to borrow a bike free of charge through 59 bike libraries. Wild about Scotland – reached 100,000 schoolchildren over our four-year partnership. Social Bite – £500,000 raised through participation in Sleep in the Park.

Engagement method	Frequency
We introduced the concept of B-Toxing your finances to our customers and to UK consumers at large, inspiring 5,000 people to enter the B-Tox Challenge across January and February 2018. We showcased the benefits of the B app for better money management via Coach B, who starred in a series of videos explaining tagging, projections and savings pots. Our consumer events on how to get financially fit at Studio B involved celebrities, journalists and B customers via live 'talk shows' and achieved widespread media coverage. We ran digital marketing campaigns across owned, earned and paid-for channels using the B-Tox theme, delivering messages across all channels and allowing all UK consumers exposure to the campaign at multiple touchpoints. We saw a 123% increase in the number of savings pots for B customers, a 97% increase in the number of B customers logging in to the app and the value of B savings pots doubling this year. Around 40% of B customers now associate the brand with financial fitness, supported by a 91% rise in use of the tagging feature in the B app. We achieved 97,000 responses through PACE – including 20,000 WOW alerts, which is feedback that has achieved the highest scores of 10 out of 10. CYBG personal customers relationship NPS declined by 3 points to 10, having been particularly impacted by branch closures and customer frustration over our internet banking transition.	Customers are at the heart of our business and providing a best-in-class service is our top priority. We actively invite customer comments on a daily basis and through several channels, including online surveys, touchpoint feedback and in person. Our insights team engaged with customers daily via PACE, supported by quarterly in-depth surveys with our B panel. We launched a new creative campaign each quarter of the financial year – for B, our creative campaign delivered a message around financial fitness via B-Tox.
We delivered engaging, multi-channel communications connecting colleagues to business performance and strategy. Our engagement score increased to 76%. Highlights include: – an above industry average open rate on CEO messages; – significant outperformance of the industry norm on measures of confidence in leadership and direction, respect and integrity and leading change; – 83% strongly believe in the Group's goals and objectives; and – 88% of colleagues fully support our values. We have enhanced our colleague engagement strategy by introducing new tools such as quarterly Pulse and feedback surveys to more regularly monitor colleague sentiment. We continue to facilitate open, conversational dialogue via social interactions on our digital channels and face-to-face events with our Leadership Team. We have seen a significant increase in comments, likes and ratings across our digital content throughout the year and 94% of colleagues said they would recommend attending a Let's Talk event with the Leadership Team.	Our new approach to performance management has enabled quarterly well-being conversations and annual aspirational discussions for every colleague. Our annual colleague MyVoice survey provides us with valuable insight on the culture of our business including in relation to our values and behaviours, as well as alignment with our strategy. Our communication channels enable regular dialogue on all aspects of our strategy with news articles on leadership, business, culture and community activity shared daily via our intranet.
We continue to build closer relationships with our community partners, strengthening relationships we are very proud of and passionate about. Our current community engagement involves: – regular stakeholder meetings to support the delivery of our community partnerships; – colleagues volunteering for our community projects – contributing 2,000 hours of their time over this financial year; – giving our expertise and providing pro bono support for our community partners; – giving space in our branches to our community partners; – employee fundraising for charitable causes, which is match-funded by our Charitable Foundation; and – providing grants each year through our Charitable Foundation to local charities that support employment, financial education and the local environment, as well as grants of up to £500 for employees involved with charities outside of work.	Year-round support for financial education and supporting employees to get involved. Quarterly campaigns with Hospice UK and annual Group-wide fundraising challenge. Monthly meetings with community partners. Daily engagement with a wide variety of community groups through our branch network.

Strategic report

Delivering to our stakeholders

Our culture

Our colleagues are integral to our ongoing success and our overall business performance is dependent on their engagement and advocacy, underpinned by a strong risk culture. Over the past year, significant progress has been made accelerating the cultural transformation of CYBG.

Our 'values and behaviours' continue to be embedded. Our values – Be ambitious, Be courageous, Be all over it, Be curious and Be connected – are brought to life through their associated behaviours. Every team continues to personalise the behaviours to their business area, and every colleague sets personal goals in relation to our values to support their own development. By turning words into actions, we are building a Group where colleagues are focused on meeting the needs of both their own development and our current and future customers.

Great leadership framework has been in place for a year and all leaders play a critical role in creating culture and driving performance. Our leaders are being supported, through targeted leadership development, to help them Lead with Purpose, Drive Inclusion, be Always Agile, Grow Trust, Be Connected and Stretch Possibilities.

Recruitment and performance management have been overhauled this year to reflect our cultural aims. Our approach has been transformed to a team-focused, forward-looking approach helping every colleague to achieve their personal best. Our new framework has captured 100,000 pieces of feedback, created 28,000 well-being conversations and ensured every colleague within the Group has had a development discussion. Internal and external selection is based on our values, ensuring we recruit and promote colleagues aligned with our culture.

Employee benefits have been transformed this year through the launch of our Flex Benefits portal, representing another key milestone in our cultural journey. This new reward framework forms an integral part of our people strategy, recognising the diversity of colleagues and empowering them to make the benefit choices appropriate for individual circumstances.

Employee well-being has also become a vital part of our cultural journey. The introduction of our first 'Well-being in the Workplace' survey has shown our commitment to creating an inclusive, safe and healthy environment where people can excel. The relaunch of our mental health awareness training module and People Leader toolkit has helped ensure colleagues feel supported and have the right tools available to them.

Engagement and communication

We have continued to evolve and enhance the way we communicate with colleagues. We have launched new digital channels such as our weekly CEO email and delivered diverse strategic content via our intranet relating to customers, our culture, business performance and community engagement. We continue to have a highly visible CEO and Leadership Team and have expanded our interactive Let's Talk events. We have increased colleague engagement with social features, such as likes and comments, and generated greater interaction with polls and surveys. This year our internal communications team lifted the 'Brilliance in Internal Communications Campaign' accolade at the IC Brilliance Awards.

Inclusion

Inclusion is at the heart of our culture. It's written into our values. We are committed to fostering and sustaining a truly inclusive culture where every colleague and customer feels they belong. We want all colleagues to recognise this and work together to ensure inclusion achieves its promise. We ensure equality, diversity and inclusion by concentrating on making sure every colleague feels comfortable to be themselves, to ask questions, to be curious and operate at their personal best.

We continue to make great strides in developing a diverse and inclusive culture, with five colleague network groups for gender, age, disability, ethnicity and sexual orientation, all sponsored by members of our Executive Leadership Team.

Some specific highlights of the year include:

- events and activities held to celebrate and improve our awareness of International Women's Day, National Inclusion Week, LGBT History Month and religious celebrations including Raksha Bandhan and Eid-ul-adha;
- continuing to work closely with LGBT Youth Scotland to broaden our reach and connection in the community, with our LGBT network representing CYBG at Glasgow Pride for the second year;
- introducing our guidance to support colleagues transitioning in the workplace and developing this work to ensure a smoother transitioning journey for both colleagues and customers; and
- working with colleagues to strengthen and modernise our existing practises in relation to flexible working, attendance and family friendly policies.

Gender pay gap

This year marks the second publication of our Gender Pay Gap report in accordance with the UK Government regulations for gender pay gap reporting. While we are confident we do not have an equal pay issue, we are committed to addressing the root causes of the gender pay gap. As a signatory to the Women in Finance Charter, we have committed to a target of 40% females in senior management roles by 2020.

Over the course of the year we have developed a much greater understanding of the drivers of our gender pay gap and of the long-term actions required to address it.

Our overall mean and median gender pay and bonus gap, based on a snapshot date of 5 April 2018 (pay) and bonus paid in the 12 months to 5 April 2018, are:

	Mean 2018	Median 2018
Hourly pay gap	36%	38%
Bonus pay gap	56%	41%

	Mean 2017	Median 2017
Hourly pay gap	37%	36%
Bonus pay gap	58%	39%

Percentage of colleagues who received a bonus:

	2018	2017
Male	93%	85%
Female	94%	90%

The key driver behind the pay gap is that we still have more men than women in senior roles and more women than men in our customer facing roles, which are often more junior. In addition, our bonus pay gap is partly driven by the fact that bonus calculations are not adjusted to reflect colleagues who work part-time and, while we encourage all colleagues to work flexibly, the majority of those who currently do are women.

In leadership terms, we are committed to 40% women in senior roles by 2020. As at 30 September 2018, we are at 38%.

As at 30 September 2018, our strong, diverse and engaged network of colleagues included:

- 5,762 permanent full-time equivalent (FTE), 59% of which are female, 41% male;
- three women and eight men on the Board; and
- three women and seven men in our Executive Leadership Team.

There are a number of steps we are taking to improve our gender balance that we expect to positively impact our gender pay, including:

Culture

- Introducing our 'Return to Work' programme, to support women returners.
- Working with colleagues to identify opportunities to enhance our flexible working proposition, particularly in more senior roles.

Reward

- In 2018, we focused on making positive changes to our pay scale to target junior colleagues.
- We continue to formally link executive reward to our inclusion targets.
- We conduct our equal pay audit in partnership with our trade union, Unite.

Development

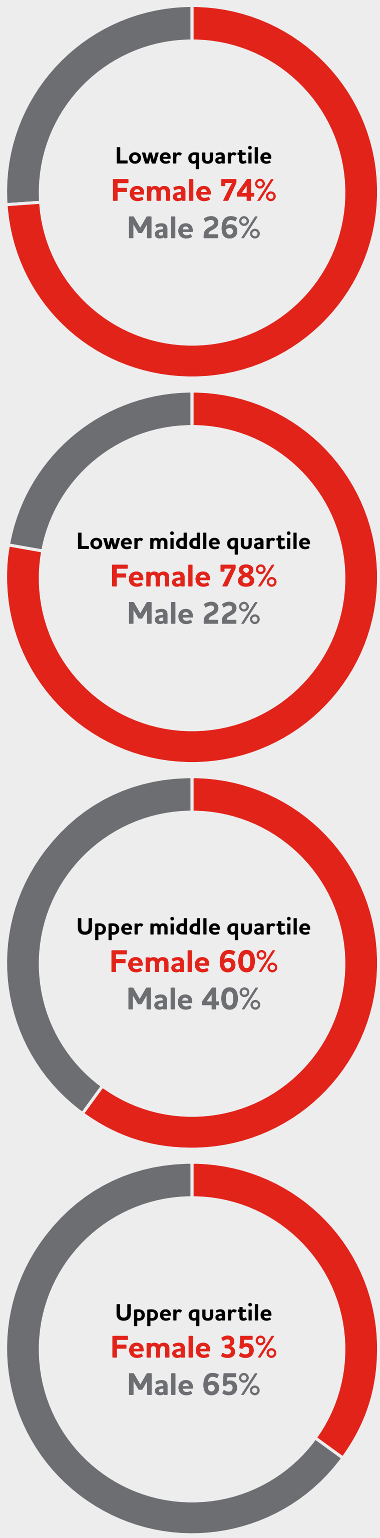
- We continue to drive a gender-balanced intake of graduates.
- This year we introduced our Career Sponsorship programme to develop a diverse pipeline of future leaders.
- We channel development opportunities through our Inclusion networks.

We are encouraged that the changes we are making are having an impact. In our last colleague survey, 86% of colleagues believe the Group supports workplace diversity and 82% feel the Group promotes an inclusive culture where they feel they can come to work and be themselves.

Our strategy is to create a culture of inclusion for everyone that works in the long term interests of customers, colleagues and shareholders, as well as society as whole.

We recognise that there is still a lot more to be done and building on the progress of this year, we will continue to shape a more diverse and inclusive culture at the Bank.

Proportion of males and females in each pay quartile
(each containing just over 1,563 colleagues, shown lowest to highest)



Strategic report

Delivering to our stakeholders

Environment

During the year, the Group made a contribution towards the drive for a low carbon and more resource efficient economy through:

- reprocuring 100% renewable green energy for all electricity supplies within the Group's direct control for the next two years;
- changing waste management supplier to drive improved levels of recycling across the business;
- continuing with the roll-out of advanced building efficiency management systems as part of the branch refurbishment programme. Such systems help automate controls to ensure we only operate air conditioning units and boilers within set operational hours and can respond quickly to changes in temperatures; and
- retention of our Carbon Trust accreditation to December 2019.

Reporting on greenhouse gases (GHG) emissions

The reporting period for GHG emissions in the Group ran from 1 July 2017 to 30 June 2018.

Total emissions for the Group have reduced by 16% in the last year. Nearly half of the reduction is driven by changes in the emission factors as defined by the Department for Business, Energy & Industrial Strategy (BEIS) guidelines. The Group used the 2017 Department for BEIS emission factors due to the timing of the release of the 2018 emission factors. The largest change in emission factors is the decarbonisation of electricity generated by the National Grid. Using the same emission factor for both the 2017 and 2018 reporting years and accounting for the impact of FTE and portfolio changes, the reduction in emissions would be 3%.

GHG emissions CO_2e tonnes

Scope	2018	2017
Scope 1 emissions Generated from the gas and oil used in all buildings where the Group operates; emissions generated from Group-owned and leased vehicles used for business travel; and fugitive emissions arising from the use of air conditioning and chiller/refrigerant plant to service the Group's property portfolio.	**3,100△**	3,297
Scope 2 emissions Generated from the use of electricity in all buildings from which the Group operates.	**11,398△**	14,247
Scope 3 emissions Relate to business travel undertaken by all colleagues using rail, private vehicles, hired vehicles, contracted taxi services, air travel, waste, water and paper.	**5,938**	6,803
Total	**20,436**	24,347

The Group reports GHG emissions in accordance with the GHG Protocol, which sets a global standard for how to measure, manage and report GHG emissions. The above figures use location-based emissions. Using market-based emissions for energy would reduce total scope 2 emissions for the Group from 11,398 to 506△ as this enables the Group to apply certificates that demonstrate electricity has been produced from renewable sources.

Intensity ratio

The Group has chosen to use an intensity ratio of GHG per average FTE for scope 1 and 2 emissions. Using FTE offers a simple way to measure and monitor Group performance on emissions and is also a useful way to benchmark and compare with others.

Scope (1 and 2)

	2018	2017
GHG emissions per average FTE	**2.25**	2.61

The only estimated emissions in the GHG emission data relate to energy consumed in properties where the landlord controls the supply and recharges the Group via a service charge arrangement or where actual meter readings were not available before year end. In these instances an average rate per kWh has been used.

Independent limited assurance

The Group engaged KPMG LLP to undertake an independent limited assurance engagement over the selected information highlighted in this report with a △.

KPMG has issued an unqualified opinion over the selected information. The full statement is available on the CYBG website.

Progress against targets

We have four environmental targets to measure the Group's performance over a three year period in comparison to a baseline in June 2016. We have made strong progress against three. While improving by 2%, there is still work to do in the next 12 months to increase the volume of recycling across the Group's operational business through promoting staff awareness and improving in-house recycling processes. Actions are well advanced and we should meet our 2019 target.

Area	2016 restated baseline*	2018 actual	2016-18 % change	2019 % target	2018 performance
GHG – measured by CO_2e	22,602	**20,436**	10%	9%	**On target**
Energy (gas and electric) – measured by gigajoules (GJ)	165,541	**150,779**	9%	9%	**On target**
Water consumption – measured by m^3 volume	77,286	**71,749**	7%	5%	**On target**
Recycling first line waste – measured by % volume	74%	**76%**	2%	6%	**Behind target**

*2016 Baseline has been restated to reflect changes in emission factors, property portfolio and FTE numbers during the course of 2016/17.

Modern Slavery Act statement

CYBG has a zero tolerance to slavery, servitude, forced labour and human trafficking (Modern Slavery) and is committed to conducting business with honesty and integrity and treating everyone with dignity and respect.

We are committed to working with our partners and suppliers to raise awareness and understanding of modern slavery and eliminating the practice from the supply chain.

The statements detailing the actions we have taken to achieve this can be found on our website at: www.cybg.com/about-us/modern-slavery/

Non-financial information statement

We aim to comply with the new non-financial reporting requirements contained in Sections 414CA and 414CB of the Companies Act 2006. The table below, and the information it refers to, is intended to help stakeholders understand our position on key non-financial matters.

Reporting requirement	Policies and standards which govern our approach	Risk management and additional information	
Environmental matters	Environmental Reporting Policy	Environment, page 30	
Employees	Employee Conduct Policy; Fit and Proper Policy; Health and Safety Policy; Whistleblower Policy; Physical and Personal Security Policy; Inclusion Policy	Colleagues, pages 26-27 Our culture, page 28 Gender Pay Gap, page 29 Corporate governance report, pages 62-67	Audit Committee report, page 72
Human rights	Modern Slavery Statement; Privacy and Data Protection Policy; Information Security Policy; Data Management Policy	Modern Slavery Act, page 31 Corporate governance report, pages 62-67 Risk Committee report, pages 79-83	Risk report, page 121 Financial Crime risk, page 168
Social matters	Corporate Responsibility Policy; Political Contact, Communications and Donations Policy; Responsible Lending Policy; Sanctions and Embargo Policy	Community, pages 26-27 Corporate Governance report, pages 62-67 Directors' report, page 116	
Anti-corruption and anti-bribery	Anti-Bribery and Corruption Policy; Anti-Money Laundering and Counter Terrorist Financing Policy; Preventing Fraud and Cyber-Enabled Crime Policy	Corporate governance report, pages 62-67 Financial crime risk, page 168	
Policy embedding, due diligence and outcomes		Risk overview, pages 16-17	Risk report pages 121-170
Description of principal risks and impact of business activity		Risk overview, pages 16-17 How we create value, pages 12-13	Principal risks, page 17
Description of the business model		Group at a glance, page 2	How we create value, pages 12-13
Non-financial key performance indicators		Strategy and performance, pages 14-15 Operational review, pages 20-24	Delivering to our stakeholders, pages 26-29 Environment, page 30

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Case study

Funding to improve the way we live

CYBG is well regarded for its expertise in the healthcare sector – specifically in care homes where we are viewed as experts in the changing needs of this multi-billion pound industry.

Oakdale Care Group

In 2016, Oakdale Care Group, a new elderly care home operator, secured a £13m funding package from Clydesdale Bank. The Buckinghamshire-based business has an aim to become a leading provider of elderly care facilities with plans to deliver three new 66-bed residential homes in the Northern Home Counties region. The Group plans to create a chain of care homes offering over 600 beds, over the next few years.

The Group supported the development of two of the homes – now fully completed – as well as a third home set to open in January 2019. The Group recently acquired an 'outstanding' CQC rating for the first home they built – a huge achievement (practically unheard of in the industry) and a testament to the strong management team Clydesdale Bank has backed.

The care homes provide a mixture of residential and dementia care, and are high-end facilities, providing cinema and garden rooms, landscaped gardens, tea and coffee 'shops' and much more, as well as being eco-friendly with solar panels.

Oakdale chose Clydesdale Bank because of the Bank's specialist knowledge in development funding and the healthcare sector, born from a wealth of previous experience in supporting the build of new care homes.

This is yet another example of our Group's commitment to supporting the ambitions of SMEs in the Health and Social Care sector. Through the great work of our Health and Social Care team, we have earned a strong and positive reputation for providing expertise to these businesses across the UK, helping to get major projects off the ground that provide crucial support to vulnerable members of society.

Project Battersea

A well-established developer of luxury care homes for the elderly is in the process of developing a new flagship facility based in Battersea in London, with £19,956,000 support from Clydesdale Bank. The award-winning Cinnamon Care Collection will redevelop the formerly closed Four Seasons York House Care Home, in order to increase bed capacity from 58 to 78 beds, alongside the construction of 28 extra care units across two new floors on top of the existing building. The new care home will be the fifth project to be funded by the Bank for Cinnamon Care, and its most ambitious to date in terms of the size of the development.
The new facility will be located just a stone's throw from one of London's most popular green spaces, Battersea Park, in the Borough of Wandsworth, and will provide high quality elderly care to residents.

Financial results

Overview of Group results

The Group has consistently delivered against each of its strategic priorities – sustainable customer growth, efficiency and capital optimisation – and is now a year ahead of plan.

The Group delivered an underlying profit before tax of £331m, up £38m (13%). Increased underlying profitability has been the primary driver for the increase in underlying RoTE from 7.5% to 10.6%, and underlying basic EPS from 21.5p to 30.4p.

A statutory loss after tax of £145m has been reported (2017: profit of £182m) primarily due to legacy conduct costs of £396m in the year (2017: £58m).

The section below details the Group's progress through each of its strategic objectives.

Summary balance sheet

as at 30 September	2018 £m	2017 £m
Customer loans	**33,281**	31,967
Other financial assets	**9,234**	10,469
Other non-financial assets	**941**	795
Total assets	**43,456**	43,231
Customer deposits	**(28,854)**	(27,679)
Wholesale funding	**(8,095)**	(8,602)
Other liabilities	**(3,321)**	(3,548)
Total liabilities	**(40,270)**	(39,829)
Ordinary shareholders' equity	**(2,736)**	(2,952)
Additional Tier 1 (AT1) equity	**(450)**	(450)
Equity	**(3,186)**	(3,402)
Total liabilities and equity	**(43,456)**	(43,231)

Summary income statement(1)

for the year ended 30 September	2018 £m	2017 £m
Net interest income	**851**	844
Non-interest income	**156**	172
Total operating income	**1,007**	1,016
Underlying operating and administrative expenses	**(635)**	(675)
Operating profit before impairment losses	**372**	341
Impairment losses on credit exposures(2)	**(41)**	(48)
Underlying profit on ordinary activities before tax	**331**	293
Restructuring and related expense	**(38)**	(67)
Virgin Money acquisition costs	**(37)**	–
RBS alternative remedies package spend	**(16)**	–
Separation costs	**(8)**	(8)
Legacy conduct costs	**(396)**	(58)
Gain on defined benefit pension scheme reforms	**–**	88
Gain on disposal of VocaLink share	**–**	20
Statutory (loss)/profit on ordinary activities before tax	**(164)**	268
Tax credit/(expense)	**19**	(86)
Statutory (loss)/profit attributable to equity holders	**(145)**	182

(1) The summary income statement is presented on a statutory and underlying basis. In addition, the financial key performance indicators (KPIs) used by management in monitoring the Group's performance and reflected throughout this section are determined on a combination of bases (including statutory, regulatory and alternative performance measures), as detailed in the Glossary on page 246. A reconciliation from the underlying to statutory basis is shown on page 42 and management's rationale for the adjustments is shown on page 248.

(2) Impairment losses on credit exposures relate solely to loans and advances to customers (refer to note 3.5 to the financial statements) and exclude credit risk adjustments on loans at fair value through profit or loss which are incorporated in the movement in other assets and liabilities at fair value within non-interest income (refer to note 2.3 to the financial statements).

Financial results

Overview of Group results

Underlying profit before tax
£331m
2017: £293m

Statutory loss after tax
£145m
2017: Profit £182m

RoTE – underlying
10.6%
2017: 7.5%

Deposit growth
4.2%
2017: 2.5%

Core loan growth
4.7%
2017: 6.9%

NIM
2.17%
2017: 2.27%

Underlying CIR
63%
2017: 67%

Cost of risk
0.12%
2017: 0.14%

Basic EPS – underlying
30.4p
2017: 21.5p

CET1 ratio
10.5%
2017: 12.4%

Pro forma IRB CET1 ratio
14.0%

Pro forma IRB total capital ratio
21.3%

Outlook for 2019

Political uncertainty related to Brexit continues to cast a shadow over the UK's short-term economic prospects. The central case projections published by many economists are based on the assumption of an orderly Brexit and forecast a temporary slowdown in GDP growth while other key economic indicators remain broadly stable. The Group is well prepared for that outcome and has also undertaken contingency planning for alternative scenarios.

Following the acquisition of Virgin Money on 15 October 2018 the Group begins FY2019 strongly capitalised and well funded with a bigger, broader business that is well prepared for the year ahead.

The short-term outlook for the Group's key lending markets – UK homeowners and SMEs – is more subdued than in recent years. In addition, the UK household savings ratio continues to decline, limiting growth in the supply of deposits. However, the Group's proven ability to win market share through superior product offerings and customer service, and to optimise its liability mix across a range of sources of funding means we expect to continue to deliver sustainable growth in customer balances.

We expect to see strong competition for mortgages and deposits in the year ahead that will feed through into margin pressure. However, the Group's broad range of lending businesses allied to its diversified funding model will enable us to continue to manage margins effectively. The Net Interest Margin for FY2019 is expected to be between 1.6 and 1.7%, having been rebased following the combination with Virgin Money.

Our strong track record in delivering cost efficiencies will help to underpin the Group's profits and capital generation. We expect the Group's underlying operating expenses to be less than £950m in FY2019, down from an estimated pro forma combined cost base of £985m in FY2018.

The Group expects to update stakeholders on strategy and other matters, including the development of medium-term performance targets, at a Capital Markets Day in June 2019.

Ian Smith
Group Chief Financial Officer

Financial performance review

1. Sustainable growth in customer lending and deposit balances

	2018 £m	2017 £m
Mortgages	**24,540**	23,480
SME lending[1] – core	**7,202**	6,821
– non-core	**336**	504
Unsecured personal lending	**1,203**	1,162
Gross loans and advances to customers	**33,281**	31,967
Current accounts[2]	**(14,224)**	(13,798)
Variable rate savings accounts[2]	**(8,427)**	(7,880)
Fixed rate term deposits[3]	**(6,202)**	(5,983)
Other wholesale deposits	**(1)**	(18)
Total customer deposits	**(28,854)**	(27,679)

Mortgages

The mortgage book remains the Group's largest asset portfolio and has a significant impact on our overall financial performance. Our continued focus on customers has resulted in growth of 4.5% in the year, higher than system growth[4] of 2.5%. Our market share increased from 1.73% to 1.77%.

The mortgage market in 2018 has been more subdued, with high remortgage activity, but lower levels of new lending and the competitive environment has continued to exert pressure on front book pricing. In late 2017, we brought mortgage processing back onshore, as part of our customer journey improvement initiatives. Some servicing and fulfilment delays arose resulting in our broker pipeline build being lower than we had hoped, with mortgage growth slower around the third quarter of the financial year when we felt the impact of lower applications at the start of 2018. These issues are now resolved, with a return to a more normalised level of growth in the final quarter.

We continued to see customers favour fixed rate mortgage products, as they sought to further capitalise on the prevailing low interest rate environment against a backdrop of market sentiment that expects modest short to medium-term interest rate rises. This, combined with our targeted customer retention strategy, has resulted in growth in the fixed rate book to 78% of total mortgage balances (2017: 73%) and accounted for 96% of mortgages drawn in the year (2017: 95%). Longer-term fixed rate mortgages are growing more popular with 5-year fixed mortgages now accounting for 27% of the portfolio (2017: 22%).

In line with our expectations, the buy-to-let (BTL) property market has been more subdued following last year's changes in tax relief for landlords, an increase in Stamp Duty and the PRA's enhanced affordability assessments. This has led to a shift in the mix of our mortgage book with BTL falling from 33% in the prior year to 31% with owner occupied accounting for a higher proportion of drawdowns in the year (79%, up from 70% in the year to 30 September 2017). Reflecting this change in mix, the average loan to value (LTV) of new lending was 70% (30 September 2017: 71%) and the average LTV of the mortgage book increased from 57.5% to 58.8%. Our proportion of residential mortgages 90 days in arrears has remained stable at 0.56% (2017: 0.52%).

SME lending

Our core SME lending portfolio increased by £381m (5.6%) in the year, in line with market guidance and ahead of system growth[5] of 2.1%. Growth has been delivered across term lending, asset finance and invoice finance. We are outperforming the market, despite the subdued demand resulting from Brexit uncertainty, as a result of our strong propositions and sector focus, while maintaining high credit underwriting standards. We are delivering on our pledge to support small and medium sized businesses across the UK as part of our commitment to lend £6bn in the three years to 2019. Lending origination targets have been achieved or exceeded in each of our core regions and this, coupled with lower attrition in the year, has contributed to the overall increase in balances.

The SME portfolio remains well positioned. Underlying asset quality is resilient and stable, reflective of the diversity within the portfolio as a result of controlled risk appetite and an economic environment which continues to support business performance. The impaired asset portfolio has reduced to £83m (2017: £126m) which is at its lowest level for more than 10 years.

In line with our strategy we continued to proactively run down our non-core portfolio, which reduced from £504m to £336m through the managed exit of non-core balances.

(1) Includes financial assets at fair value of £362m (September 2017: £477m).
(2) £150m of current account balances were reclassified as variable rate savings balances in the comparative period.
(3) Includes financial liabilities at fair value of £15m (September 2017: £26m).
(4) System growth is sourced from the Bank of England (BoE) 'Mortgages outstanding by type of lender, UK (BoE)' report (MM4).
(5) System growth is sourced from the BoE 'Industrial analysis of monetary financial institutions' lending to UK residents' report (C1,2), and excludes individuals and individual trusts, activities auxiliary to financial intermediation, insurance companies and pension funds, and financial intermediation (excluding insurance and pension funds) results.

Financial results

Financial performance review

Unsecured personal lending

Unsecured personal lending has grown by 3.5% or £41m in the year to £1,203m. This has been driven largely by a focus on the fixed rate personal loans portfolio which increased by 13% from a low base of £658m to £743m. We have improved our presence on aggregator websites and offered existing customers enhanced accessibility to our products, introducing in-app purchase functionality and allowing customers that are pre-assessed for credit worthiness to secure a loan at the click of a mouse. The fixed rate personal loan market remains highly competitive, resulting in some margin erosion, as market rates have dipped to near historical lows and are yet to respond to the rising rate environment.

Growth in the fixed rate personal loan book was slightly offset by a fall in credit card balances of £15m to £381m (2017: £396m). Variable rate personal loans and overdrafts fell by £32m in the year from £111m to £79m. Variable rate loan balances continue to reduce as, although these products remain on sale, they are not actively promoted or targeted.

Current accounts

Current account funding increased by £426m in the year from £13,798m to £14,224m due principally to continued growth in business current account balances (up £328m) with the Group continuing to see new customer recruitment from the 25-month fee free offer launched in December 2016. An unprecedented number of new personal current accounts were opened following our high profile national personal current account recruitment campaign, which had a market leading customer switching incentive. The B current account was the main beneficiary of the campaign (with balances up £256m) while there was a reduction of £158m in the Current Account Plus and other personal current account products. The new B account openings were in line with our strategy to sustainably grow this portfolio in a way that recruits new customers with whom we have an opportunity to build a long-term relationship.

Variable rate savings accounts

Funding from variable rate savings accounts increased by £547m principally driven by £783m of growth in B savings accounts and £116m in business savings accounts, the latter being driven through targeted relationship management. Partially offsetting this is attrition of £228m in cash ISA balances following continued product simplification and repricing of the portfolio. There has been a change in book mix, with a higher proportion of balances being held in longer-term notice products, providing an additional liquidity benefit.

Fixed rate term deposits

Our fixed rate term deposit book increased by £219m to £6,202m as a result of deposit raising initiatives taken primarily in the first quarter of the year, including the successful launch of our second online digital bond along with two further cash ISA fixed rate bonds designed to retain maturing term deposits. As a result of close margin management and deposit initiatives, funding costs have fallen as the number of longer-term higher priced products were allowed to mature without replacement.

Funding and liquidity

The Group continues to maintain its strong funding and liquidity position and seeks to achieve an appropriate balance between profitability, liquidity risk and capital optimisation. Reflecting our retail deposit-led funding strategy, our loan to deposit ratio was stable over the year at 115% (2017: 115%).

In addition to retail deposits, we ensure appropriate diversification in our funding base through a number of wholesale funding programmes. In the first half of the year we made further drawings from the BoE Term Funding Scheme (TFS), taking overall drawings at 30 September 2018 to £2.25bn. We have accessed TFS judiciously – we have not relied on it to fund our growth and our drawings are at a level that can be refinanced comfortably over time. We have also maintained our access to public markets – we successfully completed further issuances of mortgage-backed securities through the Group's Lanark programme across USD and GBP tranches, raising approximately £500m and £550m in January and July respectively. The Group's liquidity surplus continues to comfortably exceed our regulatory minimum and internal risk appetite, with a Liquidity Coverage Ratio (LCR) of 137% as at 30 September 2018 (2017: 164%). Net Stable Funding Ratio (NSFR) was 119% at 30 September 2018 (2017: 118%).

The issue of £500m of senior debt in September provided further funding to the Group and reflects our progression towards meeting the BoE's Minimum Requirement for Own Funds and Eligible Liabilities (MREL) by 2022.

Net interest income

Average balance sheet	2018 Average balance[(1)] £m	2018 Interest income/ (expense) £m	2018 Average yield/(rate) %	2017 Average balance[(1)] £m	2017 Interest income/ (expense) £m	2017 Average yield/(rate) %
Interest-earning assets						
Mortgages	**24,051**	**657**	**2.73**	22,439	652	2.91
SME lending[(2)]	**7,311**	**288**	**3.94**	7,110	264	3.71
Unsecured personal lending	**1,210**	**101**	**8.35**	1,172	105	8.99
Liquid assets	**6,081**	**34**	**0.57**	6,007	21	0.34
Due from other banks	**764**	**4**	**0.47**	969	2	0.17
Swap income/other	**–**	**29**	**n/a**	–	31	n/a
Total average interest-earning assets	**39,417**	**1,113**	**2.82**	37,697	1,075	2.85
Total average non-interest-earning assets	**2,891**			2,489		
Total average assets	**42,308**			40,186		
Interest-bearing liabilities						
Current accounts	**11,127**	**(11)**	**(0.10)**	11,032	(6)	(0.05)
Savings accounts	**8,136**	**(36)**	**(0.44)**	7,832	(32)	(0.41)
Term deposits	**6,306**	**(102)**	**(1.61)**	5,190	(89)	(1.71)
Wholesale funding	**7,294**	**(113)**	**(1.56)**	6,940	(104)	(1.51)
Total average interest-bearing liabilities	**32,863**	**(262)**	**(0.80)**	30,994	(231)	(0.75)
Total average non-interest-bearing liabilities	**6,070**			5,926		
Total average liabilities	**38,933**			36,920		
Total average equity attributable to ordinary equity holders	**3,375**			3,266		
Total average liabilities and average equity attributable to ordinary equity holders	**42,308**			40,186		
Net interest income		**851**			844	

(1) Average balances are calculated using the daily balances across the year.
(2) Includes loans designated at fair value through profit or loss.

We guided to a reduction in NIM this year as we expected to see the impact of the shift in our mortgage mix towards a higher proportion of lower yielding owner-occupier lending, together with the continuation of competitive mortgage pricing over the last two years, all feeding through into lower average rates across the mortgage book. Group NIM of 2.17% was in line with guidance of c.220bps, down from 2.27% since FY2017. Furthermore we continue to see mortgage customers favouring fixed rate deals and this customer preference, alongside proactive early retention programmes in the marketplace, continues to exert pressure on average mortgage margins through competitive fixed rate pricing. Nonetheless, the Group continues to drive net interest income growth through its sustainable balance sheet growth strategy.

Pricing in the unsecured personal lending market remains very competitive and the total average gross yield across the book was 8.4% (2017: 9.0%).

Offsetting the margin pressure in our Retail asset portfolios we saw improved average customer rates in our SME book, benefiting from pricing discipline and a higher interest rate environment. In addition we actively managed our funding volumes and pricing to support NIM.

Non-interest income

Non-interest income reduced by £16m (9%) in the year from £172m to £156m. Net fee and commission income reduced by £5m in the year principally due to a £6m cost for the personal current account incentives campaign which resulted in increased current account volumes, supporting our customer growth strategy. In addition, we saw net fair value losses of £3m in FY2018 compared to net fair value income of £6m in the prior year. The swing of £9m included £2m of hedge ineffectiveness and £7m of other fair value items that are not expected to recur.

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Impairment losses on credit exposures

Impairment losses decreased from £48m to £41m. Net cost of risk was 2bps lower reflecting strong portfolio quality and benign economic conditions. The reduction includes a lower charge taken on our SME exposures primarily as specific provisions were lower than previous years offsetting an increase in the impairment charge for Retail exposures. By contrast we have experienced increased impairment losses for our Retail unsecured portfolios resulting from the combined effect of personal loan portfolio growth, higher default rates on lending originated in earlier years and a lower level of recoveries.

	2018				2017			
	Retail – secured bps	Retail – unsecured bps	SME bps	Total bps	Retail – secured bps	Retail – unsecured bps	SME bps	Total bps
Gross cost of risk	1	281	36	19	2	266	70	28
Specific provision releases and recoveries				(6)				(12)
Fair value loans				(1)				(2)
Net cost of risk				12				14

2. Delivering on our efficiency programme

Operating and administrative expenses	2018 £m	2017 £m
Personnel expenses	216	248
Depreciation and amortisation expenses	89	87
Other operating and administrative expenses	330	340
Total underlying operating and administrative expenses	635	675
Restructuring and related expense	38	67
Virgin Money acquisition costs	37	–
RBS alternative remedies package spend	16	–
Separation costs	8	8
Legacy conduct charges	396	58
Gain on defined benefit pension scheme reforms	–	(88)
Total statutory operating and administrative expenses	1,130	720

In 2016, we committed to delivering a net reduction of £100m in underlying operating expenses. In 2018, we completed our Sustain efficiency programme and achieved run rate benefits that exceeded our targets. On an underlying basis, total operating and administrative expenses have fallen by £40m to £635m.

Personnel expenses fell from £248m to £216m, driven by headcount reductions following last year's voluntary severance programme, as well as the closure of the defined benefit pension scheme to future accrual on 1 August 2017. This reduction has been delivered while building an improved reward package across CYBG which has been a key area of focus in 2018. Improvements have included consolidated pay increases, enhanced defined contribution pension provision and the introduction of a flexible benefits account worth up to 5% (capped at £2,500) of salary from 1 January 2018 for all colleagues below Executive Director. In addition, in recognition of the delivery of an unprecedented level of change in FY2017, all eligible colleagues received £500 of free shares in December 2017 at a cost of £3m.

Costs related to the restructuring and streamlining of our business have fallen by £29m to £38m, largely due to a lower volume of restructuring initiatives in the year. Costs have been of a similar nature to the prior year but on a smaller scale as the majority of the Sustain initiatives were undertaken in prior financial years.

Transaction related costs of £37m were recognised in regard to the acquisition of Virgin Money and £16m of costs were incurred relating to preparation for the RBS alternative remedies package.

Statutory operating and administrative expenses have increased by £410m driven largely by legacy conduct charges. In line with the rest of the industry, the Group has experienced a sustained period of elevated Payment Protection Insurance (PPI) complaints during the year, ahead of the August 2019 industry deadline. In addition to the £350m charge recognised in the first half of FY2018, the Group has reassessed the level of provision that is considered appropriate to meet current and future expectations in relation to the mis-selling of PPI policies. The Board noted that weekly incoming complaint volumes have been reducing in the second half of FY2018. Notwithstanding the improvement the Board concluded that an additional charge of £150m is required. During the year the Group drew down the full amount of the remaining indemnity cover (£148m) as the increased provision was partially covered under the terms of the conduct indemnity deed entered into with National Australia Bank (NAB). The balance of £352m has therefore been recognised as a charge to the income statement. We continue to expect a slowdown in complaint volumes into FY2019 due to the impact of the Financial Guidance and Claims Act that became effective in July which implemented a fee cap and limits to cold-calling for Claims Management Companies. The Group has also recognised additional costs of £44m for other less significant conduct related matters. The Group continues to assess the impact of resolving legacy conduct issues on an ongoing basis.

3. Capital optimisation

	2018 £m	2017 £m
CET1 capital	**2,113**	2,437
AT1 capital	**450**	450
Tier 2 capital	**626**	627
Total capital	**3,189**	3,514
Risk weighted assets	**20,102**	19,678

	2018 % bps	2017 % bps
At 1 October	**12.4%**	12.6%
Generated	**185**	168
Asset growth	**(23)**	(42)
Investment spend	**(85)**	(93)
AT1 distributions	**(14)**	(20)
Underlying capital generation	**63**	13
Non underlying items – conduct	**(182)**	(27)
Non underlying items – Virgin Money transaction costs	**(18)**	–
Non underlying items – restructuring costs	**(16)**	(31)
Other	**(34)**	25
Net capital absorbed	**(187)**	(20)
At 30 September	**10.5%**	12.4%

The Group's fully loaded total capital ratio was 15.9% and the CET1 ratio stood at 10.5% at 30 September 2018. The reduction in the capital ratios related primarily to legacy conduct charges.

Underlying capital generation was 63bps, largely driven by strong underlying profits offset by growth in mortgages and SME lending with risk weighted assets (RWAs) increasing by £424m. Investment spend absorbed 85bps as the Group has invested heavily in our digital proposition to improve the customer experience and drive operational efficiencies.

Formal IRB accreditation for the mortgages and SME portfolios was received in October 2018. The adoption of IRB models is expected to result in a material reduction in the Group's credit RWAs and a consequential significant increase in the Group's CET1 ratio of 350bps. The pro forma CET1 ratio on the IRB basis at 30 September 2018 was 14.0%. The pro forma CRD IV leverage ratio on the IRB basis at 30 September 2018 was 5.5%.

On 15 October 2018, the Group completed the acquisition of Virgin Money. Following the combination, the CET1 ratio is expected to be c.15.2%. prior to the impact of the International Financial Reporting Standard (IFRS) 3 accounting adjustments.

Financial results

Financial performance review

Reconciliation of statutory to underlying results

The underlying results presented within this Financial performance review reflect the Group's results prepared on an underlying basis and as presented to the CEO and his Leadership Team and the Board. These exclude certain items that are included in the statutory results, as management believes that these items are not reflective of the underlying business and do not aid meaningful year on year comparison. The table below reconciles the statutory results to the underlying basis, and full details on the adjusted items are included in the Glossary on page 248:

2018 income statement

	Statutory results £m	Legacy conduct costs £m	Business restructuring £m	RBS alternative remedies package spend £m	Virgin Money transaction costs £m	Separation costs £m	Underlying basis £m
Net interest income	**851**	**–**	**–**	**–**	**–**	**–**	**851**
Non-interest income	**156**	**–**	**–**	**–**	**–**	**–**	**156**
Total operating income	**1,007**	**–**	**–**	**–**	**–**	**–**	**1,007**
Total operating and administrative expenses before impairment losses	**(1,130)**	**396**	**38**	**16**	**37**	**8**	**(635)**
Operating (loss)/profit before impairment losses	**(123)**	**396**	**38**	**16**	**37**	**8**	**372**
Impairment losses on credit exposures(1)	**(41)**	**–**	**–**	**–**	**–**	**–**	**(41)**
(Loss)/profit on ordinary activities before tax	**(164)**	**396**	**38**	**16**	**37**	**8**	**331**
Tax credit/(expense)	**19**	**(40)**	**(6)**	**(3)**	**(1)**	**(2)**	**(33)**
(Loss)/profit attributable to equity holders	**(145)**	**356**	**32**	**13**	**36**	**6**	**298**
Financial performance measures							
CIR	**112%**	**(38)%**	**(4)%**	**(2)%**	**(4)%**	**(1)%**	**63%**
RoTE	**(6.9)%**	**14.0%**	**1.3%**	**0.5%**	**1.4%**	**0.3%**	**10.6%**
Basic EPS	**(19.7)p**	**40.3p**	**3.6p**	**1.4p**	**4.1p**	**0.7p**	**30.4p**
Return on assets	**(0.34)%**	**0.83%**	**0.07%**	**0.03%**	**0.09%**	**0.02%**	**0.70%**

(1) Impairment losses on credit exposures relate solely to loans and advances to customers (refer to note 3.6 to the financial statements) and exclude the credit risk adjustments on loans at fair value through profit or loss which are incorporated in the movement in other assets and liabilities at fair value within non-interest income (refer to note 2.3 to the financial statements).

Underlying profit after tax attributable to ordinary equity holders is equal to the underlying profit attributable to equity holders less dividends and distributions (net of tax relief) of £29m (2017: £29m) and amounted to £269m (2017: £191m).

2017 income statement

	Statutory results £m	Legacy conduct costs £m	Business restructuring £m	Separation costs £m	Pension scheme reforms £m	AFS investment disposal £m	Underlying basis £m
Net interest income	844	–	–	–	–	–	844
Non-interest income	192	–	–	–	–	(20)	172
Total operating income	1,036	–	–	–	–	(20)	1,016
Total operating and administrative expenses before impairment losses	(720)	58	67	8	(88)	–	(675)
Operating profit before impairment losses	316	58	67	8	(88)	(20)	341
Impairment losses on credit exposures[(1)]	(48)	–	–	–	–	–	(48)
Profit on ordinary activities before tax	268	58	67	8	(88)	(20)	293
Tax expense	(86)	(5)	(9)	(2)	31	(2)	(73)
Profit attributable to equity holders	182	53	58	6	(57)	(22)	220
Financial performance measures							
CIR	69%	(5)%	(6)%	(1)%	8%	2%	67%
RoTE	6.1%	2.1%	2.1%	0.2%	(2.1)%	(0.9)%	7.5%
Basic EPS	17.3p	5.9p	6.6p	0.7p	(6.5)p	(2.5)p	21.5p
Return on assets	0.45%	0.14%	0.16%	0.01%	(0.16)%	(0.06)%	0.54%

(1) Impairment losses on credit exposures relate solely to loans and advances to customers (refer to note 3.6 to the financial statements) and exclude the credit risk adjustments on loans at fair value through profit or loss which are incorporated in the movement in other assets and liabilities at fair value within non-interest income (refer to note 2.3 to the financial statements).

Case study

On a mission to get the UK financially fit

With consumer debt levels at an all-time high we believe now is the time to encourage UK consumers to get financially fit by taking ownership of their financial well-being. We are starting to see some very positive brand awareness (peaking at 13% in July 2018) and a strong link between B and the notion of getting into shape financially (40% of customers now associate B with financial fitness).

A big part of the programme has been a series of fully integrated marketing campaigns under the umbrella theme of 'B-Tox.' We began the conversation in October 2017 when we started a campaign questioning why UK consumers are apathetic when it comes to changing banks and stopping unnecessary payments. We also highlighted some of the pitfalls of Black Friday where deals are not always all they are cracked up to be. Then in January 2018 B-Tox launched in branches, and across outdoor and digital channels nationally. We urged the UK to 'take the B-Tox Challenge' and 5,000 people signed up to change a bad spending habit for a good saving habit.

As part of B-Tox, this year we have hosted events at Studio B in London with panellists from ITV's This Morning and Good Morning Britain, Elle and Grazia magazines and from the B senior management team. By inviting customers and media to Studio B for exciting events like this we continue to position B as a lifestyle brand with serious appeal to young professionals and the Millennial audience.

One of the panellists at our January B-Tox event was Ryan Crabbe – shown below with his wife, Keira – a B customer who won our 'live rent free in London for a year' prize back in May 2017 when we opened Studio B. Ryan has become a true brand ambassador for both B and for our financial fitness movement. He has been interviewed by UK national papers and radio stations where he talks about the amazing opportunity B has given him to get closer to home ownership and also to adopt great money management skills through the app. There is no better way to build trust with customers than allowing them to talk about a brand in a positive but – crucially – credible way. Ryan has been a great asset for B this year.

Governance

Governance

Chairman's letter

"The Board is focused on achieving the highest standards of corporate governance and is committed to delivering long-term sustainable value for CYBG's shareholders."

Dear shareholder,

I am pleased to present our Corporate governance report for 2018 setting out our approach to governance in practice, the work of the Board in 2018 and including reports from the Board's Governance and Nomination Committee, Audit Committee and Risk Committee and the Remuneration Committee report included in the Directors' remuneration report.

2018 has been a landmark year for CYBG as we completed the acquisition of the Virgin Money business. Strong corporate governance and an effective Board have been key in the run-up to the acquisition and the Board remains focused on ensuring that the highest standards of corporate governance underpin our commitment to delivering a strong and sustainable business and real value for all shareholders.

Board changes

The acquisition of Virgin Money has enabled the Board to benefit from the appointment to the Board of Geeta Gopalan, Darren Pope and Amy Stirling, former Non-Executive Directors of Virgin Money. Geeta, Darren and Amy bring knowledge, skills and experience that complement those of the existing Board and also provide continuity which is important in the early period of the Combined Group. Their biographical details, skills and experience are described on pages 53 to 57. Board committee changes during the year are set out on pages 73 and 80.

David Browne retired from the Board on 30 June 2018 and I would like to thank him for his contribution during his six years on the Board. Debbie Crosbie stepped down as an Executive Director of the Company on 19 November 2018 to take up an external opportunity and the Board thanks Debbie for her significant contribution over more than 20 years with the Group.

The structure, size and composition of the Board and its committees will continue to be kept under review in 2019.

Strategy

A key focus for the Board continues to be on the creation of long-term sustainable value for our shareholders and this year the Board spent significant time working with the Executive Leadership Team on shaping the recommended offer for Virgin Money and in doing so the Board spent considerable time assessing the strategic and financial rationale for the combination and the opportunities for shareholders. At the same time the Board has continued to support the Executive Leadership Team to execute the three-year strategic plan and delivery of our strategic objectives. In particular the Board has spent time overseeing the continued delivery of the customer growth strategy, progress on our efficiency programme, the preparation for the IRB accreditation application and the multi-year strategic investment necessary to deliver an enhanced digital experience for customers. In doing so the Board has spent time discussing the challenges arising from an increasingly competitive market, regulatory change and the risks in the current economic and political environment.

Culture

CYBG is building a purpose-led, high performing, team-based culture with a clear set of organisational values and behaviours which shape the culture of the business. The Board firmly believes that strong governance underpins a strong culture and the Board is committed to leading by example and ensuring that culture transformation is focused on creating leaders, colleagues and ways of working that will allow the business to evolve and change in line with the market and the Group's strategy. During the year a new Culture Dashboard was introduced to provide the Board with insight on the progress in transforming culture and the Board also spent time reviewing the feedback from colleagues in the annual MyVoice colleague engagement survey which showed that we have sustained our strong customer-focused culture and that our culture continues to encourage high levels of accountability, respect and integrity.

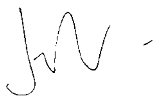
During the year a new programme was introduced to develop the Board's engagement with senior colleagues through informal discussion sessions. Some of these sessions were used to explore the topics of culture, values, behaviours and inclusion and for Directors to hear first-hand from colleagues on how our culture is operating in practice.

Stakeholder engagement
Hearing from our stakeholders remains an important part of the Board's programme and helps us focus on the things that are important to them. Our stakeholders include our customers, shareholders and colleagues in addition to government, regulatory bodies, our suppliers and wider society. This year the Board continued to develop its stakeholder engagement programme. A highlight was meeting with stakeholders in the political and business community in the West Midlands which provided the Board with good insight into the current economic and political environment and for the Board to reinforce CYBG's commitment to grow our business in that region. In addition, during the year the Board, either collectively or individually, undertook site visits, met with customers and representatives from wider communities and continued to receive regular stakeholder updates. In addition, the Board is updated regularly on both retail shareholder and institutional investor feedback and my fellow Directors and I very much looking forward to having the opportunity to meet with our shareholders at our 2019 AGM.

Board effectiveness
An important part of my role as Chair is to ensure that the Board and its individual members operate effectively and that the Board environment enables effective challenge and high-quality decision making. The Board takes its effectiveness seriously and adopts a programme of continuous improvement supported by a formal annual review. This year I led an internal review with the assistance of the Group Human Resources Director and Company Secretary. In line with the Board's commitment to lead by example on culture, our internal review focused on how the Board aligns to the Great Leadership framework and demonstrates the behaviours we expect of all leaders. The Board will continue to keep its governance arrangements under review through 2019 to ensure that the new Combined Group Board remains effective.

Looking ahead
In the year ahead the Board will focus on preparing our readiness to comply with the provisions of the new 2018 UK Corporate Governance Code (applicable to CYBG for the financial year ending 30 September 2020) in addition to continuing to evolve our corporate governance framework to suit the requirements of the new Combined Group Board.

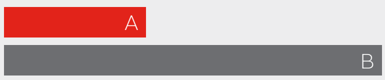
Finally, I would like to thank the Board and our colleagues for their support and commitment throughout 2018. I am confident that CYBG is very well placed to make the most of the opportunities that the combination with Virgin Money brings about.



Jim Pettigrew
Chairman

As at 30 September 2018

Gender diversity



A Female	3 (27%)
B Male	8 (73%)

Age

A 45–55 years	4
B 56–65 years	7

Role split

A Executive	3
B Non-Executive	7
C Non-Executive Chairman independent on appointment	1

As at the date of publication of this report

Gender diversity

A Female	4 (31%)
B Male	9 (69%)

Age

A 45–55 years	6
B 56–65 years	7

Role split

A Executive	2
B Non-Executive	10
C Non-Executive Chairman independent on appointment	1

Governance

Board of Directors

Left to right

Dr Teresa Robson-Capps
Independent Non-Executive Director

Clive Adamson
Independent Non-Executive Director

Paul Coby
Independent Non-Executive Director

David Duffy
Executive Director and Chief Executive Officer

Jim Pettigrew
Chairman

Adrian Grace (seated)
Independent Non-Executive Director

Tim Wade
Independent Non-Executive Director

Ian Smith
Executive Director and
Group Chief Financial Officer

Fiona MacLeod
Independent Non-Executive Director

Debbie Crosbie
Executive Director and
Group Chief Operating Officer
(stepped down from the Board on 19 November 2018)

David Bennett
Deputy Chairman and Senior Independent Non-Executive Director

Appointed on 15 October 2018 (not pictured)

Geeta Gopalan
Independent Non-Executive Director

Darren Pope
Independent Non-Executive Director

Amy Stirling
Non-Executive Director

Governance

Board of Directors

Board roles and responsibilities

The Board has agreed a clear division of responsibilities between the Chairman and Chief Executive Officer. The Chairman's priority is to lead the Board and ensure its effectiveness and the Chief Executive Officer's priority is to manage the day-to-day running of the Group's business. The roles of the Chairman, Chief Executive Officer and other Directors are clearly defined so that no single individual has unrestricted powers of decision. Their key responsibilities are set out below.

Position	Name	Roles and responsibilities
Chairman	**Jim Pettigrew**	Leading the Board and its effectiveness by organising its business and setting its agendas, ensuring that the Board as a whole plays a full and constructive part, being forward looking, and primarily focused on strategy, performance and key value creation matters. Guiding the Board in establishing the culture, value and ethics of the Company. Promoting the highest standards of corporate governance including promoting a culture of openness and debate and ensuring that the Board receives accurate, timely and high-quality supporting information. Ensuring properly constructed Board induction, evaluation and development, and effective communications with the Group's shareholders.
Deputy Chairman and Senior Independent Non-Executive Director	**David Bennett**	**Deputy Chairman** – Supporting the Chairman, and when required, acting as the Chairman's delegate and ensuring continuity of Chairmanship. Being available to the Board for consultation and advising and representing the Group's interests at official enquiries and with review bodies. **Senior Independent Non-Executive Director** – Providing a sounding board for the Chairman and serving as a trusted intermediary between the Chairman and the other Directors when necessary, and ensuring that the views of all Directors are conveyed to the Chairman. Being available to shareholders in the event of any matters which cannot be resolved through the normal channels of communication with the Chairman or the Executive Directors. Maintaining contact as required with major shareholders to understand their issues and concerns, maintaining stability and cohesion within the Board particularly during periods of stress. Meeting with the Non-Executive Directors without the Chairman present at least annually and leading the Non-Executive Directors in the ongoing monitoring and annual evaluation of the Chairman.
Chief Executive Officer	**David Duffy**	Leading the day-to-day management of the Group's business ensuring its effective running. Leading the Executive Leadership Team, being responsible for developing, coordinating and proposing to the Board all activities to implement the Group's strategy and its overall objectives in accordance with the Group's risk appetite, and maintaining a close working relationship with the Chairman.
Non-Executive Directors	**Clive Adamson** **Paul Coby** **Geeta Gopalan**(1) **Adrian Grace** **Fiona MacLeod** **Darren Pope**(1) **Dr Teresa Robson-Capps** **Amy Stirling**(1) **Tim Wade**	Bringing an external perspective, knowledge, experience and insight from other industries and applying sound judgement and objectivity to the business of the Board. Developing and setting the Group's strategy and monitoring its implementation, reviewing the RMF, and supporting and constructively challenging Executive Directors. Satisfying themselves on the integrity of financial information, considering and taking account of the views and concerns of the Company's shareholders and other stakeholders. Having a principal role in appointing and, where necessary, removing Executive Directors. Devising appropriate succession plans and approving appropriate levels of remuneration for the Executive Directors following recommendations from the Remuneration Committee.

(1) Appointed on 15 October 2018.

Key:

REM Remuneration Committee
RISK Risk Committee
AUDIT Audit Committee
GOV Governance and Nomination Committee
Chair

Non-Executive Directors

Jim Pettigrew
Chairman

GOV REM

Joined the Group
September 2012 and became Chairman in 2014

Key areas of expertise
Finance, Governance, M&A

Skills and experience:
Jim has over 30 years' experience in business and finance gained from executive and senior positions principally within financial services. Jim was formerly Chief Executive Officer at CMC Markets PLC, Chief Operating Officer at Ashmore Group PLC, Group Finance Director at ICAP PLC and Deputy Group Finance Director and Group Treasurer at Sedgwick Group PLC. He is a chartered accountant and has extensive Non-Executive Director experience in a listed environment. He was previously Chairman of The Edinburgh Investment Trust PLC, Senior Independent Non-Executive Director of Crest Nicholson PLC, Non-Executive Director at Aberdeen Asset Management PLC, Non-Executive Director at AON UK Limited and Non-Executive Director at Hermes Fund Managers Limited. He is a past President of the Institute of Chartered Accountants of Scotland. His breadth of experience, credibility with key stakeholders and strong leadership qualities make him an effective Chairman.

Key external appointments:
Senior Independent Non-Executive Director of Rathbone Brothers Plc and Director of a subsidiary company within the Rathbone Brothers Plc group; Chairman of Miton Group PLC; Chairman of RBC Europe Limited and Director of subsidiary companies within the RBC Group; Chairman of Scottish Financial Enterprise; and Co-Chair of Scotland's Financial Services Advisory Board.

David Bennett
Deputy Chairman and Senior Independent Non-Executive Director

REM RISK AUDIT GOV

Joined the Group
October 2015

Key areas of expertise
Finance, M&A, Retail Banking

Skills and experience:
David has significant experience in retail banking gained from a career spanning more than 30 years and including executive and senior roles in both the UK and internationally. David was Group Finance Director of Alliance & Leicester plc for six years before becoming its Group Chief Executive. Following the acquisition of Alliance & Leicester plc by Banco Santander he was appointed Executive Director on the Board of Abbey National plc. His in-depth experience of retail banking and involvement in organisational, operational and structural change is invaluable as the Group executes its strategy. He was formerly Chairman of Homeserve Membership Limited and has significant Non-Executive Director experience in a listed environment which has included being a Non-Executive Director of Bank of Ireland (UK) PLC, easyJet plc, and CMC Markets PLC.

Key external appointments:
Chairman of Ashmore Group plc, Non-Executive Director of PayPal (Europe) S.a.r.l et Cie, S.C.A and Chairman of various companies within the Together Financial Services Limited group.

Clive Adamson
Independent Non-Executive Director

RISK AUDIT

Joined the Group
July 2016

Key areas of expertise
Governance, Financial Services Regulation, Risk

Skills and experience:
Clive has considerable experience of UK and global economic, banking and regulatory matters gained from an extensive career in banking and financial services regulation. He held senior executive and advisory positions with the Financial Conduct Authority (FCA), the former Financial Services Authority and the Bank of England. He was previously Head of Supervision and an Executive Director of the Board of the FCA until May 2015. His strong understanding of the UK and global banking industry and related risks is invaluable to the Board.

Key external appointments:
Chairman at JP Morgan International Bank Limited; Senior Independent Non-Executive Director at Ashmore Group plc; Non-Executive Director of The Prudential Assurance Company Limited; and senior adviser at McKinsey & Company.

Governance

Board of Directors

Non-Executive Directors

Paul Coby
Independent Non-Executive Director
RISK

Joined the Group
June 2016

Key areas of expertise
Information Technology, Strategy

Skills and experience:
Paul is an accomplished IT professional with significant e-commerce, international and technology experience. In particular his understanding of how technology has changed consumer behaviour, how advances in digital technology can impact customer outcomes and his appreciation of the end-to-end customer journey in a strategic omni-channel context is invaluable to the Group as we develop new products and digital capability. In April 2018, Paul was appointed Chief Information Officer (CIO) of Johnson Matthey PLC. Prior to this, Paul was the John Lewis Partnership's CIO, responsible for leading and coordinating IT across the John Lewis, Waitrose and JLP Group. Previously, Paul was IT Director at John Lewis and CIO at British Airways for 10 years. Paul's other previous roles include Chairman of the Société Internationale de Télécommunications Aéronautiques (SITA), the global provider of systems, solutions and telecommunications to the air transport industry, Non-Executive Director at Pets at Home Group Plc and at P&O Ferries Limited, Chairman of the eSkills UK CIO Board and Chairman of the oneworld CIO Group which coordinated IT links across the 10 airline oneworld Alliance partners.

Key external appointment:
Chief Information Officer of Johnson Matthey PLC.

Adrian Grace
Independent Non-Executive Director
REM

Joined the Group
December 2014

Key areas of expertise
Finance, Financial Services Regulation, Strategy

Skills and experience:
Adrian has extensive financial, business leadership and general management experience gained from a career which has spanned a range of consumer and commercial financial services sectors and involved a variety of senior roles. Adrian's experience of designing and implementing substantial change programmes and delivering transformational growth through simple customer focused visions and plans is aligned to the Group's strategy. Having started his career with the Leeds Permanent Building Society and then Mercantile Credit, Adrian joined GE Capital where he spent time in the UK, Asia, and the Americas. He became Managing Director of the Small Business Division at Sage Group plc. He was Chief Executive at Barclays Insurance and Managing Director of Commercial Banking within the Corporate Division of HBOS. Since 2011 Adrian has been Chief Executive Officer at Aegon UK having joined Aegon in 2009 as Group Business Development Director. He was previously on the boards of the Association of British Insurers and Scottish Financial Enterprise.

Key external appointments:
Director of various companies within the Aegon Group and a member of the FCA Practitioner Panel representing the life and pensions sector.

Fiona MacLeod
Independent Non-Executive Director
RISK GOV REM

Joined the Group
September 2016

Key areas of expertise
M&A, Marketing, Strategy

Skills and experience:
Fiona has 30 years' international business experience in leading complex, large-scale business transformation and in managing the commercial, human resources and cultural aspects of change programmes. She has demonstrated this both as an executive and as an advisory consultant to both listed and governmental organisations. A substantial part of her career was at BP Group plc where she held various executive positions encompassing Mergers and Acquisitions, Branding and Marketing and latterly the role of President Retail, USA & Latin America. Fiona was formerly Senior Independent Non-Executive Director of SThree plc.

Key external appointment:
Non-Executive Director of Denholm Oilfield Services Limited.

Key:
REM Remuneration Committee
RISK Risk Committee
AUDIT Audit Committee
GOV Governance and Nomination Committee
Chair

Dr Teresa Robson-Capps
Independent Non-Executive Director
AUDIT

Joined the Group
October 2014

Key areas of expertise
Finance, Strategy

Skills and experience:
Teresa has extensive financial, customer service and general management experience from across a range of industries including telecommunications, financial services and retail. She is a chartered management accountant and has a Doctorate in Accounting and Management Control. Teresa has a breadth of experience gained from executive leadership roles with BT Mobile, Sears plc, Eagle Star/Zurich Financial Services, Cable & Wireless, Reality and Accenture. She joined HSBC Group in 2006 and from 2010 was Deputy Head, Direct Bank & First Direct. Teresa also has strong board experience gained from her previous roles as Chairman of ACS Clothing Group Limited and Non-Executive Director of Broker Network Holdings Limited, Paymentshield Group Holdings Limited, PowerPlace Insurance Services Limited, Towergate Insurance Limited and Yorkshire Water Services Limited.

Key external appointments:
Non-Executive Director of Hastings Group Holdings PLC and FIL Holdings (UK) Limited.

Tim Wade
Independent Non-Executive Director
AUDIT RISK

Joined the Group
September 2016

Key areas of expertise
Finance, M&A, Retail Banking, Risk

Skills and experience:
Tim has over 20 years' senior experience in retail financial services, including retail banking in both the UK and internationally. An Australian national, he is an experienced Chief Financial Officer, a chartered accountant and a Fellow of the Institute of Chartered Accountants of Australia. Tim was Managing Director at AMP International, responsible for AMP Bank and the Virgin Direct (now Virgin Money) joint venture. He began his career at Arthur Andersen working in Melbourne and Singapore, and in 1994 he joined Colonial Limited, the mutual financial services group, as Chief Taxation Counsel. He became Group Chief Financial Officer in 1997 and Executive Director of State Bank of New South Wales. Tim subsequently oversaw the Initial Public Offering (IPO) of Colonial and was involved in Colonial's subsequent acquisition by Commonwealth Bank – at the time the largest acquisition in Australian corporate history. His previous Non-Executive Director board experience includes Friends Life Group Limited and Monitise plc.

Key external appointments:
Chairman at Macquarie Bank International Limited; Non-Executive Director of companies within the Chubb European Group Limited and The Access Bank UK Limited groups; and Non-Executive Director of The Coeliac UK Trading Company Limited.

Additional Non-Executive Directors of the Board following the acquisition of Virgin Money on 15 October 2018

Geeta Gopalan
Independent Non-Executive Director
RISK

Joined the Group
October 2018

Key areas of expertise
Finance, Financial Services, Retail Banking, Digital

Skills and experience:
Geeta has over 25 years of experience of financial services and retail banking, particularly payments and digital innovation. Geeta was Director of Payment Services with HBOS plc and previously Managing Director, UK Retail Bank and Business Development Head EME at Citigroup. Geeta was also formerly the Chair of Monitise Europe and was previously a Non-Executive member and vice-chair of the England Committee of the Big Lottery Fund. She is a chartered accountant.

Key external appointments:
Non-Executive Director of Funding Circle Holdings plc, Ultra Electronic Holdings Plc and Wizink Bank S.A.

Governance

Board of Directors

Additional Non-Executive Directors of the Board following the acquisition of Virgin Money on 15 October 2018

Darren Pope
Independent Non-Executive Director
AUDIT

Joined the Group
October 2018

Key areas of expertise
Finance, Financial Services, Retail Banking

Skills and experience:
Darren has over 30 years of experience in retail banking and financial services. Darren held the post of Chief Financial Officer of TSB Bank plc, having taken a lead role in the design and divestment of the TSB business from Lloyds Bank plc and its subsequent IPO and takeover. He previously held a number of executive and senior roles at Lloyds Banking Group plc including Retail Bank Commercial Director. Darren is a Fellow of the Chartered Institute of Certified Accountants.

Key external appointment:
Senior Independent Non-Executive Director of Equiniti Group plc.

Amy Stirling
Non-Executive Director

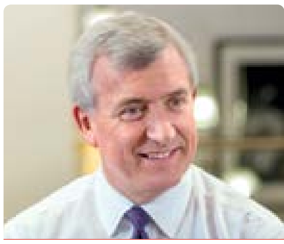
Joined the Group
October 2018

Key areas of expertise
Finance, Strategy, Operations

Skills and experience:
Amy has extensive board, financial and management experience from senior and board roles in a range of sectors including telecommunications, financial services and commerce. She was previously Non-Executive Director of Pets at Home Group Plc and the UK Cabinet Office. Amy is a Fellow of the Chartered Institute of Accountants for England and Wales.

Key external appointments:
Chief Financial Officer of the Virgin Group and Non-Executive Director of RIT Capital Partners plc.

Executive Directors



David Duffy
Executive Director and Chief Executive Officer

Joined the Group
June 2015

Key areas of expertise
Banking, Finance, M&A, Strategy

Skills and experience:
David has significant international finance and banking experience gained from a career spanning almost three decades. David's proven ability to build and transform businesses and lead strong management teams brings significant value to all of the Group's stakeholders. Prior to joining the Group, David was Chief Executive Officer at Allied Irish Banks plc, one of the largest retail and commercial banks in Ireland. He is a former Chief Executive Officer of Standard Bank International where he had responsibility for operations in the UK, Europe, Latin America and Asia. He was also previously Head of Global Wholesale Banking Network with ING Group and President and Chief Executive Officer of the ING wholesale franchises in the United States and Latin America. David is a past President of the Banking and Payments Federation of Ireland and a past Director of the European Banking Federation. David's broad-based skills, leadership, energy and strategic vision are invaluable to the Group as it continues its strategic journey and cultural transformation.

Key external appointments:
Senior Independent Director of NewTA Limited (trading as UK Finance), the industry body representing leading firms providing finance, banking, markets and payments-related services in or from the UK; HM Treasury Fintech Envoy for England; and a Board member of The Northern Powerhouse Partnership.

Key:
REM Remuneration Committee
RISK Risk Committee
AUDIT Audit Committee
GOV Governance and Nomination Committee
Chair

Debbie Crosbie
Executive Director and
Group Chief Operating Officer
(stepped down from the Board on 19 November 2018)

Joined the Group
June 1997

Key areas of expertise
Information Technology, Retail Banking, Strategy, Operations

Skills and experience:
Debbie has broad experience and knowledge gained over 20 years in the banking sector, particularly around information technology, complex project delivery, material outsourcing and strategy and planning. She has significant experience at a senior management level and is a strong advocate for customers and improving the customer experience by driving a change and transformation journey which has the customer as its core focus. Since joining the Group in 1997 Debbie has held a variety of positions including Head of Technology Governance, Head of Strategic Projects and Head of the Group's Development Centre. She was Chief Information Officer from 2008 to 2011, became Operations and IT Director in 2011, was appointed Executive Director in 2014 and became Chief Operating Officer in 2015. Debbie was Acting Chief Executive Officer from February 2015 to June 2015 and during this period led the preparation for the Group's demerger and IPO and was part of the management team which completed the transaction. She was previously a Non-Executive Director of the Scottish Court Service. She holds an Honours degree in Industrial Relations from the University of Strathclyde and is a Fellow of the Chartered Institute of Bankers.

Key external appointments:
Vice-Chair of the Board of CBI Scotland, member of the Board of Glasgow Economic Leadership and Member of the Strathclyde Business School Advisory Board.

Ian Smith
Executive Director and
Group Chief Financial Officer

Joined the Group
November 2014

Key areas of expertise
Banking, Finance, M&A, Strategy

Skills and experience:
Ian has considerable experience in finance, audit and advising on bank strategy and corporate transactions from a career spanning more than 25 years. He has held senior finance roles in HBOS plc and Lloyds Banking Group plc. He joined the Group in November 2014 from Deloitte LLP where he was a partner specialising in financial services.

Key external appointment:
Non-Executive Director of 67 Pall Mall Limited.

Company Secretary

Lorna McMillan
Company Secretary

Joined the Group
September 1994

Skills and experience:
Lorna has broad experience and knowledge gained from over 20 years in the Group having held various roles in retail and business banking, wholesale banking, risk management and legal and governance areas. Lorna was appointed Company Secretary in October 2014.

Governance

Executive Leadership Team

The Executive Leadership Team operates under the direction and authority of the Chief Executive Officer and is responsible for supporting him in all aspects of his role. Each member has been assigned individual accountability for delivery of the overall strategy and the principal risks outlined in the Strategic report. They also have accountability for delivering against the initiatives designed to underpin our strategic priorities of improving efficiency, driving sustainable customer growth and capital optimisation

David Duffy
Executive Director and
Chief Executive Officer

Debbie Crosbie
Executive Director and
Group Chief Operating Officer

Ian Smith
Executive Director and
Group Chief Financial Officer

Enda Johnson
Group Corporate Development Director

Joined the Group
September 2015

Skills and experience:
Enda joined the Group in 2015 and he is responsible for leading the strategic planning process across the Group, and its strategic stakeholder engagement plan, fully aligning this to the Group's cultural transformation and customer/commercial strategies.

Before joining the Group, Enda worked at Allied Irish Banks in Dublin, where he joined as Head of Strategy and was appointed to Head of Corporate Affairs/Strategy and the Executive Leadership Team in July 2012. Prior to this, Enda was a member of the Banking Unit at the Irish National Treasury Management Agency (NTMA), where he worked on the recapitalisation and restructure of Irish banks following the global financial crisis and subsequent programme of financial support for Ireland provided by the IMF, ECB and EU in 2010.

Before joining the NTMA, he worked with Merrill Lynch in New York, London and California, in their investment banking and capital markets divisions, focusing on client advisory and equity transactions for global clients on a cross industry basis.

Kate Guthrie
Group Human Resources Director

Joined the Group
January 2016

Skills and experience:
Kate joined the Group in January 2016, and is responsible for developing and leading HR strategy. Kate has over 30 years of domestic and international HR experience, having worked in six different blue-chip organisations in four industrial sectors. Kate joined from Lloyds Banking Group after 11 years of service in a number of senior HR Director positions, most recently HR Director, Culture, Capability and Engagement.

Fergus Murphy
Group Customer Value Director

Joined the Group
January 2016

Skills and experience:
Fergus joined the Group as Products Director in January 2016. He has over 20 years' experience in financial services and he is responsible for the delivery of the Group's product suite, including pricing, liability strategy and capital allocations.

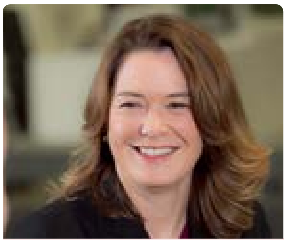
Prior to joining the Group, Fergus held a number of key roles at Allied Irish Banks from 2011 until 2015 including Director of Products and Capital Markets and, most recently, Director of Corporate and Institutional Banking. From 2008 until 2011 he served as CEO and Managing Director of BES Building Society and EBS Limited.

Fergus also held a number of senior positions at Rabobank International between 1994 and 2007. He served as CEO Asia Region from 2003 and was previously a member of their Global Financial Markets management team, holding roles as Head of Global Treasury and Head of Global Investment Banks. Fergus spent his earlier career in the BNP Group working as a derivatives and corporate trader in the Markets division.

Gavin Opperman
Group Customer Banking Director

Joined the Group
November 2015

Skills and experience:
Gavin joined the Group in November 2015. He has over 30 years of leadership experience in risk, operations and across front-line digital, retail, commercial, corporate and investment banking services. Gavin was previously Regional Head of Consumer Banking, Standard Chartered based in China, and prior to that held a number of senior positions across Asia in a career spanning 20 years with Barclays Group.



Helen Page
Group Innovation and Marketing Director

Joined the Group
December 2012

Skills and experience:
Helen joined the Group in December 2012 with over 25 years' experience in marketing, consultancy and product development. Almost 15 years of those have been spent in financial services.

Prior to joining the Group, Helen spent eight years at RBS in a number of roles.

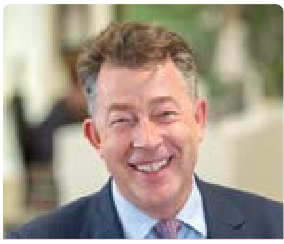
She became Managing Director for Marketing and Innovation and held responsibility for all UK brands across the Retail, Commercial and Corporate divisions. During this time, Helen was responsible for developing and delivering 'Helpful Banking' for NatWest.

Helen was also Head of Brand Marketing at Argos, where she relaunched the catalogue company as a Retailer, and played a key role when the business became 'Retailer of the Year' and 'Advertiser of the Year' in 2003. Prior to Argos, Helen held a number of product and marketing roles at Abbey National (now Santander), where she became Head of Marketing. She also has experience in research, consultancy and central government roles. Helen has a degree in economics, development and planning and holds a diploma in Marketing from the Chartered Institute of Marketing.

James Peirson
Group General Counsel

Joined the Group
November 2014

Skills and experience:
James joined National Australia Bank Limited (NAB) in May 2005 and was appointed as General Counsel for the Group in November 2014. His previous roles include leading NAB's London Branch legal team and roles supporting NAB and Clydesdale Bank Treasury activities as part of NAB's Capital and Funding legal team in Melbourne and London. Prior to joining NAB, James worked in private legal practice at Hogan Lovells in London.



Mark Thundercliffe
Group Chief Risk Officer

Joined the Group
September 2016

Skills and experience:
Mark was appointed in September 2016 and has over 29 years of financial services experience. He joined the Group from HSBC where he was Chief Risk Officer responsible for management and oversight of risk for HSBC's Retail Banking and Wealth Management business in 18 countries across the UK, Europe, the Middle East and Africa.

Mark has also held a number of senior international positions, including President and CEO (Asia) with Home Credit in Hong Kong and he was also an Executive Director and Business Head (Russia) with Renaissance Capital in Moscow. With Citigroup he progressed from Chief Risk Officer (UK and Ireland) to become CEO of CitiFinancial (Russia). Prior to Citi, he worked with Associates Capital Corporation, latterly as Executive and Business Head, based in India.

Additional members of the Executive Leadership Team following the acquisition of Virgin Money on 15 October 2018

Hugh Chater
Managing Director, Core Bank (Virgin Money)

Joined the Group
October 2018

Skills and experience:
Hugh has over 25 years of experience in financial services. He was an executive founder at MBNA Europe, joining in 1993 from KPMG Management Consulting.

At MBNA Hugh held executive roles in HR, Credit Management, Customer Satisfaction and Marketing before becoming Chief Operating Officer and then UK Managing Director. In 2007 Hugh joined RBS Retail to run the consumer credit card business. He subsequently ran the current account, savings, investments and insurance products. Hugh joined Virgin Money in June 2016 with responsibility for commercial performance, customer outcomes and optimising distribution and servicing channels.

Peter Bole
Integration Director

Joined the Group
October 2018

Skills and experience:
Peter is a Chartered Accountant and has over 25 years of experience in financial services. Following roles with Deloitte and Standard Life, Peter joined RBS in 2001 where he held a variety of senior finance roles, latterly in RBS Insurance. In 2009, he joined Tesco Bank where he established the finance function as Chief Financial Officer and played a key role in the leadership of the business as it was migrated from RBS infrastructure. Peter joined Virgin Money in 2016 and became Chief Financial Officer in January 2017. Peter has responsibility for leading our integration programme across all functions, leveraging the best talent from CYBG and Virgin Money while minimising disruption to the Group's operations and customer base.

Governance

Corporate governance report

Statement of compliance

The Annual Report and Accounts for the year ended 30 September 2018 has been prepared in accordance with the UK Corporate Governance Code 2016 ('Code') which was issued in April 2016. The Code is available at www.frc.org.uk.

Throughout the year ended 30 September 2018 the Board confirms that the Company fully complied with all relevant provisions of the Code, except with regard to membership of the Remuneration Committee from 1 July 2018, following the retirement of David Browne, a former independent Non-Executive Director and member of the Remuneration Committee.

The Governance and Nomination Committee, in consultation with the Chairman of the Remuneration Committee, reviewed the composition of the Remuneration Committee and appointed Fiona MacLeod, as a member of the Remuneration Committee with effect from 5 November 2018. The Board confirms that the Company from 5 November 2018 to the date of this report fully complied with all relevant provisions of the Code.

Leadership

The Board is the principal decision-making body of the Group and is collectively responsible to shareholders for promoting the long-term success of the Company.

The Board's role is to provide leadership to the business as a whole within a framework of prudent and effective controls which enable risk to be assessed and managed. It sets strategy and oversees its delivery and establishes its culture, values, ethics and standards. It sets the Group's risk appetite, monitors operational and financial performance and reporting, ensures the Group is adequately resourced and has effective controls and remuneration policies, and that there are appropriate succession planning arrangements.

In order to assist the Board in carrying out its functions and to ensure that there is independent oversight of financial reporting, internal controls, risk management, governance and remuneration matters, the Board delegates certain clearly defined responsibilities to its four principal committees. Reports from the Governance and Nomination Committee, the Audit Committee and the Risk Committee are contained in this report. A report from the Remuneration Committee is included in the Directors' remuneration report.

As required, the Board may also establish special purpose Committees to assist the Board in the oversight of specific areas that may require more detailed attention. The Board established a special purpose IRB and Credit IFRS 9 Committee which provided oversight for the transition from a standardised approach to calculating capital requirements for credit risk to an IRB approach with accreditation announced on 11 October 2018, and the implementation of the credit element of the IFRS 9 accounting standard which has been in effect for the Group from 1 October 2018.

The charts below and on page 126 of the Risk report provide further details of the Board and management structure as at 30 September 2018.

Board governance framework

CYBG Board
The Board's role is to provide leadership to the business by setting the strategy and overseeing its delivery and it is collectively responsible to its shareholders as a whole for promoting the long-term success of the Company.

Governance and Nomination Committee
Board composition, evaluation, succession and governance standards.

See pages 68-71 for further information.

Audit Committee
Financial reporting, internal control, internal and external auditor effectiveness and monitoring the Group's whistleblowing arrangements.

See pages 72-78 for further information.

Risk Committee
Overseeing risk management activities, including the Group's risk appetite, the risk management framework and effective risk culture.

See pages 79-83 for further information.

Remuneration Committee
Remuneration framework and individual Director packages.

See pages 96-97 for further information.

Matters reserved to the Board and delegated authorities

In order to retain control of key decisions and ensure there is a clear division of responsibilities at the head of the Company, the Board has identified certain 'reserved matters' that only it can approve. Other matters, responsibilities and authorities have been delegated to its committees and the Chief Executive Officer.

The matters reserved to the Board are set out in the Charter for the Board and this, as well as the Charters for each principal Board committee, is available to view on the Company's website (www.cybg.com/about-us/corporate-governance). The Charters are also available on request from the Company Secretary at the Company's registered office. During the year the Board and each of the Board committees reviewed its Charter.

The authorities delegated by the Board to the Chief Executive Officer are set out in the Delegation of Authority Framework.

Board attendance

The core activities of the Board were carried out in 11 scheduled meetings. 13 additional ad hoc meetings of the Board were arranged when matters required to be brought to the Board's attention or when decisions were required outside scheduled meetings, which during the year were predominately related to the acquisition of Virgin Money.

The attendance of Directors at scheduled Board meetings, which they were eligible to attend, and the number of meetings attended in the year ended 30 September 2018 is shown in the following table.

Director	Number of scheduled Board meetings eligible to attend	Number of scheduled Board meetings attended
Chairman		
Jim Pettigrew	11	11
Non-Executive Directors		
Clive Adamson	11	11
David Bennett	11	11
David Browne(1)	8	7(3)
Paul Coby	11	10(2)
Adrian Grace	11	10(3)
Fiona MacLeod	11	10(3)
Dr Teresa Robson-Capps	11	11
Tim Wade	11	11
Executive Directors		
David Duffy	11	11
Debbie Crosbie	11	10(3)
Ian Smith	11	11

(1) David Browne retired from the Board on 30 June 2018.
(2) Unable to attend the meeting due to a conflicting business commitment.
(3) Unable to attend the meeting due to personal circumstances.

Board activity

Setting the Board agenda

There is a comprehensive and continuous process in place for ensuring the Board has full and timely access to all relevant information in an insightful format.

The Chairman is responsible for setting the Board agenda and is assisted by the Chief Executive Officer and Company Secretary. The Board agenda is structured to ensure it covers each of the three strategic priorities and underpinning core capabilities to support strategy engagement and the challenge and debate on performance and delivery at Board level. The Chairman reviews the time allocation with the Company Secretary to ensure adequate time is allowed to discuss material matters. The Company Secretary keeps the Chairman informed of any agenda items requested by Non-Executive Directors. In order to carry out its work, a yearly planner is prepared by the Company Secretary to map out the flow of key items of business to the Board and to ensure that sufficient time at the meeting is provided for debate and challenge. Directors are sent papers for Board meetings up to five working days in advance of the meeting (whether they are able to attend or not) in order that they may have the time to consider the proposals put forward, seek clarification or, if required, request further information.

As well as considering scheduled agenda items in line with the Board's annual plan and ad hoc items as required, at each main meeting the Board discusses:

– the Chief Executive Officer's report – including performance against the strategic plan, key developments in the external environment, the economic outlook and impacts for the Group, business performance, product and proposition developments, stakeholder engagement and investor relations matters, material regulatory issues, and key matters relating to people, cultural and organisational transformation and capability;

– the Group Chief Financial Officer's report – including performance against the financial plan, key performance indicators, capital, liquidity and funding matters;

– the Group Chief Operating Officer's report – including delivery against customer service commitments, operational efficiency, IT service and security, and the status of major investment programmes; and

– the Group Chief Risk Officer's report – including the risk profile and risk categorisation and principal and emerging risks, key risk issues and RAS performance and trends.

Governance

Corporate governance report

How Board meetings are run

Prior to the start of a scheduled Board meeting, the Senior Independent Non-Executive Director meets with Non-Executive Directors (excluding the Chairman and then with the Chairman present) to discuss matters of concern or focus. Both the Chairman and the Senior Independent Non-Executive Director report to the Board on issues to be brought to the Board's attention at the commencement of each meeting and these are recorded in the Board minutes. The Chairman ensures Board meetings are structured to facilitate open discussion, debate and challenge with dissenting views of Directors being freely expressed and discussed within the decision-making process, leading to Board decisions being made on a sound and well-informed basis.

All Directors are expected to attend each Board meeting and committee meeting for which they are members, save for in exceptional circumstances. Reasons for non-attendance are generally unavoidable conflicts with prior business commitments, personal reasons or illness, and non-attendance must always be notified in advance to the Chairman, relevant committee Chair or the Company Secretary. In the rare event of a Director being unable to attend a meeting, he/she has the opportunity to discuss with, or notify, the Chairman, relevant committee Chair or the Company Secretary of any matters he/she wishes to raise and to follow up the decisions made at the meeting. The Chairman and Company Secretary, together with members of the Executive Leadership Team, are available to discuss issues relating to meetings or other matters with Directors.

During the year, the Chairman held a number of meetings with Non-Executive Directors without the Executive Directors being present.

Board committees

The Board delegates certain clearly defined responsibilities to its four principal Board committees, namely: the Governance and Nomination Committee; the Audit Committee; the Risk Committee; and the Remuneration Committee.

The committee Chairs report to the Board on the activities of the committees at each Board meeting. Each principal committee membership comprises Non-Executive Directors only and is chaired by an experienced Chair. Committee memberships are spread between the Non-Executive Directors, drawing on each of their relevant skills and experience. Only members of the committees are entitled to attend their meetings, but others may attend at the discretion of the committee Chair.

Stakeholder engagement

Directors, either collectively or individually, undertook site visits and met with customers and representatives from our wider communities. Site visits provide an opportunity to get closer to business operations, current issues and customer service in an operational environment. This provides insight into customer experiences and allows Directors to connect with management and colleagues alike. The Board attended colleague events in Leeds and Birmingham during the year and participated in informal discussion sessions with colleagues as part of the broader Talent Engagement Programme when the topics of culture, values, behaviours and inclusion were discussed. In October 2017, Directors met in Leeds with customers, business leaders and representatives of The Northern Powerhouse Partnership which enabled the Board to gain insight on opportunities to support growth in the North of England region, particularly for SMEs, and to reinforce its commitment to help the delivery of the Northern Powerhouse agenda. Meetings followed in March 2018 with stakeholders in the political and business community in Birmingham and the West Midlands region which provided the Board with insight into current economic, political and business challenges and opportunities in that region.

Effectiveness

Board size and composition

At the date of this report, the Board comprises the Chairman, two Executive Directors, nine independent Non-Executive Directors and one Non-Executive Director appointed by Virgin Enterprises Limited pursuant to its right under the Brand Licence Agreement. The size of the Board is considered to be suitable in the context of a highly complex commercial and regulatory operating environment, and reflecting the acquisition of Virgin Money, consists of the appropriate combination of Executive and Non-Executive Directors such that no individual or small group of individuals can dominate the Board's decision making. The names of the Directors together with their full biographical details, including the skills and experience they each bring to the Board, are on pages 53 to 57. Further details on the composition of the Board and independence of the independent Non-Executive Directors are provided in the Governance and Nomination Committee report on page 70.

Time commitments

The Board recognises that it is vital that Directors should be able to dedicate sufficient time to the Company to effectively discharge their responsibilities. The time commitment is considered by the Board on appointment and kept under review. The letters of appointment of the Chairman and of each of the Non-Executive Directors set out the minimum time commitment for their roles and that they undertake to allocate sufficient time to the Company as is necessary for the effective discharge of their duties.

The Chairman is expected to commit at least 60 days per year on Company business, the Deputy Chairman 45 days per year and Non-Executive Directors at least 35 days. Time commitment increases for other Board roles such as the Senior Independent Non-Executive Director and committee Chairs and for involvement in a committee as a member.

As described within the relevant sections of this Corporate governance report, the Non-Executive Directors' preparation for, and attendance at, Board and committee meetings is only part of their role.

The other significant commitments of the Chairman and Non-Executive Directors are disclosed to the Board before appointment, with an indication of time involved. During the year, the Governance and Nomination Committee kept under review the number of external directorships held by each Director and considered the limits on the number of directorships which Directors may hold as a result of PRA Rulebook 'General Organisational Requirements 5.4' (having regard to General Organisational Requirements 5.5 and 5.6) and FCA Handbook Senior Management Arrangements, Systems and Controls (SYSC) 4.3A.5R (having regard to SYSC

4.3A.6R and 4.3A.7R). Details of the Chairman's other significant commitments are set out on page 53. Details of the Non-Executive Directors' other significant commitments are set out on pages 53 to 56. Any changes to the Non-Executive Directors' time commitments were reported by the Governance and Nomination Committee to the Board. The Board is satisfied that each Non-Executive Director is able to devote sufficient time to their role.

Executive Directors are encouraged to take non-executive positions in other companies and organisations to broaden their experience. The appointment to such positions is subject to the approval of the Board which considers, in particular, the time commitment required.

Board changes
David Browne, independent Non-Executive Director, retired from the Board on 30 June 2018. Geeta Gopalan and Darren Pope, independent Non-Executive Directors, and Amy Stirling, Non-Executive Director, were appointed to the Board on 15 October 2018. Debbie Crosbie stepped down as an Executive Director of the Board on 19 November 2018.

The Governance and Nomination Committee is responsible for considering the recruitment of new Directors and it adopts a formal, rigorous and transparent procedure with due regard to diversity, including gender. Before commencing the recruitment process, the Committee evaluates the balance of skills, knowledge, experience, independence and diversity on the Board and, in light of this evaluation, prepares a description of the role and capabilities required. In identifying suitable candidates, the Committee:

– uses open advertising or the services of external advisers to facilitate the search;
– considers candidates from different genders and a wide range of backgrounds;
– considers candidates on merit and against objective criteria ensuring that appointees have sufficient time to devote to the position, in light of other potential significant positions; and
– engages from time to time with the Group's major shareholders in future skills requirements and ideas for potential candidates.

Further details about the Group's approach to succession planning and diversity can be found in the Governance and Nomination Committee report on pages 70 to 71. Changes to committee memberships are set out on pages 73, 80 and 96.

Board independence
It is the Company's policy that at least half the Board should be independent Non-Executive Directors. The Board assesses the independence of Directors on an annual basis following a review by the Governance and Nomination Committee. The Board considers Clive Adamson, Paul Coby, Geeta Gopalan, Adrian Grace, Fiona MacLeod, Darren Pope, Dr Teresa Robson-Capps and Tim Wade to be independent in character and judgement. Amy Stirling is not considered by the Board to be independent as her appointment as a Non-Executive Director is pursuant to the right of Virgin Enterprises Limited to nominate a director under the terms of a Brand Licence Agreement. The Chairman was considered independent on appointment. Further information is given in the Governance and Nomination Committee report on page 70.

Conflicts of interest
Pursuant to the Companies Act 2006, the Directors have a statutory duty to avoid situations in which they have or can have a direct or indirect interest in the Company, unless that interest is first authorised by the other Directors. This duty is in addition to the existing duty that a Director owes to the Company to disclose to the Board any transaction or arrangement under consideration by the Company. Prior to appointment, potential conflicts of interest are disclosed and assessed to ensure that there are no matters which would prevent the incoming Director from taking the appointment, and during their tenure Directors are asked to consult with the Company Secretary and the Chairman before taking up any external appointment or responsibilities. Any changes to the commitments of Directors are reported to the Governance and Nomination Committee and the Board. Directors are reminded, at each Board meeting, of their duty to report any actual or potential conflict as soon as they become aware of any such events. If any actual or potential conflict arises, the relevant Director will excuse himself/herself from any meeting or discussions where the potential conflicts are considered and all relevant material will be restricted including Board papers and minutes. A Director with a potential or actual conflict will not be permitted to form part of the quorum or vote upon the matter giving rise to the conflict. Directors do not participate in decisions concerning their own remuneration or interest. All potential conflicts authorised by the Board are recorded in a Register of Directors' Conflicts of Interests which is reviewed by the Board annually.

Board induction
The Chairman ensures that each newly appointed Director receives a full and formal induction on joining the Board which is tailored to reflect a Director's skills, experience and Board role.

The Company Secretary designs and facilitates the induction programme having consulted with the Chairman and having regard to the particular needs of the new Director. Progress is reported to the Chairman and reviewed regularly by the Chairman with each Director.

The aim of the induction programme is to quickly provide a new Director with an understanding of how the Group works and the key opportunities and challenges that it faces to enable them to contribute fully in Board and Committee meetings and covers at least the following:

– the Group and its strategy;
– key business drivers of performance and the competitive environment and regulatory landscape in which the Group operates;
– major strategic and investment programmes and priorities;
– the key current and top and emerging risk issues and challenges for the business and risk appetite;
– the organisational culture and capabilities, the role of the Board and its committees, and the Company's corporate governance practices; and
– training on the role and responsibilities of a Director, including statutory duties.

The induction programme is delivered through a combination of: one-to-one briefings with the Chairman, Company Secretary, current Directors and members of the Executive Leadership Team; site visits to some of the Group's customer-

Governance

Corporate governance report

Board focus in 2018

The significant matters addressed by the Board during the financial year ended 30 September 2018 and its evaluation of the Company's 2018 Annual Report and Accounts are described below.

Regular agenda items
Chairman's report
Senior Independent Non-Executive Director's report
Chief Executive Officer's report
Group Chief Financial Officer's report
Group Chief Operating Officer's report
Group Chief Risk Officer's report
Reports from committee Chairs
Board administration and governance

Strategy and business performance

- Monitored delivery of the Group's strategic plan and performance of the financial plan including the impacts of changes in the economic, political, regulatory and competitive environment
- Received updates on the progress on the efficiency programme, preparation for IRB accreditation and major investment programmes; monitored key performance indicators
- Approved the all-share off for Virgin Money and related matters including the regulatory Change in Control application and supporting governance arrangements; received updates on the readiness for Change in Control becoming effective and the integration of the CYBG and Virgin Money businesses
- Approved the property strategy including plans for a new Glasgow head quarters
- Approved the Group tax strategy
- Approved major capital and investment expenditure including IRB Programme funding requests
- Received the draft FY19-FY23 Financial Plan; reviewed financial and economic forecasts

Structure and capital

- Reviewed the adequacy of capital, funding and liquidity and approved the Capital Plan and the Funding Plan
- Approved the Internal Liquidity Adequacy Assessment Process (ILAAP)
- Approved the proposed scenarios and risks for assessment under the Internal Capital Adequacy Assessment Process (ICAAP) and the economics to be used for assessing capital requirements; approved an addendum to the ICAAP reflecting the impact of IRB accreditation
- Received briefings on IFRS 9 implementation
- Approved additional PPI provisions

Financial reporting and controls

- Approved an increase to the provision for legacy PPI costs
- Approved the Company's Annual Report and Accounts, Interim Financial Report, related announcements and supporting analyst presentations
- Reviewed quarterly trading updates
- Approved the annual Pillar 3 Disclosures
- Approved the Dividend Framework

Risk and control

- Approved the Cybersecurity strategy
- Approved the RAS and received updates on RAS performance
- Approved the Group's recovery plan in the event of a significant deterioration in financial stability
- Monitored the Group's top and emerging risks
- Reviewed internal control systems; completed the annual review of underwriting Delegated Commitment Authorities and that of the Chief Executive Officer
- Received updates on the Group's transition to using an IRB approach to capital requirements for credit risk and the implementation of IFRS 9 from 1 October 2018
- Approved the renewal of Group insurance programmes including a Directors & Officers Liability Insurance Policy
- Received updates on material litigation
- Received updates on readiness for the introduction of Ring-fencing
- Received an update on duties under the Senior Manager and Certification Regime

People, culture and conduct

- Reviewed the Culture Dashboard and monitored progress on transforming culture
- Considered the results from the annual 'MyVoice' colleague engagement survey
- Received health and safety updates
- Approved the Modern Slavery Act Statement

Stakeholders and customers

- Received updates on the customer growth strategy and customer-centric key performance indicators including measures of customer satisfaction
- Reviewed progress of the PPI complaints remediation programme
- Monitored the Conduct Framework progress and outcomes
- Received investor relations updates and feedback on shareholder engagement
- Received updates on the stakeholder engagement strategy
- Kept informed of regulatory changes and material updates from regulatory engagement

Corporate governance

- Monitored completion of actions from the 2017 Board performance evaluation and agreed the approach to the 2018 Board effectiveness review
- Approved the Group's Diversity Policy and targets
- Approved the division of responsibilities between the Chairman and Chief Executive Officer
- Reviewed the structure, size and composition of the Board and its Committees; considered the independence of Non-Executive Directors; reviewed the register of Conflicts of Interest
- Reviewed and approved the Charters for the Board and each Board Committee; appointed a Board Committee in relation to the acquisition of Virgin Money
- Approved the appointment of new Non-Executive Directors
- Approved and recommended to shareholders the reappointment of the External Auditor
- Recommended the election or re-election by shareholders of Directors at the Annual General Meeting
- Received an update on the refresh of the executive management governance committee framework

facing and operational areas; and reading materials including archive Board and committee papers and other key corporate governance documents. Meetings are also arranged with other selected senior managers, including the Group Director Internal Audit, and with external stakeholders including the External Auditor.

Directors joining the Board to perform a specific role or holding a senior management function role, such as a committee Chair, are provided with additional in-depth training including meeting with the outgoing role holder or committee Chair where possible and completing a documented handover. Particular attention is given to the tailored components of the programme where a Director is appointed from outside the financial services sector or where a Director has not previously served on a UK listed company board. Directors who take on or change role during the year participate in an induction programme tailored to their new role.

As described in the following section, the Board has in place a professional development and training programme which ensures that Director development continues after the initial induction programme has been completed.

Professional development and training
Continuing professional development is an important aspect of a Director's role. Skills and knowledge need to be kept up to date to ensure the effectiveness of the Board as a whole to allow every Director to contribute fully in Board and committee meetings. The Board Development Programme includes components covering: Board 'deep dive' and briefing sessions (details below); stakeholder engagement (see page 62); opportunities for wider stakeholder engagement in the community in which the Group operates; seminars, courses and round tables to provide external insights on topical issues, technical briefings and peer group debates; and Board briefings (details below).

The Chairman reviews with each Non-Executive Director their individual training and development need and progress at regular one to one meetings.

The Company Secretary maintains a training and development log for each Director.

Board performance evaluation
Following the very thorough externally facilitated review undertaken in 2017 covering both the Board and Board Committees, the 2018 Board effectiveness review was an internal review led by the Chairman with the support of the Group Human Resources Director and Company Secretary. It took the form of a survey completed by each Board member and key stakeholders. The review sought the Directors' views on performance against each of the six elements of the Great Leadership framework introduced to the Group in 2017 and which sets the expectations of all leaders. The review also sought feedback on the Board's strengths and the greatest opportunities for development. The structure of the survey enabled feedback to be produced for the Board collectively and also at an individual Director level. In addition, a report was produced on the Chairman's performance.

Key themes were collated from the feedback on the Board collectively and shared with the Governance and Nomination Committee and the Board, and where relevant the Board committees. The Chairman meets regularly with each Non-Executive Director and uses the individual feedback reports to inform discussions on individual contributions and development needs. The Senior Independent Non-Executive Director received the report on the Chairman's performance which he used to inform the annual review of the Chairman's performance in addition to seeking the input of other Directors. This feedback was shared with the Chairman individually and with the Non-Executive Directors without the Chairman being present.

Overall the conclusion from the 2018 review was that the Board strongly demonstrates all elements of Great Leadership with strengths being the good balance of enterprise-wide and longer-term Board focus and appropriate

Deep dives and Board briefings

The Board has a programme of 'deep dive' and briefing sessions focusing on thematic updates aligned to the strategic priorities and core capabilities which give Directors the opportunity to engage with management in a more informal way outside of the structure of a Board meeting to gain insight on topics of interest or focus for the Board. Listed below are the 'deep dive' and briefing topics which were discussed during the year. In addition a significant part of the Board's time was dedicated to preparing for the acquisition of Virgin Money and Board time was allocated to Board reports and briefings on this topic.

Deep dives and board briefings
– The cultural transformation programme
– Top and emerging risks
– The Company's role and opportunities to support economic growth in the North of England
– Brand awareness and development opportunities
– Improvements to enhance the customer experience and improve automation
– Progress on our digital strategy
– Cybersecurity threats and emerging risks
– Arrangements for business and operational resilience to ensure continuity of critical processes

The Board receives regular briefings on regulatory and corporate governance change. During the year these topics included Open Banking, IFRS 9, ring-fencing regulations and updates to the Senior Managers Regime.

Governance

Corporate governance report

challenge and oversight of the business. In 2019 the focus will be on further developing the Board agenda and the quality of information provided to the Board so that the Board is able to balance its time on business performance, the integration of the CYBG and Virgin Money businesses and future thinking, in particular, continuing to involve customer experience insights more fully in Board discussions.

During the year the Governance and Nomination Committee, the Board and the other Board Committees also reviewed the progress made on the continuous improvement actions identified in the 2017 review and agreed that the Board had continued its evolutionary development and had made strong progress across all previous recommendations and actions.

Information and support

The Board has processes in place to ensure that it is supplied in a timely manner with information in a form and of a quality to enable it to effectively discharge its duties. The Chairman, through the Company Secretary, is responsible for ensuring communication flows between the Board and its committees with the support of the Executive Directors and management, and ensures that this information is of high quality in terms of its currency, clarity, accuracy, appropriateness and comprehensiveness. All Directors have access to the advice of the Company Secretary in relation to the discharge of their duties and matters of governance. Directors are able to seek clarification or further detail from management where necessary. The Company Secretary is also responsible for facilitating communications with shareholders, as appropriate, and ensuring due regard is paid to their interests. All Directors are provided with sufficient resources to undertake their duties. In appropriate circumstances, Directors may obtain, at the Group's expense, independent professional advice where they judge it necessary to discharge their responsibilities as Directors. The appointment and removal of the Company Secretary is a matter reserved for the Board as a whole.

Service contracts and letters of appointment

Details of Executive service contracts and letters of appointment of the Board are set out on pages 93 and 94 of the Directors' Remuneration report.

Internal control

Board responsibility

The Board is responsible for the Group's systems of internal control. The internal control framework is designed to facilitate effective and efficient operations, ensure a high quality of internal and external reporting, and ensure compliance with applicable laws and regulations. The Directors and management are committed to maintaining a robust control framework as the foundation for the delivery of effective risk management. Owing to the limitations inherent in any internal control framework, the controls have been designed to manage and mitigate, rather than eliminate, the risk of failure to achieve the Group's business objectives and can provide only reasonable, not absolute, assurance against material misstatement or loss. The Directors acknowledge their responsibilities in relation to the Group's internal control framework and for reviewing its effectiveness.

The Board confirms that throughout the year ended 30 September 2018 and up to the date of approval of this Annual Report and Accounts, there have been rigorous processes in place to identify, evaluate and manage the principal risks faced by the Group, including those that would threaten its business model, future performance, solvency or liquidity, the likelihood of a risk occurring and the costs of control in accordance with the Guidance on Risk Management, Internal Control and Related Financial and Business Reporting published by the Financial Reporting Council (FRC).

In order to assist in the identification and management of the principal risks, the Board has established a RMF which is integrated into the Group's overall framework for risk governance and has developed a system of regular reports from management. The Board has authorised the Risk Committee to oversee the Group's compliance with the Board's approved RAS, RMF and risk culture. Further details can be found in the Risk report on pages 121 to 170.

Reviews by the Board

The effectiveness of the risk management and internal control systems is reviewed regularly by the Risk Committee and the Audit Committee. The Risk Committee is responsible for providing oversight and advice to the Board in relation to current and potential future risk exposures. The Audit Committee assists the Board in discharging its responsibilities with regard to external and internal audit activities and controls including reviewing audit reports, internal controls and risk management systems.

The Group's risk management and internal control systems are regularly reviewed by the Board and are consistent with the guidance on Risk Management, Internal Control and Related Financial and Business Reporting issued by the FRC and compliant with the requirements of the Capital Requirements Directive IV (CRD IV). They have been in place for the year under review and up to the date of the approval of the Annual Report and Accounts.

Control effectiveness

A review of the effectiveness of controls is regularly undertaken across the Group, providing an assessment and statement on the effectiveness of the Group's control environment. This provides assurance to the Risk Committee that no new material control issues have been identified and that robust management actions are in place to address specific known gaps.

Bribery and corruption

In compliance with the Bribery Act 2010, the Group has in place risk assessments, policies and guidelines on interacting with customers, suppliers and agents, including specific policies for gifts and hospitality. Certain Senior Managers are required to assess money laundering risks and the adequacy of related internal controls within their areas of responsibility on an ongoing basis. Formal anti-bribery and corruption training is required for all colleagues, the Executive Leadership Team and Directors.

Overall assessment

Over the past year, the Group has further enhanced the RMF, strengthening expectations around managing risks relating to vulnerable customers, model risk, ring-fencing and GDPR. The control environment remains stable with the 2018 Control Effectiveness Statement providing assurance that ineffective controls are escalated appropriately and have adequate action plans in place.

The Risk Committee, in conjunction with the Audit Committee, concluded that the Group's risk management and internal control framework in relation to the Group's risk profile and strategy was effective and adequate, and was recommended to and approved by the Board.

Remuneration

The statement by the Chair of the Remuneration Committee and the Directors' annual report on remuneration are set out on pages 84 to 114.

Shareholder relationships

The Board recognises the need for a programme of engagement which offers all shareholders opportunities to receive information from the Company and enables them to share their views with the Board. In addition, the Board regularly receives feedback on shareholder sentiment and sell side analyst views of the Group and the wider industry.

The Board is committed to ensuring that there are effective channels of communication with the Company's shareholders and the Group's website enables access to documents and communications as soon as they are published, including recordings of webcasts and investor presentations.

A significant level of engagement with institutional investors (both existing and potential investors) took place throughout the year, in order to update the market on our progress against the Group's long-term strategy, recent financial performance and the acquisition of Virgin Money. Investor roadshows were held in both the UK and Australia reflecting the nature of the Company's shareholder register, and were attended by an appropriate mix of Directors including the Chairman, Chief Executive Officer, Group Chief Financial Officer and Group Chief Operating Officer, among others.

The Board receives regular feedback on share price performance, investor and analyst views and changes to the shareholder register via regular monthly reports, a quarterly detailed investor relations update and ad hoc intelligence.

Relationships with retail shareholders
The Company Secretary oversees communication with retail shareholders and provides feedback to the Board and appropriate committees to ensure the views of retail shareholders are received and considered.

The Group's Registrar, Computershare, provides a dedicated shareholder service at www.investorcentre.co.uk in the UK and www.investorcentre.com.au in Australia through which shareholders can manage their shareholding online, receive Company communications and cast proxy votes for forthcoming general meetings .

The annual general meeting (AGM)
The Board and the Executive Leadership Team consider the AGM to be a key date for shareholder engagement. It provides an opportunity to engage with shareholders, particularly retail shareholders, on the key issues facing the Group and any questions they may have. The majority of the Directors, including the Chairman, were available for informal discussion either before or after the 2018 AGM.

All resolutions proposed at the 2018 AGM, which were considered on a poll, were duly passed by the Company's shareholders. The Company noted that a significant number of votes were cast against resolution 24, to authorise the calling of general meetings of the Company by notice of 14 clear days. Following a review during the year, the Company provided the Companies Act 2006 minimum notice period for general meetings of 21 clear days for the General Meeting held on 10 September 2018 in relation to the acquisition of Virgin Money. The Company is also not seeking a special resolution to reduce the minimum notice period for general meetings from 21 clear days' notice at the Company's next AGM in 2019.

	Reporting events	Stakeholder engagement
Q1	**Nov 2017** 2017 preliminary results	**Nov 2017** 2017 results Analyst presentation and Q&A session
	Dec 2017 2017 Annual Report and Accounts published	**Nov 2017** 2017 results Investor engagement
Q2	**Jan 2018** Q1 trading update	**Jan 2018** Q1 trading update Analyst engagement
	Jan 2018 2018 AGM (London)	**Feb 2018** Australian investor roadshow
Q3	**May 2018** Interim results announcement	**May 2018** Interim results Analyst and investor engagement
	Jun 2018 Virgin Money Offer announcement	**Jun 2018** Virgin Money transaction investor roadshows (London and Australia)
Q4	**Aug 2018** Q3 trading update	**Aug 2018** Q3 trading update Analyst engagement
	Sep 2018 General Meeting for Virgin Money transaction Shareholder approval	**Aug 2018** Virgin Money acquisition Stakeholder engagement

Governance

Governance and Nomination Committee report

"The Committee has made progress on its 2018 priorities and has continued to keep the Board's skills, knowledge and experience under review."

Dear shareholder,

I am pleased to present the report on the Committee's activity during 2018 and to confirm that the Committee has made good progress on its agreed 2018 priorities.

During 2018 the Committee oversaw an evaluation of the skills, knowledge and experience on the Board which was documented in a refreshed skills matrix. This review highlighted areas where Board skills and experience could be further strengthened and helped inform the selection of new Board members which the Committee recommended to the Board. As I mentioned in my Chairman's letter, Geeta Gopalan, Darren Pope and Amy Stirling joined the Board as Non-Executive Directors on completion of the acquisition of Virgin Money on 15 October 2018. In preparation for these new Board appointments the Committee reviewed the arrangements for the full, formal and tailored induction of the new Directors and will oversee the delivery of the induction programme through 2019. The skills matrix is also helping inform longer-term requirements and future Board and Board Committee composition.

The Committee also spent time reviewing the executive and senior management succession planning arrangements and continued to develop the Committee's and Board's role in the areas of talent management and leadership development. Fiona MacLeod, a Committee member, supported the Career Sponsorship Programme along with fellow Non-Executive Director Dr Teresa Robson-Capps. This Programme aims to develop colleagues into broader or more senior roles reinforcing our high performing culture and building greater diversity into our long-term leadership pipeline.

In addition to the new Board appointments, as part of the preparations for the combination of CYBG with Virgin Money, the Committee reviewed the proposed governance arrangements to be in place upon completion of the acquisition with a strong focus on ensuring that Board and executive governance structures continue to adhere to the highest standards of corporate governance. This included a review of the intended Board and Board Committee structure, size and composition post the acquisition in both the Company, the Bank and Virgin Money plc.

The Committee spent time overseeing the progress on the recommendations and actions arising from the 2017 evaluation of the Board and its Committees and ensured that status reports were made to the Board periodically. The Committee worked with the Group Human Resources Director and Company Secretary on the approach to and design of the 2018 Board and Committee evaluation. In view of the externally facilitated review in 2017 which had looked in-depth at the effectiveness of the Board and its Committees, the Committee agreed, with the support of the Board, that the 2018 review should be internally facilitated with a focus on individual Director effectiveness. The process is described on pages 65 and 66.

In the year ahead, the Committee will continue to monitor the needs of the Board, its Committees and the longer-term leadership of the business. Key areas of focus will include developing the succession plan for the Board and keeping the composition of the Board and its Committees under review. The Committee will also continue to oversee the effectiveness of the corporate governance arrangements particularly in view of the new 2018 UK Corporate Governance Code and will monitor the implementation of actions agreed by the Board following the 2018 Board evaluation.

Jim Pettigrew
Chair, Governance and Nomination Committee

Membership and meetings

The current members of the Committee are:

Jim Pettigrew, Chair

David Bennett

Fiona MacLeod

The Committee is chaired by the Chairman of the Board and the members of the Committee are independent Non-Executive Directors, in accordance with the provisions of the Code. If a matter were to concern the Chairman, then he would leave the meeting and the remaining members would elect one of their number to take the Chair, unless the Chairman had designated a member to do so.

The Chief Executive Officer attends meetings at the invitation of the Committee. The Group Human Resources Director also attends meetings at the invitation of the Committee, particularly when it is considering Executive succession planning matters.

Members of the Committee took no part in any discussions concerning their own membership of the Board or appointment as a Chair of a committee.

Committee attendance

The core activities of the Committee were carried out in five scheduled meetings of the Committee. The table below shows the Committee members during the year to 30 September 2018 and their attendance at scheduled Committee meetings.

	Number of scheduled Committee meetings eligible to attend	Number of scheduled Committee meetings attended
Committee Chair		
Jim Pettigrew	5	5
Committee members		
David Bennett	5	5
Fiona MacLeod	5	4[1]

(1) Unable to attend the meeting due to personal reasons.

Committee role and responsibilities

During the year, the Committee revised its Charter which sets out the role and responsibilities of the Committee. The Charter of the Committee can be found on the Company's website www.cybg.com/about-us/corporate-governance/

Committee performance evaluation

During the year the Committee made progress on key findings from the in-depth Board Performance Evaluation carried out in 2017, which included an assessment of the Committee's effectiveness, by agreeing a work plan to address the Committee's priorities for 2018 in addition to its wider Charter responsibilities. This work plan has driven the matters considered by the Committee during the year as set out on pages 70 and 71. The Committee has adopted a continuous improvement approach to its performance evaluation and considers at the end of each meeting the effectiveness of the meeting and the quality of the reports that were presented. During the year the Committee noted the improvement made in Committee agenda setting and reporting which enabled a fulsome discussion and debate with several actions generated and decisions made to progress matters within the Committee's remit.

Governance

Governance and Nomination Committee report

Matters considered and actions taken by the Committee

The significant matters addressed by the Committee during the year ended 30 September 2018 and in evaluating the 2018 Annual Report and Accounts are described in the following pages.

Role of the Committee	Key matters considered and actions completed
Board and Board committee composition Membership of the Board and the current and future composition of its committees	– Reviewed the structure, size and composition of the Board and Board Committees including skills, experience, independence, knowledge and diversity and considered the longer-term succession of Board and Board Committee members relative to tenure, mix and diversity of skills and the Group's strategy, future, challenges and opportunities and reported the outcome and recommendations to the Board; – Recommended to the Board the appointment of Geeta Gopalan and Darren Pope as independent Non-Executive Directors and of Amy Stirling as a Non-Executive Director; – Reviewed the time commitment including external appointments of serving Directors; and – Undertook the annual review of the Conflicts of Interests Register.
Skills and independence	– Agreed the methodology for and oversaw an evaluation of the skills, knowledge and experience on the Board; reviewed the outcomes and agreed a refreshed skills matrix; the skills matrix will be used to inform future Board and Board Committee succession plans; – Assessed the independence of Non-Executive Directors having regard to both the Code requirements on independence and factors such as length of tenure and the ability of Non-Executive Directors to objectively challenge the Executive, free from relationships or circumstances which are likely to affect, or could appear to affect, the Directors' judgement. The Committee also took account of any relationships that had been disclosed and authorised by the Board. Based on the assessment for 2018 the Committee is satisfied that throughout the year, all Non-Executive Directors remained independent as to both character and judgement and that Jim Pettigrew, the Board Chairman, was considered independent on appointment. At least half the Board comprised independent Non-Executive Directors; and – Recommended to the Board the election of Geeta Gopalan, Darren Pope and Amy Stirling and recommended to the Board the re-election of all other Directors.
Executive succession planning and talent management	– Received updates from the Group Human Resources Director on the executive and senior management succession plan; – Monitored executive succession plans including the strength and depth of succession coverage both on a contingency and permanent basis; and – Kept informed of the Group's talent management and leadership development programme and participated in events designed to broaden Directors' engagement with senior colleagues.

Role of the Committee	Key matters considered and actions completed
Diversity and inclusion	– The Board is committed to delivering the Group's inclusion strategy and although new appointments are always based on merit, careful consideration is given to the benefits of improving and complementing the diversity, skills, experience and knowledge of the Board. In making recommendations to the Board, the Committee makes sure that the Board is made up of competent colleagues with the necessary balance of diversity, skills and experience required to ensure that the Board can function effectively; – The Board remains committed to building strong female representation at all levels within the Group including at Board, executive and senior management levels. The Committee and the Board remains committed to achieving the target it set last year to achieve 33% female representation on the Board by 2020, achieved through the natural cycle of Board renewal. It remains the Board's intention to broaden diversity on the Board beyond gender diversity alone, to reflect the communities in which the Group operates and the diversity of our customers. As at 30 September 2018 there were three female Directors (27%) on the Board which has risen to four (31%) following the appointment of Geeta Gopalan and Amy Stirling on 15 October 2018 and Debbie Crosbie stepping down from the Board on 19 November 2018; – The Group supports the Women in Finance Charter and has a target of 40% women in senior management roles by 2020. During the year a new Culture Dashboard was introduced for the Board which enables the Board to track progress on both gender diversity and broader inclusion metrics and commitments.
Board and Board committee effectiveness review	– Oversaw progress on the recommendations and actions arising from the 2017 in-depth, externally facilitated evaluation of the Board and its Committees; – Ensured status reports on progress of actions were made to the Board periodically; – Agreed the approach, methodology and timing of the 2018 evaluation of the Board, its Committees and of individual Director effectiveness which was internally facilitated and oversaw progress; and – Reviewed the arrangements for the full, formal and tailored induction for new Directors in preparation for their appointments becoming effective. The full Board was updated on the plans for developing Directors' knowledge of the Virgin Money business following completion of the acquisition.
Governance	– Reviewed and challenged the proposed governance arrangements to be in place upon completion of the acquisition by the Company of Virgin Money including a review of the intended Board and Board Committee structure, size and composition, post the acquisition in both the Company, the Bank and Virgin Money plc; – Agreed a work plan to ensure that the Committee would address its priorities for 2018 in addition to its wider Charter responsibilities and monitored progress throughout the year; – Received an update on proposed corporate governance reforms; and – Reviewed and agreed a revised Committee Charter setting out the Committee's role and responsibilities.

Governance

Audit Committee report

"During the year the Committee maintained its focus on supporting the Board in ensuring appropriate challenge and governance in the integrity of the Group's financial reporting and financial internal controls."

Dear shareholder,

As Chair of the Audit Committee, I am pleased to present the report from the Committee for the year ended 30 September 2018.

David Browne, Independent Non-Executive Director, retired from the Board on 30 June 2018. I'd like to thank David for his knowledge and advice as a member of the Audit Committee. At the same time, I'd like to welcome Darren Pope who became a member of the Audit Committee on 15 October 2018.

Highlights in 2018

The report will outline how the Committee has fulfilled its key objectives of providing effective governance of the Group's financial reporting, discussing and challenging the judgements made by management and the assumptions and estimates on which they are based. The Committee has exercised judgement in deciding which of the issues it considered in the financial statements as being significant and this report sets out the material matters that it has considered in these deliberations.

In particular the Committee kept existing provisions for liabilities such as those in relation to PPI and other related conduct issues (including potential redress and administrative costs) under close review throughout the year to ensure they continued to be appropriate. With the Committee's oversight, this resulted in the £350m provision increase recorded in March 2018 and the £150m increase recorded in September 2018. While PPI itself will be finalised by the end or shortly after 2019 time bar, the Committee will continue to focus on the financial impact of both legacy and emerging conduct issues as a matter of priority.

The Committee spent a considerable amount of time overseeing and challenging the transition to IFRS 9 and the accounting judgements which underpin this, which the Group adopted on 1 October 2018.

In addition, it has provided oversight of the Group's financial and internal controls to ensure that risks are carefully identified and assessed, and that sound systems of risk management and internal control are in place. In conjunction with the Risk Committee, the Committee challenged the Three Lines of Defence model in relation to the Group's internal controls which are fundamental to the appropriate management and mitigation of risks.

The Group Director Internal Audit provided regular updates to the Committee on enhancements made during the year to the Internal Audit function. The Committee reviewed the scope, skills and competencies of this function against a backdrop of significant projects and programmes to understand and fully challenge where Internal Audit has focused and how it optimises value from its resource. In particular, the Committee continued to assess the Internal Audit oversight of the Group's IRB application and the successful receipt of the PRA's formal IRB accreditation for the Group's mortgage and SME/Corporate portfolios. The Committee concluded after considering feedback from stakeholders, peer benchmarking analysis, results of quality assessments and the Internal Audit reports provided to the Committee, that the Internal Audit activities were effective.

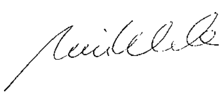
The Committee closely monitored the external audit process and the performance of the External Auditor, EY through an annual effectiveness review against four themes in line with the FRC guidance: judgement, mindset and culture skills, character and knowledge and an overarching assessment of quality control. The Committee considered the review and concluded in terms of the themes assessed that the external audit process was effective. Based on the Committee's recommendation, the Board is proposing that EY be reappointed as external auditors at this year's AGM.

During the year, the Committee received reports on the Group's Whistleblowing programme and as Whistleblowing Champion, I am responsible for ensuring and overseeing the integrity, independence and effectiveness of the Group's policies and procedures on whistleblowing and to promote a safe and effective culture for employees to raise genuine concerns without fear of reprisals. The promotion and enhancements to the operating model of whistleblowing continued during the year. Management's response and handling of reported cases continues to be considered appropriate and satisfactory by the Committee.

Looking ahead

The Committee will ensure the appropriate oversight over the Combined Group following the acquisition of Virgin Money and I have already received a detailed briefing from the Virgin Money Audit Committee Chair.

Many of the areas of focus of the Committee during the year will again be the focus for the Committee in 2019. Specifically, the Committee will monitor the application of the Three Lines of Defence Model, review Internal Audit's oversight of the IRB project as practices continue to embed and assess the critical accounting estimates and judgements in relation to the Group's adoption of the expected credit loss model for measuring impairment losses under IFRS 9.



Tim Wade
Chair, Audit Committee

Membership and meetings

The current members of the Committee are:

Tim Wade, Chair

Clive Adamson

David Bennett

Darren Pope (appointed 15 October 2018)

Dr Teresa Robson-Capps

As at the date of this report the Committee comprises five independent Non-Executive Directors. Tim Wade, Chair, has recent and relevant accounting and audit experience for the purposes of the Code, having held a number of senior finance roles. The other Committee members have significant current or recent experience in the financial services and banking industries (details of which are contained within the biographies section on pages 53 to 56). This depth of experience enables the Committee to deal effectively with the matters within its remit and to challenge management and auditors when required.

In addition to the Committee members, the Chairman, Chief Executive Officer, Group Chief Financial Officer, Group Head of Finance, Group Chief Risk Officer, Company Secretary, Group General Counsel, Group Director Internal Audit and the External Auditor are invited to attend Committee meetings. The Chair is also a member of the Risk Committee.

Private sessions are held with the External Auditor and Group Director Internal Audit to provide additional opportunity for open dialogue and feedback without management being present. The Chair of the Committee also meets with the Group Director Internal Audit and the Senior Statutory Auditor outside the formal Committee process at regular intervals throughout the year.

Alignment with Risk Committee

The Committee recognises the common interest in issues relevant to both the Risk Committee and Audit Committee and in particular the responsibilities of both in relation to the effectiveness of internal control. Joint discussions by both committees for the financial year ended 30 September 2018 included: progress made towards the implementation of IFRS 9; assurance plans from the Three Lines of Defence; the Viability Statement; and bonus risk adjustments to be recommended to the Remuneration Committee. There was a joint discussion on the Group's RAS, including a Day 1 RAS for the acquisition of Virgin Money. The RAS will be kept under close scrutiny for the Combined Group. To support the coordination of information between the committees, the Chairs of each of the Audit and Risk Committees are members of both committees.

Committee attendance

The core activities of the Committee were carried out in six scheduled meetings of the Committee. The Audit Committee and Risk Committee also hold at least one joint meeting per year. The table below shows the Committee members during the year ended 30 September 2018 and their attendance at scheduled Committee meetings.

	Number of scheduled Committee meetings eligible to attend	Number of scheduled Committee meetings attended
Committee Chair		
Tim Wade	6	6
Committee members		
Clive Adamson	6	6
David Bennett	6	6
Dr Teresa Robson-Capps	6	6
Former Committee members		
David Browne(1)	5	5

(1) David Browne retired as a Committee member on 30 June 2018.

Committee role and responsibilities

During the year, the Committee revised its Charter which sets out the role and responsibilities of the Committee. The Charter of the Committee can be found on the Company's website www.cybg.com/about-us/corporate-governance/

Committee performance evaluation

During the year the Committee incorporated a work plan resulting from an in-depth external Board Performance Evaluation carried out in 2017. An internal evaluation of the Committee at the end of 2018 concluded that the Committee was performing well and had progressed its agenda setting and reporting at its meetings.

Governance

Audit Committee report

Matters considered and actions taken by the Committee

The significant matters addressed by the Committee during the financial year ended 30 September 2018 and in evaluating the 2018 Annual Report and Accounts are described in the following pages.

Role of the Committee	Key matters considered and actions completed
Accounting, tax and financial reporting	
To review and challenge the appropriateness of the Company's financial statements, including the content of the Interim Financial Report, Annual Report and Accounts, and related Preliminary Results Announcements, Interim and quarterly results announcements and supporting analyst presentations.	– Understood the process for the production of the reports under the remit of the Group Chief Financial Officer and the level of involvement of cross-functional subject matter experts, including monitoring the procedures in place to ensure that all contributors attested to the completeness, accuracy and appropriateness of the disclosures provided.
Accounting policies and practices To review and challenge the critical accounting policies, disclosure obligations and changes in accounting requirements.	– Reviewed with both management and the External Auditor, the critical accounting estimates and judgements, and significant accounting policies and disclosures for the Group's interim and annual financial statements during the year; – Received regular updates from the Group Accounting Policy team and External Auditor on key changes and developments in financial reporting requirements; – Monitored the Group's readiness for the adoption of IFRS 9 with effect from 1 October 2018 which included regular updates from management on the progress being made throughout parallel run and detailed analysis of the Day 1 impact and related disclosure requirements; – Received updates from management on the readiness for adoption of IFRS 15 (Revenue Recognition) with effect from 1 October 2018 and agreed with management's assessment that the introduction of IFRS 15 will not result in a significant impact on the Group; – Received updates from management on the preparation for the adoption of IFRS 16 (Leases) with effect from 1 October 2019; and – Considered the financial disclosures for the acquisition of Virgin Money.
Significant issues and areas of judgement To consider where necessary, the actions of management on those areas identified as requiring the exercise of critical accounting estimate and judgements. These are summarised in note 1.8 to the financial statements.	
Impairment losses on loans and advances The Group's loans and advances are subject to impairment losses, which are measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the asset's effective interest rate. The process of calculating the collective loan loss provision requires the use of significant estimates and judgements over the following: (i) estimating the probability of default (PD) and estimates of future recoveries in Base Models; (ii) Model Risk Reserves; and (iii) the use of overlays.	– Reviewed regular reports from management in relation to the level of impairment provisioning, with the key focus being on the assumptions used within the collective provisioning element; – Reviewed and challenged the inputs and resulting output of the base models, with a particular focus on probabilities of default and the estimate of future recoveries; – Reviewed and challenged the level of overlays included within the collective provision and the rationale for their inclusion that augment the collective provisioning modelled output; – Agreed that the judgements and assumptions used were necessary and appropriate at 30 September 2018; and – Noted that the introduction of IFRS 9 with effect from 1 October 2018 would increase the overall level of credit impairment provisioning held. The disclosures relating to impairment provisions are set out in note 3.6 to the financial statements and in the Risk report from page 129.

Role of the Committee	Key matters considered and actions completed
PPI redress provision and other conduct related matters The level of provisions required for both redress and administration in relation to past conduct related matters requires assumptions to be made that are based upon a combination of historical data and management judgement. These judgements are inherently complex as they involve making estimates based on multiple factors that incorporate expectations of future customer behaviour, the impact of regulatory rule making and the application of precedent from the Financial Ombudsman Service.	– Reviewed and challenged the assumptions made by management when determining the level of provisions required for PPI and other conduct related matters; – Reviewed in detail proposals in relation to PPI and other conduct scenarios (including potential redress and administrative costs) presented by management which reflected alternative potential outcomes before concluding on the £350m provision increase recorded in March 2018 and the £150m increase recorded in September 2018. Under the terms of the Conduct Indemnity Deed in place with NAB, the impact of this on the Group income statement was £352m. As at 30 September 2018, the Conduct Indemnity Deed in place with NAB had been fully utilised; and – Based upon the most recent information the Committee concluded that management assumptions were supportable and that the other related conduct provisions recorded at 30 September 2018 were appropriate. The disclosures relating to provisions for conduct matters and the impact of the Conduct Indemnity Deed are set out in note 3.14.
Deferred tax assets The largest elements of the Group's deferred tax asset are historic losses and capital allowances. In determining that the deferred tax asset balance remains on the balance sheet, management has exercised judgement over the forecast future profitability of the Group; and the number of years over which to take account of future profits, i.e. the period over which profits can be reliably estimated.	– Reviewed the recoverability of deferred tax assets throughout the year; – Considered the judgements made by management over the forecast future profitability of the Group and the time horizon over which the use of tax losses was foreseeable in light of the continuing and progressively tightening restrictions on their use; and – Agreed that the recognition of a deferred tax asset balance of £206m at 30 September 2018 was appropriate. The disclosures relating to the Group's deferred tax asset position as at 30 September 2018 are set out in note 3.11.
Retirement benefit obligations The actuarial valuation of the Group's defined benefit scheme liabilities involves making several financial and demographic assumptions, including: discount rate; future inflation rates; and future mortality rates.	– Reviewed the discount and inflation rate assumptions proposed by management at 30 September 2018 against a benchmark range provided by the external adviser and concurred with these key assumptions. The disclosures relating to the Group's retirement benefit obligations at 30 September 2018 are set out in note 3.16.
Fair value of financial instruments Significant management judgement is over future expectation of credit losses in the fair value loan portfolio, through the application of a credit risk adjustment (CRA).	– Reviewed the judgement made by management and concurred with the level of CRA applied at 30 September 2018. The disclosures relating to the Group's fair value loan portfolio and fair value measurements at 30 September 2018 are set out in note 3.3.
The Committee considered management's review of the disclosed critical accounting estimates and judgements and concluded that the judgements had been applied appropriately and that the disclosures were sufficient.	
Going concern	– Reviewed and challenged the going concern assessment undertaken by management including evidence of the Group's capital, liquidity and funding position and confirmed to the Board that it was appropriate for the Group's financial statements to be prepared on a going concern basis.
Long-term viability	– Reviewed and challenged the viability assessment (including the three-year time horizon selected) undertaken by management in the 2018 Annual Report and Accounts, including the impact from the acquisition of Virgin Money. The Committee considered the process to support the viability statement in conjunction with an assessment of principal risks and strategy/business model disclosures, taking into account the assessment by the Risk Committee of stress testing results and risk appetite. The Committee recommended the draft viability statement (as set out on page 117) to the Board for approval.

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Audit Committee report

Role of the Committee	Key matters considered and actions completed
Assessment of the fair, balanced and understandable reporting	– Considered, at the request of the Board, the comprehensive review process which supports the Board and Committee in reaching its conclusion whether the 2018 Annual Report and Accounts was fair, balanced and understandable and whether it provided the necessary information for shareholders to assess the Group's performance, business model and strategy. The process which enabled the Committee to reach this conclusion included: – the production of the 2018 Annual Report and Accounts which was managed by the Group Chief Financial Officer, with overall governance and coordination provided by a cross-functional team of senior management led by the Group Head of Finance; – cross-functional support to drafting the 2018 Annual Report and Accounts, which included input from Finance, Risk, Legal and Governance, Investor Relations, HR and the wider business; – a robust review process of inputs into the 2018 Annual Report and Accounts by all contributors to ensure disclosures were balanced, accurate and verified, and further comprehensive reviews were conducted by senior management; – a review by the Company Secretary of all Board and Committee minutes to ensure all significant matters discussed at meetings were appropriately disclosed in the 2018 Annual Report and Accounts as required; – a formal review by the Committee of the draft 2018 Annual Report and Accounts in advance of final sign-off; and – a final review by the Board of Directors. – After careful review and consideration of all relevant information, including principal risks, the Committee was satisfied that, taken as a whole, the 2018 Annual Report and Accounts is fair, balanced and understandable and has affirmed that view to the Board. – This process was also undertaken in respect of all the Group's financial reporting during the year to ensure that, taken as a whole, based on the information supplied to it and challenged by the Committee, they were fair, balanced and understandable, and advised the Board to that effect.
Regulatory compliance Oversight of the Group's compliance with all necessary regulatory reporting.	– Reviewed the integrity of the Pillar 3 Disclosures and recommended approval by the Board; and – Oversight of significant management judgement in the regulatory returns to the Group's regulators, the PRA, BoE and FCA.
Internal controls and RMF Details of the internal controls and risk management systems for the Group's financial reporting process are provided within the Corporate governance report on page 66 and in the Risk report on pages 121 to 170.	– Reviewed in line with the Internal Audit plan, the output of Internal Audit reports (including thematic and focused reviews of prudential, credit, conduct and strategic change risks) to confirm the effectiveness of the Group's internal control and risk management systems; – Considered the Group's Financial Reporting Control Effectiveness Statement for Finance and Treasury together with an overview of key financial reporting controls; and – Considered the findings of the External Auditor in connection with the Group's control environment.

Role of the Committee	Key matters considered and actions completed
Monitoring the effectiveness of the Group's whistleblower framework The Chair of the Committee is the Whistleblower Champion in accordance with the Senior Managers Regime with responsibility for the integrity, independence and effectiveness of the Group's policies and procedures on whistleblowing and the Committee has oversight of the whistleblower policy standard and framework.	– Considered periodic whistleblower framework reports covering the Group's whistleblowing arrangements, including monitoring the trends in reported and substantiated whistleblowing cases; – Obtained assurance on the completion of training by colleagues and campaign to promote and raise awareness across the organisation of the whistleblower framework; and – Had oversight of updates to the whistleblowing policy standard.
As a result, the Committee, in conjunction with the Risk Committee, is satisfied that internal controls for financial reporting and risk management systems were appropriate and fit for purpose throughout the year.	
Independence and assurance **Internal audit** Monitoring the role and effectiveness of the Internal Audit function including the role of the Group Director Internal Audit	– Approved revisions to the Internal Audit Charter which sets out the role and responsibilities of the function. The Internal Audit Charter can be found on the Company's website at www.cybg.com/about-us/corporate-governance/ – Approved the audit plan and monitored progress to deliver the plan and material changes to it on a quarterly basis; – Reviewed the outcomes of Internal Audit's work, the actions agreed with management to address any issues raised and the status of previously agreed actions; – Regular interactions with the Group Director Internal Audit during the year, including private sessions with the members of the Committee and specific workshops with Internal Audit and senior management to discuss audit planning and priorities; – Assessed the annual performance of the Group Director Internal Audit. The Group Director Internal Audit continued to report directly to the Chair of the Committee, with a secondary reporting line to the Chief Executive Officer for administrative purposes; – Considered deep dive analysis from Internal Audit on a number of matters including: Internal Audit's increasing use of Data Analytics and Internal Audit's delivered and planned work across the Group's IRB framework; and – Reviewed the results of internal and external quality assurance reviews on the effectiveness of the Internal Audit function.
The Internal Audit function was sufficiently resourced and skilled to operate as a standalone entity	– Monitored the adequacy of Internal Audit resources, including the financial budget and capability to draw on external specialists when appropriate. This included an externally facilitated peer benchmarking exercise conducted during the year.
External audit Responsible for overseeing the relationship with the External Auditor	– Approved the annual audit plan, approved the engagement letter and agreed the auditor's remuneration. The Committee was authorised by shareholders at the 2018 AGM to agree the remuneration of the External Auditors; – Reviewed the findings of the external audit including key judgements and the level of challenge provided by the External Auditor; – Reviewed the findings of the FRC's Audit Quality team's inspection of EY's audit of the 2017 Group audit; – Reviewed the External Auditor's representation letter; and – Reviewed management's responses to control findings, non-compliance and any other findings identified by external audit.
Assessed the performance of the External Auditor	– The Committee considered the effectiveness of the audit process and the External Auditor performance as part of an annual performance review which takes into account management's assessment of audit effectiveness. The assessment focused on the areas of judgement; mindset and culture; skills, character and knowledge; with an overarching assessment of quality control.

Governance

Audit Committee report

Role of the Committee	Key matters considered and actions completed
External Auditor independence and objectivity, and remuneration for audit and non-audit services	– Both the Board and the External Auditor have safeguards in place to protect the independence and objectivity of the External Auditor which are detailed in the External Auditor Policy Standard (Policy Standard). This Policy is reviewed at least annually and was refreshed during 2018; – The Policy Standard details the nature of the services that the External Auditor may not undertake and specifies that non-audit services may not be pre-approved and are subject to prior approval from the Committee or a delegate. In certain cases, the External Auditor may be selected over another service provider due to their detailed knowledge and understanding of the Group's operations. Any allowable non-audit service with a value above £100,000 requires approval from the Chair of the Committee. The Policy Standard also specifies that the overall fee for non-audit services be continually monitored and should not exceed 70% of the average audit fee over the prior three-year period; – The total amount paid to the External Auditor in 2018 was £2,518k (2017: £1,766k). Non-audit services of £820k (2017: £432k) performed by the auditor during the year included the review of the Interim Financial Report; agreed upon procedures under the Conduct Indemnity arrangement with NAB; preparation of a comfort letter for the global medium-term note programme issuance; and a TFS assurance review. The increase in the year is principally due to reporting accountant procedures in relation to the Virgin Money transaction. Payments by the Group for both audit and non-audit services provided in 2018 and 2017 are further detailed in note 2.4 to the financial statements; and – The Policy Standard also regulates the appointment of former audit colleagues to senior finance positions in the Group.
Following the Committee's review of the effectiveness of the external audit process and the assessment of the External Auditor's independence and objectivity, it has recommended to the Board the reappointment of EY as the Group's External Auditor for recommendation to and approval by shareholders at the 2019 AGM.	
The External Auditor, the Senior Statutory Auditor and The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014	– EY has been the External Auditor for Clydesdale Bank PLC and other Group entities since January 2005. EY was appointed as the Company's External Auditor on 14 January 2016 following an audit tender, shortly before the Company became the holding company of the Group and for the initial period, post the Demerger and IPO in February 2016, however, the Committee recommended that this be kept under review; – The Group has no current retendering plans. The Committee undertook a competitive tender of the audit of the Group in early 2015. In applying the CMA's requirements, the next mandatory tender would be in respect of the 2026 financial year; – Steven Robb fulfils the role of Senior Statutory Auditor for the second year and EY will continue to practice the rotation of the Senior Statutory Auditor responsible for the Group audit at least every five years; all other audit partners and audit senior management will be required to rotate at least every seven years; – The Committee continues to follow developments in the reform of the external audit regulations and the UK and European requirements on publicly listed banking groups; and – The Committee confirms that the Group has complied during the period of financial review and to the date of this report with The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014, which relates to the frequency and governance of tenders for the appointment of the External Auditor and the setting of a policy on the provision of non-audit services.

Risk Committee report

"The Committee maintained its approach of supporting the Board in ensuring strong and effective risk management and promoting a risk culture that supports the safety and soundness of the firm and fair treatment of its customers."

Dear shareholder,

I am pleased to report on how the Committee has discharged its responsibilities throughout the financial year ended 30 September 2018.

On 30 June 2018, David Browne retired as a Director of the Company and I'd like to thank him for his contribution as a member of the Committee. Following the acquisition of Virgin Money on 15 October 2018, the Committee welcomed Geeta Gopalan to the Committee. As a result, the Committee continues to comprise six independent Non-Executive Directors.

Highlights in 2018

During the year, the Committee maintained its approach of supporting the Board in ensuring strong and effective risk management and promoting a risk culture that supports the safety and soundness of the firm and fair treatment of its customers. The Committee considered the Group's RAS and associated metrics in alignment with the Group's strategic and financial plans and provided appropriate challenge to ensure that the RMF remains fit for purpose. It continued to review stress and scenario analysis to give assurance on the Group's ability to mitigate potential risks.

An area of focus for the Committee, was to provide oversight of performance of IRB models submitted to the PRA to support the Group's application to adopt the IRB approach for the calculation of Credit Risk Weighted Assets (RWA). I am delighted the Group received IRB accreditation for the Group's mortgage and SME/Corporate portfolios which was announced on 11 October 2018 and this will take effect in the first quarter of the 2019 financial year. Achieving IRB status improves our capital ratios and capital efficiency and will help us grow the business in a prudent, sustainable manner. Jointly with the Audit Committee, it also reviewed the model and calculation engine capability to support the credit impairment element of IFRS 9 to support implementation from 1 October 2018.

The Committee, through a balanced agenda, has ensured there is sufficient focus on the management of principal risks and the identification and monitoring of top and emerging risks that may have an impact for its customers, products, operating model and strategy. The environment in which the Group operates continues to be subject to considerable change. Uncertainties include heightened political and economic risk in the UK in the backdrop of the UK's withdrawal from the EU and the uncertain outcome of Brexit negotiations and wider geopolitical risks. The Committee has monitored developments and associated impacts on the Group's risk profile. Given high profile cybersecurity breaches and the rising level of cyberthreat across many industries, where the dynamic nature and significance of related risks and challenges continue to evolve, the Committee has increased focus on ensuring strong levels of operational resilience including improving defences for cybersecurity. The Committee has also been provided with ongoing updates to monitor changes in various mandatory regulatory requirements on the horizon, including ring-fencing legislation and the Minimum Requirement on Own Funding and Eligible Liabilities (MREL) and provides oversight of the Executive Leadership Team's plans to implement and apply these regulations.

The following report sets out the principal risks, and areas of top and emerging risks the Committee evaluated over the year. More details on the wider risk profile and the RMF that the Committee oversees can be found in the Risk overview within the Strategic report on pages 16 to 17 and in the Risk report on pages 121 to 170.

Looking ahead

Many of the areas the Committee focused on in 2018 will again be areas of focus for the Committee in 2019, reflecting the complex environment in which the firm operates and the rightly high expectations of our stakeholders that the Bank is managed prudently and in the interests of our customers. In addition, the Committee will oversee the embedding of IRB into the business and following the acquisition of Virgin Money, as part of the integration planning, the Committee will consider how the RAS and RMF are applied across the Combined Group to ensure the Group has the appropriate risk tolerances in place.

Clive Adamson
Chair, Risk Committee

Governance

Risk Committee report

Membership and meetings

The current members of the Committee are:

Clive Adamson, Chair

David Bennett

Paul Coby

Geeta Gopalan (appointed 15 October 2018)

Fiona MacLeod

Tim Wade

As at the date of this report, the Committee comprises six independent Non-Executive Directors who have a variety of industry backgrounds, including banking and financial services. Membership of the Committee has been designed so that there is a deep understanding of the risk management, banking and financial sector expertise it needs to fulfil its responsibilities. In addition to the Committee members, the Chairman, Chief Executive Officer, Group Chief Financial Officer, Group Chief Operating Officer, Group Chief Risk Officer, Company Secretary, Group General Counsel, Group Director Internal Audit, and Head of Regulatory and Compliance Risk are invited to attend Committee meetings. The Chair is also a member of the Audit Committee.

Committee attendance

The core activities of the Committee were carried out in four scheduled meetings of the Committee. One additional ad hoc meeting was arranged for decisions required outside scheduled meetings. The Audit Committee and Risk Committee also hold at least one joint meeting per year. The table below shows the Committee members during the year ended 30 September 2018 and their attendance at scheduled Committee meetings.

	Number of scheduled Committee meetings eligible to attend	Number of scheduled Committee meetings attended
Committee Chair		
Clive Adamson	4	4
Committee members		
David Bennett	4	4
Paul Coby	4	4
Fiona MacLeod	4	3(1)
Tim Wade	4	4
Former Committee members		
David Browne (2)	3	3

(1) Unable to attend the meeting due to personal reasons.

(2) David Browne retired as a Committee member on 30 June 2018.

Committee role and responsibilities

During the year, the Committee revised its Charter which sets out the role and responsibilities of the Committee. The Charter of the Committee can be found on the Company's website www.cybg.com/about-us/corporate-governance/

Committee performance evaluation

During the year, the Committee adopted the work plan from the external Board Performance Evaluation carried out in 2017 which has driven the agenda setting and debate and discussion during the year. The internal evaluation of the Committee at the end of 2018 concluded the Committee was effective with no significant areas of concern noted.

Matters considered and actions taken by the Committee

The significant matters addressed by the Committee during the financial year ended 30 September 2018 and in evaluating the 2018 Annual Report and Accounts are described in the following pages.

Role of the Committee	Key matters considered and actions completed
Enhancing the RAS and stress testing Reviewing and approving the Group's risk appetite	– Conducted six-monthly reviews and recommended any updates to the Board for approval of the RAS taking into consideration the strategic objectives and target business model of the Group as well as the environment in which it operates; – Reviewed a combined Group Day 1 RAS for the acquisition of Virgin Money to ensure the Combined Group had the appropriate risk tolerances in place; – Reviewed regular reports of performance against each RAS measure, and assessed and confirmed the adequacy of management actions in relation to actual or potential breaches of Red and Amber RAS thresholds; – Refreshed the statements of appetite and limit settings for the material sources of risk during the year; and – Reviewed deep-dive analysis on a variety of risk matters including: Corporate Failure Contagion, Financial Crime and IT Cyber Security, Technology and Resilience Risk.
Reviewing the ICAAP and ILAAP and recommending approval to the Board	– Reviewed and monitored the capital, funding and liquidity profile through the ICAAP and ILAAP processes.
Embedding the risk framework and governance Providing oversight and reviewing the application of the Group's risk management, compliance and control systems	– Reviewed and approved proposals to refresh and update the RMF in relation to the evolving nature of the Group's activities; – Reviewed and approved an updated Policy Management Framework which provides the overarching principles and minimum control requirements that operate across the Group to mitigate risks to within the Group's risk appetite; – Considered a refresh of and updated the Group's range of Principal Risk Policy Statements which were supported by deep dive reviews into the application and effectiveness of the policy led by the Policy Statement owners; – Received reports on the Risk Management Framework with a focus on the effectiveness of controls relating to the Group's Policy Statement; – Considered an annual review of the Group's anti-money laundering and counter-terrorist policy, systems and controls; and – Reviewed the policies and procedures for preventing and detecting fraud and bribery.
Supporting an effective risk culture Ensuring that all colleagues operate in line with the Group's risk focused culture	– Continually assessed risk culture, including considering risk events and undertaking root cause analysis; – Considered any risk adjustments to be taken into account by the Remuneration Committee when making remuneration decisions for 2018 and 2019.
Risk management Overseeing the risk profile and risk management of the Group within the Board approved RAS	– Reviewed and challenged regular reports from the Group Chief Risk Officer that considered matters of concern on the material sources of top and emerging risks to the Group and outlined the remedial activities initiated to ensure that the risk was brought within risk appetite; – Reviewed and challenged regular reports from the Group Chief Financial Officer to manage the risks related to Funding, Liquidity and Capital; – Approved the annual Three Lines of Defence Oversight and Assurance Plans and received regular updates on the adequacy and effectiveness of the application of the risk and control framework; – Received updates on the output of assurance activities from the Three Lines of Defence regarding internal control processes for risk management; – Carried out an assessment of the Viability Statement in the 2018 Annual Report and Accounts and advised the Board and Audit Committee to that effect; and – Alongside other risk categories, oversaw Conduct Remediation Programmes ensuring that they deliver the right outcomes for our customers.

Governance

Risk Committee report

As part of the RMF, during the year the Committee maintained oversight of the following identified principal risks and associated top and emerging risks:

Risk categories considered	Key matters considered and actions completed
Credit risk The risk of loss of principal or interest stemming from a borrower's failure to meet contracted obligations to the Group in accordance with the terms agreed. Credit risk is evident at both a portfolio and transactional level.	– The Committee regularly reviewed the performance of the credit risk portfolio, including concentrations alongside changes in the economic environment to ensure that concentration risks were minimised. An area of particular focus and attention is the Group's mortgage portfolio spread and the level of concentration of mortgage lending; and – Jointly with the Audit Committee, reviewed the model and calculation engine capability to support the credit impairment element of IFRS 9 for implementation from 1 October 2018; **Emerging risk – Macroeconomic environment –** The impact of the sustained low interest rate environment places increased pressure on the Group's financial performance and, conversely, a sharp rise in interest rates may lead to an increased risk of default rates and credit losses. **Emerging risk – Consumer credit –** Maintaining awareness of the risk of significant unforeseen credit losses occurring within a short time period which has the potential to have a detrimental impact on earnings and profitability. Unsecured consumer lending is an area of considerable regulatory focus and one where the Group is particularly alert to potential regulatory, economic and customer impacts.
Balance sheet and Prudential regulation risks This covers a number of categories of risk which, combined, affect the manner in which the Group can support its customers in a safe and sound manner	– The Committee monitored closely the Group's funding and capital positions giving due consideration to any additional risks arising from increased market uncertainty following changes in the macroeconomic environment, including the Brexit negotiations, which continue to create significant economic uncertainty for the UK; – At each meeting the Committee considered a report from the Treasurer which provided an update on the Group's exposure to balance sheet and prudential regulation risks; – Considered the Group's recovery plan in the event of a significant deterioration in financial stability; and – The Committee considered the impact of Structural Reform legislation and the Group's progress to compliance.
Regulatory and compliance risks This consists of regulatory strategy and change risk, regulatory relationship risk and the risk of failing to understand and comply with relevant laws, regulations, licence conditions, supervisory requirements, industry codes of conduct and voluntary initiatives.	– The Committee obtained frequent briefings from management on forthcoming regulatory developments and upstream risk, to allow members to consider and oversee the implications of these on the Group's strategic objectives and operations, systems and controls; and – Regular updates were received by the Committee from the Group Chief Risk Officer on progress made towards achieving IRB accreditation and reviewed the performance of IRB models submitted to the PRA to support the Group's application to adopt the IRB approach for the calculation of Credit Risk Weighted Assets (RWA). **Emerging risk – Regulatory capital requirements –** The Group, in common with the financial services industry as a whole, continues to face a significant agenda of regulatory and legislative change, such as the Basel III framework and MREL requirements.
Conduct risk Defined as the risk of treating customers unfairly and/or delivering inappropriate outcomes resulting in regulatory fines, compensation, redress costs and/or reputational damage.	– Through the execution of the Group Conduct Strategy, the Committee oversaw the pro-active review of the business for potential conduct issues; – The Committee monitored progress to remediate key legacy conduct issues throughout the year, including PPI and other remediation programmes; and – The Committee received regular updates on the implementation and effective execution of the Group Conduct Strategy including the bi-annual Conduct Framework assessment and the development of enhancements to conduct risk management information and assurance. The Committee oversaw performance against conduct risk appetite including the introduction of additional and enhanced Conduct-related RAS measures.

Risk categories considered	Key matters considered and actions completed
Operational risk The risk of loss resulting from inadequate or failed internal processes and systems or from external events.	– The Committee reviewed the Group's Operational Resilience Framework to ensure that the controls and processes associated with the four key resilience pillars of People, Information Technology (including oversight of the effectiveness of actions to exit remaining Transitional Service Agreements (TSA) with NAB), Suppliers and Property were embedded across the organisation.
	Emerging risk – Cybersecurity and IT – As there are increasing levels of attempted cyberattacks across the industry, the Group remains vigilant to the potential risk of such attacks including: service interruption, data loss, customer and financial detriment and reputational damage.
Financial crime risk The risk that the Group's products and services will be used to facilitate financial crime against the Group, its customers or third parties.	– The Committee maintained oversight of the effectiveness of the Financial Crime Framework for monitoring, management and mitigation of financial crime and considered reports on the strength of the Group's cybercrime defence strategy.
	Emerging risk – Financial crime (including cyber-enabled financial crime) – The Group in conjunction with the wider industry continues to be subject to increasing fraud attacks. There is a risk that the Group is unable to keep pace with the increased threat of cyber-enabled crime that digital expansion presents. External data loss events are driving an increasing threat of social engineering and account takeover due to the volume of compromised data available.
Strategic, business and financial performance risk The risk of significant loss of earnings and/or damage arising from business decisions that impact the long-term interests of stakeholders or from an inability to adapt to external developments.	– The Committee reviewed a consolidated report outlining the triggers and exposure to strategic risk by the Group Chief Risk Officer.
	Emerging Risk – Acquisition of Virgin Money – The risks associated with the acquisition of Virgin Money have been described in detail in the prospectus to the transaction. The acquisition presents a significant programme of change requiring prudent management in order to deliver the benefits from the transaction.
	Emerging risk – Geopolitical uncertainty – The UK's withdrawal from the EU (Brexit) with ongoing negotiations has created significant economic uncertainty and a potential negative impact for the UK macroeconomy.
	Emerging risk – Competition – The financial services industry is a highly competitive environment. The emergence of new entrants and regulatory initiatives, such as Open Banking, may lead to material changes in the future provision of financial services.
People risk The risk of not having sufficiently skilled and motivated colleagues who are clear on their responsibilities and accountabilities and who behave in an ethical way.	– The Committee provided oversight of key people risks such as capability and capacity planning, values and behaviours, inclusion and health and well-being.

Further details on the Group's approach to risk appetite, risk culture, the RMF, and significant and emerging risks can be found in the Risk report beginning on page 121.

Governance

Statement by the Chair of the Remuneration Committee

"The Committee continues to ensure the Group's remuneration arrangements support delivery of its strategic priorities for 2019 and onwards."

Dear shareholder,

As Chair of the Remuneration Committee, I am pleased to present the Directors' remuneration report, including details of the Directors' and Non-Executive Directors' pay, for the year ended 30 September 2018.

Our Directors' remuneration policy (the Policy) was approved by shareholders in 2017 and no changes to the approved policy are proposed for 2019.

This statement and the accompanying report demonstrate the framework in which decisions have been made, the outcomes for the 2018 performance year and how the Committee plans to approach the year ahead.

The successful acquisition of Virgin Money and what this means for the future of the Group is an important consideration for the Committee as we look to the coming year. As we integrate the two businesses it is critical that we retain and motivate our Executive Leadership Team and colleagues to execute the Group's strategy.

2018 review

During 2018 the Group has maintained momentum in delivering against its strategic priorities. These priorities and commitments will remain unchanged for the combined Group, providing sustainable customer growth, efficiency and capital optimisation delivered by a strong customer-focused culture, all within a framework of prudent risk management and governance. This framework will once again be reflected in our remuneration arrangements and will be supported by the implementation of our remuneration policy for 2019.

Underlying profit is up 13% and underlying CIR has improved by 4% from 67% to 63%. Overall underlying costs for the year of £635m were ahead of plan. Balance sheet growth continued based on a prudent risk appetite with core loans increasing by 4.7% as mortgage balances increased by 4.5% and core SME balances grew by 5.6%.

Following the success of the demerger and IPO, we continued a programme of delivering cost efficiencies throughout 2018. Against this backdrop of change, our colleague engagement increased to 76, a rise of four percentage points. The results show an increase across a number of categories and our scores remain strong.

As detailed in the annual report on remuneration, a substantial majority of both financial and non-financial targets set by the Committee for the 2018 bonus were achieved. However, this year we did not achieve our bonus threshold levels for our customer metric (NPS) and Cost:Income Ratio. Therefore, the Committee approved an outcome of 42% for the element of bonus linked to company performance. No allowance was made for the acquisition of Virgin Money on determining the Company performance element. Details of the element of bonus linked to personal performance for the Executive Directors can be found on pages 102 and 103 of this report.

Changes to the Board

Debbie Crosbie, Group Chief Operating Officer, stepped down from the Board and from her role as an Executive Director on 19 November 2018. She will remain in her role as Group Chief Operating Officer for a period of time to facilitate an orderly handover with a leaving date to be agreed. Details of her remuneration arrangements on departure are detailed on page 98.

Considerations for the year ahead

The Committee will continue to operate within the existing approved Directors' remuneration policy in 2019 and will continue to focus on ensuring the remuneration policy remains in line with the market and compliant with regulatory requirements. Our continuing strategy will align the interests of the Executive Directors and shareholders. Following the acquisition of Virgin Money, the continuing uncertainty over the pending exit of the UK from the EU and the relatively high inflation figures, the Committee will also focus on ensuring the Group is able to attract, retain and motivate key talent at all levels of the organisation, in a challenging market.

The Remuneration Committee recognises that value creation for shareholders will be delivered through the successful implementation of the long-term strategy. Therefore, in conjunction with advisors, the Remuneration Committee initiated a full review of our Policy against that of other financial services companies to determine whether the current arrangements will be sufficient to retain our talented team who have delivered well and who are considered essential to the next phase of the Group's development.

Based on the findings of that review we intend to evolve how we implement the Policy for 2019. We propose to introduce certain adjustments to the implementation of our compensation arrangements that are permitted by the prevailing European Banking Authority's (EBA) regulations, can be delivered by our approved Policy and that are common across the financial services sector in the UK. Please note that in reviewing the total compensation arrangements for Executive Directors our focus is on increases to variable pay, 60% of which will be delivered over the long term and vest over three to seven years with an additional one-year holding period. More detail on the implementation of our Policy this year is detailed in the Implementation Report on pages 99 to 104 of this report.

Executive Directors' salaries and Non-Executive Directors' fees

It is the Committee's intent that Executive Director salary increases remain aligned to those applied to colleagues generally across the Group. However, as per our Policy, the Committee reserves the right to provide increases that are greater than those applied across the Group where there is a strong rationale to do so.

This year the CEO and CFO will receive an increase in line with those applied to Group colleagues of 2%, effective from 1 October 2018. This will be the first time since joining the Group in 2015 that the CEO has seen his salary increase. The COO's salary will increase, for the first time since 2016, by 5.6% to £475,000. This was approved prior to her resignation and will be paid from 1 October 2018 until her employment ceases.

CYBG Non-Executive Directors' fees were set in November 2015 in preparation for and payable from listing of CYBG in February 2016 and whilst they have been reviewed annually they have not changed since. From 15 October 2018, being the point the Scheme of Arrangement in relation to CYBG's offer for Virgin Money became effective, the CYBG Non-Executive Directors have been appointed Non-Executive Directors of Virgin Money. There are additional Board Committee roles for some Non-Executive Directors .

Therefore, following review it is the intention of the CYBG Board to change the rates for fees payable to Non-Executive Directors for the year ending 30 September 2019.

The new fee structure has sought to ensure that Non-Executive Directors' fees are reflective of the additional responsibilities and time commitment in the combined Group. Details of the new Non-Executive Directors' fees including that of the Chairman approved by the Committee, are detailed on pages 106 and 107.

Pay and employment conditions of other colleagues in the Group were taken into account when considering these outcomes. Building an improved colleague proposition across CYBG has been a key area of focus and for 2018 this included the introduction of private medical insurance and Group income protection as core benefits for all colleagues across the Group.

Variable pay

The Committee will set appropriate and stretching annual variable reward targets for the year ahead based on the new combined Group's key financial, risk, customer and culture objectives. The Remuneration Committee is committed to providing transparency in decision making in respect of the Group's incentive plans. It will disclose when available, targets and measures; together with information relating to performance against those targets, except to the extent that the Board deem these to be commercially sensitive, in which case it will disclose this information once it is deemed not to be sensitive.

The new Long-Term Incentive Plan (LTIP) award for our Executive Directors, awarded in respect of performance in the financial year ended 30 September 2018, is subject to a three-year performance period (1 October 2018 to 30 September 2021) and a three- to seven-year deferral period. This ensures a significant proportion of Executive Directors' remuneration continues to be deferred and delivered in shares and that Executive Directors' remuneration is aligned with the delivery of our combined Group's long-term strategy and the long-term interests of shareholders.

However, as you will be aware the acquisition of Virgin Money has only just completed. The timing of the acquisition presents several additional considerations when it comes to the application of our Policy for 2019 and the development of our variable pay arrangements for the coming year. We intend to maintain the general technical design of both our bonus and LTIP, as we believe our current framework continues to provide high levels of alignment between the interests of our customers, regulators, shareholders and the Group. However, whilst we remain committed to the synergy savings we detailed in the prospectus for the acquisition of Virgin Money we will not be in a position to confirm the quantitative metrics, targets and weightings in this year's Implementation Report and until we are able to integrate both the financial and non-financial performance indicators for the Combined Group.

Consideration of shareholders' views

Shareholders have an essential role to play in guiding responsible pay practices. The Committee received feedback from our major shareholders ahead of the 2017 Annual General Meeting (AGM), and took account of these views when formulating our Policy, which was reflected in the high levels of support for resolutions relating to remuneration. For each subsequent year we have continued to engage directly with our main shareholders both here in the UK and in Australia.

On behalf of the Board, I am pleased to recommend this statement to shareholders, ahead of the 2019 AGM.

Adrian Grace
Chair, Remuneration Committee

This report has been prepared in accordance with Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 as amended in 2013, the provisions of the UK Corporate Governance Code (2016) and the Listing Rules.

On behalf of the Board

Adrian Grace
Chair, Remuneration Committee
26 November 2018

Governance

Directors' remuneration report

Directors' remuneration policy – abridged

Directors' remuneration policy and principles

The current Directors' remuneration policy approved by shareholders at the AGM on 31 January 2017 remains in force. The Committee will consider the remuneration policy annually to ensure that it remains aligned with business needs and is appropriately positioned relative to the market. There is no intention to revise the Policy more frequently than every three years, unless amendments to the Policy are required in the interim, in which case appropriate shareholder approval will be sought.

An abridged version of the Policy which includes the remuneration tables for Executive Directors and Non-Executive Directors is included in the following pages for reference. This does not replace or override the full approved policy which is available on pages 106 to 115 of the 2016 Annual Report and Accounts available at: www.cybg.com/investor-centre/annual-reports/

Details on how the policy will be applied in 2019 are included on pages 99 to 104 of the report. In applying this policy the Group remuneration approach remains to:

- provide competitive, transparent and fair rewards, benefits and conditions;
- reward achievement of short- and long-term individual objectives and business strategy;
- align the interests of colleagues and shareholders through colleague share ownership;
- deliver outcomes over short- and long-term horizons with appropriate performance and risk adjustments, ensuring performance assurance principles are applied;
- support the RMF with regard for the risk appetite of the Group; and
- attract, recognise, motivate and retain high performers.

Remuneration arrangements are fully compliant with, and will be operated in line with, all regulatory requirements, including the PRA Remuneration Code and are in line with UK listed financial services sector best practice.

Our peer group companies

The CYBG comparator peer group was reviewed by the Committee and is defined as other UK-based banks and wider financial services firms of a comparable size, divisional heads in larger UK banks and other FTSE companies reflecting our market capitalisation.

Elements of package – fixed remuneration

The policy in relation to each element of Executive Directors' remuneration is set out in the following tables.

Base salary

Purpose and link to strategy	Recruit, reward, retain and recognise leadership position and responsibility for delivering strategy.
Operation	Base salaries are paid in 12 equal monthly instalments during the year and are reviewed annually. When determining and reviewing base salaries, the Committee considers: – Group and individual performance; – the skills, experience and responsibilities of the Executive Director and their market value; – the scope and size of the role; – base salary increases for colleagues throughout the Group; and – external benchmarks data for peer banks, the divisional heads of larger UK banks and FTSE data reflecting our market capitalisation.
Maximum potential	The Committee will seek to limit pay increases for Executive Directors, where there is no change in role, to those applied to colleagues generally across the Group. However, where an Executive Director is relatively new in role the Committee reserves flexibility to provide increases that are greater than those applied across the Group to bring the individual's salary into line with the market and reflect the gaining of experience.
Other colleagues	The approach takes into account affordability, economic factors, external market data, business and personal performance.

Pension

Purpose and link to strategy	Recruit, reward, retain key talent and contribute towards individuals' funding for retirement.
Operation	Executive Directors are entitled to participate in the Group defined contribution pension scheme or may receive a cash allowance in lieu of some, or all, of the employer pension contribution. The Group's defined benefit pension scheme closed to new entrants in 2004 and closed to future accrual of benefits for the majority of colleagues from 31 July 2017.
Maximum potential	The maximum cash allowance for Executive Directors will be set at 20% of an Executive Director's base salary. Only one Executive Director was a member of the Group's defined benefit scheme prior to it closing to future accrual in 2017 and they ceased to accrue benefits from 31 July 2017 in line with the majority of other colleagues. For members of the Leadership Team who are affected by the Annual and Lifetime Allowances for pension saving, the Bank introduced two options in addition to participation in the defined contribution pension scheme under the standard terms. The two options are a cash allowance in lieu of pension contributions from the Bank or a combination of pension contributions and cash of an equivalent value.
Other colleagues	All new colleagues are automatically enrolled in the Group's defined contribution pension scheme. In line with pensions legislation the minimum colleague contribution is 2% of pensionable salary. The Group operates a contribution matching scheme with contributions ranging from a minimum 8% based on the 2% minimum colleague contribution up to a maximum of 13% based on an employee contribution of 7%.

Benefits

Purpose and link to strategy	To provide benefits consistent with role.
Operation	The Group provides a range of benefits which can include private medical insurance, health assessments, life assurance and car allowance/car. The Committee retains the discretion to provide additional benefits as may be reasonably required. These may include relocation benefits such as (but not limited to) accommodation, family relocation support and taxable travel. The Executive Directors are entitled to a maximum of 30 days holiday in addition to applicable bank/public holidays.
Maximum potential	The CEO has a cap of £250,000 on his benefits, including pension contributions and any cash allowance in lieu of pension contributions. For the other Executive Directors, the maximum value of benefits is set by the nature of the benefits and the cost of providing them.
Other colleagues	The Group provides a range of benefits based on colleagues' roles, which include flexible benefits allowances, private medical insurance, health assessments, life assurance and car allowance/car. Colleagues receive between 25 and 30 days' holiday annually depending on their role.

Governance

Directors' remuneration report

Directors' remuneration policy – abridged continued

Elements of package – variable remuneration

Bonus

Purpose and link to strategy	The annual bonus is designed to reward Group and personal performance in line with strategic objectives.
Operation	Annual bonuses are discretionary and are based on Group and individual performance within the year. The measures, their weighting and targets are set annually with awards determined by the Committee at the end of the financial year. The annual bonus may be delivered in cash and shares, which, in combination with the LTIP awards and any relevant awards under the all-employee Share Incentive Plan (SIP) will be structured in line with the requirements on the deferral of variable pay under the PRA Remuneration Code. The equity-based element of the award will be made as rights to CYBG shares or other instruments, which are released at the end of the required holding period. The mechanism for making these awards will be the Deferred Equity Plan (DEP). The amount and deferral period for bonus will be determined in line with regulatory requirements and to the extent that the LTIP award does not fully meet the deferral requirements. Dividends or dividend equivalents accrued on deferred annual bonus shares are paid on vesting, subject to the extent permitted under the relevant remuneration regulations. For the 2019 performance year dividend equivalents will not accrue on deferred annual bonus shares. Discretion may be exercised by the Committee to ensure that the bonus outcomes are a fair and accurate reflection of the business and individual performance and consider any risk-related issues (but may not exceed the maximum opportunity). The Group can, in specific circumstances, apply malus and/or clawback to all or part of any bonus award.
Maximum potential	Taken together with the LTIP awards, total variable remuneration is limited by the 2:1 ratio of variable pay to fixed pay, subject to the LTIP award being at least half of the total variable pay award.
Performance conditions	Performance measures are set by the Committee each year and are set out in the Annual Report on remuneration, normally this would be: – 80% of the annual bonus opportunity for Executive Directors is based on performance of the Group against key financial and non-financial measures; and – 20% is based on personal performance and behaviours. When determining the outcome of the performance measures, the Remuneration Committee will seek the advice of the Risk Committee to ensure all relevant risk factors are identified and the bonus pool and/or individual awards adjusted accordingly. Specific measures, targets and weightings will be set by the Remuneration Committee annually and disclosed on a retrospective basis.
Other colleagues	All colleagues within the Group below Leadership Team level are in a single Group-wide scheme with target opportunities ranging from 8% to 50% of salary depending on role. For Leadership Team members below Executive Director target opportunities range from 52% to 57% of salary depending on role. Awards will be funded from a bonus pool reflecting the same financial and non-financial measures that apply to Executive Directors. When determining the outcome of the performance measures the Remuneration Committee will seek the advice of the Risk Committee to ensure all relevant risk factors are identified and the bonus pool and/or individual awards are adjusted accordingly.

Long Term Incentive Plan (LTIP)

Purpose and link to strategy	Delivery of the Group's strategy and growth in shareholder value.
Operation	Awards are based on a three-year performance period reflecting a basket of business and shareholder measures aligned with strategic goals. Awards will vest a minimum of three years after being awarded, or longer, for example where required by the PRA Remuneration Code. Where a period of deferral extends beyond three years, awards will only be subject to service requirements for the first three years, thereafter awards will only be subject to forfeiture for reasons of gross misconduct or malus. The value of awards for the purposes of determining total variable remuneration will be in line with the rules set by the Regulator. The Committee, in its absolute discretion, will determine the level of the LTIP awards made under the LTIP after taking account of an Executive Director's individual performance and business performance. Any LTIP award, when combined with any deferred element of the annual bonus, will meet the deferral requirements under the PRA Remuneration Code. Malus and clawback also apply to the whole of the LTIP award in line with the requirements of the PRA Remuneration Code. Awards are made as conditional rights to CYBG shares, or other instruments, which will be released at the end of the holding period or later where required under the PRA's Remuneration Code. Dividends or dividend equivalents accrue on the LTIP awards and, to the extent that the award vests, are paid on vesting, subject to the extent permitted under the relevant financial services remuneration regulations. For the 2018 award dividend equivalents will not accrue.
Maximum potential	Taken together with the bonus award, the total variable remuneration is limited by the agreed 2:1 ratio of variable pay to fixed pay, subject to the LTIP award being at least half of the total variable pay award.
Performance conditions	Service and performance conditions must be met over a three-year period. Measures aligned with strategic goals are proposed for all LTIP awards: – Sustainable Customer Growth; – Efficiency; – Capital Optimisation; and – Prudent Risk Management and Governance. The weighting of metrics will be determined before each award with 25% of the maximum vesting for each measure for threshold performance. The measures reflect a balanced approach between financial and non-financial. The Committee has discretion to vary the weighting of performance metrics, or to substitute the metrics over the life of this Directors' remuneration policy. Shareholders will be consulted should the metrics themselves be varied. In determining the outcome, the Remuneration Committee will seek the advice of the Risk Committee to ensure all relevant risk factors are identified and the level of vesting adjusted accordingly.
Other colleagues	Members of the Executive Leadership Team and other senior managers are eligible to participate in the LTIP with awards made solely at the discretion of the Committee.

Governance

Directors' remuneration report

Directors' remuneration policy – abridged continued

Shareholding requirement

Purpose and link to strategy	To align Executive Directors' interests with those of shareholders.
Operation Executive Directors	Executive Directors are expected to build up a specified holding of CYBG shares equivalent to a percentage of salary. 60% of the shares vesting (after settling tax and National Insurance liabilities) from CYBG share plans must be retained until the shareholding requirements are met. **Executive Director** – **Shareholding requirement (% of salary)** CEO – 200% CFO and COO – 150% When assessing an Executive Director's shareholding against the requirement, vested awards which are held as rights rather than shares will be included based on the anticipated net number of shares that would be released to the Executive Director at the end of the holding period.
Other colleagues	Additionally, members of the Leadership Team below Executive Director are expected to build up a holding of CYBG shares equivalent to 100% of salary. 50% of the shares vesting (after settling tax and National Insurance liabilities) from CYBG share plans must be retained until the shareholding requirement is met.

Executive Director	Shareholding requirement (% of salary)
CEO	200%
CFO and COO	150%

Performance measures

The Committee selects the short- and long-term performance measures to ensure an appropriate balance between short- and long-term strategic goals and aligning the interests of Executive Directors with shareholders. Targets are set each year having regard to the strategic plan and consensus forecasts. Measures and targets for both the bonus plan and LTIP are aligned to the strategic plan and are approved by the Board.

The Committee may apply discretion, in exceptional circumstances (for example, if there is a major corporate event), to amend or vary targets or the weighting of performance metrics (measures), or to substitute the metrics over the life of this Directors' remuneration policy if these are no longer appropriate to ensure alignment with strategy and any risks within the business. The Committee will consult with the Group's risk management and control functions to ensure changes are appropriate and do not inadvertently encourage irresponsible or inappropriate behaviour. The Committee will consult with shareholders in advance of any change to performance metrics and retains discretion to adjust outcomes to ensure these are consistent with corporate performance.

Risk adjustments, malus and clawback

For Material Risk Takers (MRTs), which include the Executive Directors, bonus and LTIP awards may be reduced before they are released (malus) or may be subject to clawback where the Committee determines that an adjustment should apply. Clawback may be applied up to seven years from the award date, or 10 years for those holding a senior management function where an investigation has commenced.

Malus may be applied where: there is evidence of colleague misbehaviour, misconduct, material error, where a colleague participated in conduct which resulted in losses for the Group or they failed to meet appropriate standards; any material failure of risk management at a Group, business area, division or business unit level; if the financial results at a Group, division or business unit level are restated; if the financial results for a given year do not support the level of variable remuneration awarded; or any other circumstances where the Committee consider adjustments should be made. The Committee is supported in this by the Board Risk Committees and the CYBG Risk function.

Clawback may be applicable where there is reasonable evidence of colleague misbehaviour or material error, or there is material failure of risk management at a Group, business area, division or business unit level.

Other CYBG share plans

The Executive Directors are invited to participate in all-employee share plans on the same basis as other Group colleagues. These plans encourage share ownership, aligning colleagues' interests with those of shareholders and allowing them to benefit from the long-term success of the Group.

The CYBG SIP provides for the purchase of shares, in line with HMRC participation level rules, on a monthly basis from gross pay and is also the vehicle used to allow for awards of free or matching shares.

Each Executive Director received 256 free shares following the demerger (March 2016) and a further 159 free shares in November 2017. The CFO participates in the monthly purchase of shares through the SIP.

If operated in the future, Executive Directors will also be eligible to participate in any employee share plans operated by the Group.

Legacy arrangements

Awards granted under the NAB Share Plans were retained by colleagues of the Group following the demerger and IPO on 8 February 2016. Awards remain subject to their existing terms and performance conditions, with service requirements based on employment by Clydesdale Bank PLC.

Detailed below are the rights under the NAB LTIP held by the COO. Neither the CEO, nor the CFO received any NAB LTIP awards.

Debbie Crosbie's NAB LTIP awards	Vesting date	Release date (1)	Performance period (if applicable)	NAB performance rights
FY2013 LTIP	20 Dec 17	20 Jun 18	11 Nov 13 to 11 Nov 17(2)	10,161
FY2014 LTIP	21 Dec 18	21 Jun 19	10 Nov 14 to 10 Nov 18(2)	13,380

(1) Reflects the end of the six months post vesting holding period.
(2) Awards that do not vest at the end of the first performance period will be retested after 12 months.

The level of vesting for these awards is determined by the NAB Board, and in 2017 the NAB Board determined that the 2012 NAB LTIP should be lapsed in full.

The 2013 LTIP was due to be released in June 2018 and 2014 LTIP award is due to be released in June 2019. Both are based on NAB's relative Total Shareholder Return (TSR) performance with half measured against the S&P/ASX Top 50 Index peer group and half against a selection of financial companies in the ASX Top 200 peer group. In line with the terms of the awards those that do not vest at the end of the first performance period will be retested after 12 months. The 2013 LTIP award did not vest in December 2017 and will therefore be retested after the 12 months have elapsed.

The final decision on the level of vesting will be taken by the NAB Board, with value at the date of vesting included in the Directors' single table figure in the year they vest. As the COO stepped down from the Board on the 19 November 2018 the treatment of the awards in the future will be determined by NAB in accordance with rules of the NAB share plans.

Governance

Directors' remuneration report

Directors' remuneration policy – abridged continued

Illustration of the application of remuneration policy

The chart below illustrates the potential remuneration of the Executive Directors based on the policy in the following three scenarios:

– minimum remuneration based on fixed elements of package only including salary, pension, and cash benefits (i.e. Fixed Pay);

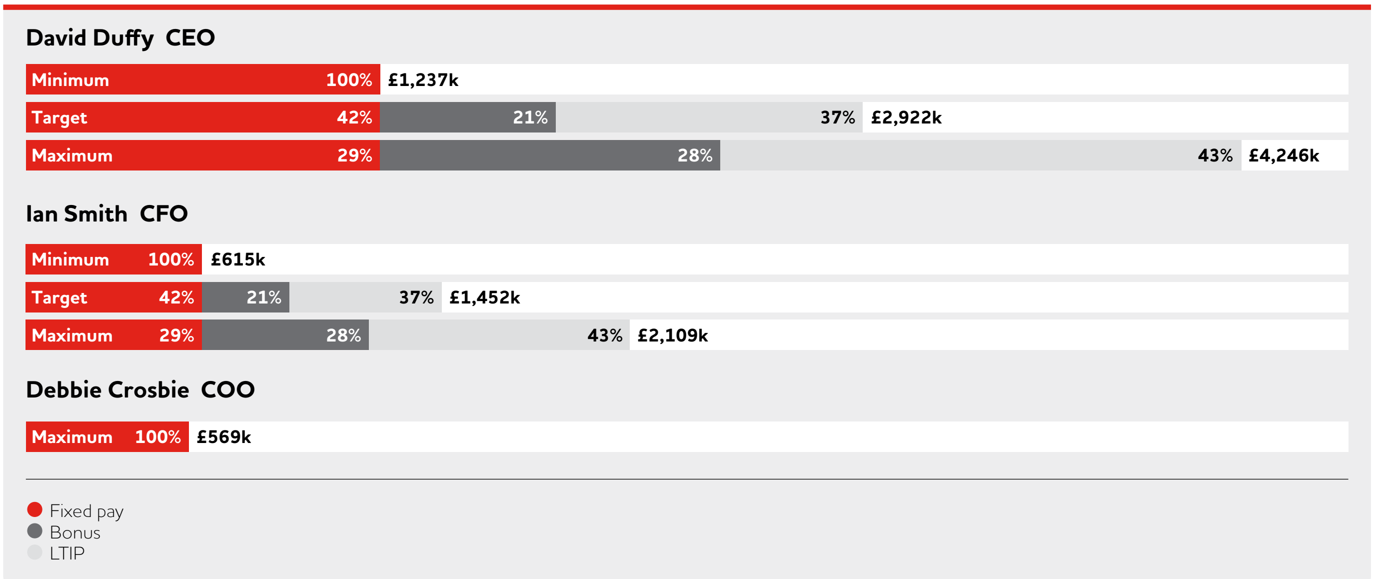
– target outcome assumes the actual bonus award is 50% of the maximum opportunity with 60% of the LTIP vesting; and

– maximum outcome which assumes the actual bonus award is 100% of the maximum opportunity and 100% vesting of the LTIP.

The amounts do not allow for share price appreciation but include implementation of the European Banking Authority's (EBA) discount factor. Salary figures are as at 1 October 2018. Full details on the bonus and LTIP opportunities for the CEO and CFO can be found on page 100.

The figures for the COO are limited to fixed pay (i.e. salary, car cash allowance, cash in lieu of pension benefit funding) based on the circumstances of her departure and until her employment with the Company ceases. More information on the remuneration arrangements for her departure can be found on page 98.

Potential 2019 remuneration outcomes



Service contracts and policy on payments for loss of office

Standard provision	Provision	Details
Election	All Executive Directors are subject to annual re-election.	
Notice periods within Executive Directors' service contracts	12 months notice from Company. 12 months notice from Executive Directors.	Executive Directors may be required to work during the notice period, unless determined otherwise.
Confidentiality	Six-month post-termination restrictive covenants.	Executive Directors are subject to a confidentiality undertaking without limitation in time, as well as to six-month post-termination restrictive covenants covering non-competition; non-solicitation of and non-dealing with clients; non-interference with suppliers or contractors and non-solicitation of colleagues.
Compensation for loss of office	Payment in lieu of notice of no more than 12 months' salary.	Payable monthly and subject to an obligation on the Executive Director to mitigate their loss such that payments will either reduce or cease completely if the Executive Director obtains alternative employment. In the event of redundancy, the Executive Director shall be entitled to receive statutory redundancy pay, together with outplacement and legal support.
Treatment of annual bonus on termination	With the exception of good leavers, where participants leave before 1 December they will not be eligible for an award.	The Committee has discretion to reduce the entitlement of a 'good leaver' in line with performance and the reason for leaving.
Treatment of unvested deferred bonus on termination	With the exception of good leavers, awards lapse where participants leave in the three years following the award being made.	Awards to good leavers will be retained in full, with no change to vesting or release dates. With the exception of gross misconduct and malus, service provisions end three years from the date of award.
Treatment of unvested LTIP awards on termination	With the exception of good leavers, awards lapse where participants leave in the three years following the award being made.	Awards to good leavers will be prorated, unless the Committee decides otherwise, to reflect the period worked in the three years following the award. The award will vest, unless the Committee decides otherwise, on the normal vesting date to the extent that any performance condition has been met. With the exception of gross misconduct and malus, service provisions end three years from the date of award.
Outside appointments	Executive Directors may accept outside appointments in other listed companies with Executive Directors retaining any fees received.	The Chair is required to approve appointments in advance. Agreement from the Board must be sought before Executive Directors accept any additional Non-Executive roles outside of CYBG. Procedures are in place to ensure that regulatory limits on the number of directorships held are complied with. Details of the directorships held can be found in the biographies section of the Corporate governance report.

Governance

Directors' remuneration report

Directors' remuneration policy – abridged continued

The Committee retains the discretion to determine whether an Executive Director is to be treated as a good leaver. Unless determined otherwise, an Executive Director will be treated as a good leaver in cases where their employment ends due to death, injury, ill-health, disability, redundancy, retirement, or the Company being transferred out of the CYBG Group and any other reason (except for dishonesty, fraud, misconduct or dismissal). The Committee reserves the right to make additional payments where such payments are made in good faith and are required to discharge legal obligations or are due to the breach of such obligations.

The notice periods and dates of their service contracts are shown below.

Executive Directors	Notice period	Date of service contract
Debbie Crosbie	12 months	24 November 2015
David Duffy	12 months	25 November 2015
Ian Smith	12 months	3 December 2015

Considerations of employment conditions elsewhere in the Group
Pay and employment conditions generally in the Group are considered when setting Executive Directors' remuneration. The Committee is provided with regular updates on overall pay and conditions, including negotiated pay increases for the broader colleague population, has oversight of significant changes in the provision of benefits (including pension provisions) and approves the colleague bonus pool.

During the year the Committee considered the following in relation to colleagues other than Executive Directors:

- remuneration packages of Executive Leadership Team members;
- design of the annual bonus plan for Executive Leadership Team and all colleagues;
- measures and targets for the 2019 annual bonus pool;
- identification and bonus awards for MRT;
- non-regulatory bonus deferral for MRT and other colleagues;
- annual inflation linked salary increases for all colleagues;
- changes to the performance management approach for all colleagues;
- policy in relation to pension arrangements for Executive Leadership Team members and other colleagues impacted by the pension Life Time Allowance/Annual Allowance;
- design of the 2018 LTIP and awards to members of the Executive Leadership Team and other Group senior colleagues (based on role); and
- commencement and termination payments made to MRTs.

The Committee does not specifically invite colleagues to comment on the Directors' remuneration policy but any comments made by colleagues are taken into account. Consideration is given to feedback provided by colleagues through the annual MyVoice colleague engagement survey.

Chairman and Non-Executive Directors' remuneration policy – abridged

The table below sets out the Non-Executive Directors' remuneration policy which applies to the Chairman and Non-Executive Directors.

Non-Executive Directors are engaged through letters of appointment which are for an initial period of three years, subject to three-months' notice by the Non-Executive Directors or the Group. The Chairman has a six-month notice period. All Non-Executive Directors are subject to annual re-election by shareholders at each AGM and are subject to early termination without compensation if he or she is not reappointed at a meeting of shareholders.

Non-Executive Directors' packages

Purpose and link to strategy	To ensure the Group is able to engage and retain highly skilled and experienced individuals.
Operation	Fees paid to the Chairman are determined by the Remuneration Committee, while the fees paid to the Non-Executive Directors are set by the Board annually. The fees reflect a base fee with additional fees payable for being members of, or chairing, Board committees and a separate fee is payable to the Senior Independent Director and Deputy Chairman. Non-Executive Directors are appointed for an initial three-year term and will normally serve two terms, exceptionally three. The fees are set at a rate that reflects the value to the Group and expected time commitment given the added regulatory complexity within the financial services sector. In exceptional circumstances, incremental fees may be paid for additional duties and time commitment, to reflect increased workload. From time to time, new Board committees may be established and/or responsibilities distributed between committees, at which point fees for committee membership and Chair may be reviewed. The Chairman and Non-Executive Directors are reimbursed for expenses incurred in performing their duties and any tax arising on such reimbursed expenses is borne by the Group. For individuals based outside of the UK this will include travel to and from the UK. Non-Executive Directors and the Chairman do not participate in any variable remuneration or benefits arrangements.
Maximum potential	The maximum aggregate value of fees payable to the Chairman and the Non-Executive Directors is capped at £2.5m under the Articles of Association.
Performance conditions	There are no performance conditions attached to the fees payable to the Chairman or Non-Executive Directors.

The dates of current Non-Executive Directors' letters of appointment are shown below:

Non-Executive Directors

Clive Adamson	19 May 2016
David Bennett	23 November 2015
Paul Coby	19 May 2016
Adrian Grace	11 November 2015
Fiona MacLeod	8 September 2016
Jim Pettigrew	11 November 2015
Teresa Robson-Capps	11 November 2015
Tim Wade	8 September 2016
Geeta Gopolan	15 October 2018
Darren Pope	15 October 2018
Amy Stirling	15 October 2018

Governance

Directors' remuneration report

Annual report on remuneration

Remuneration Committee

Membership and meetings

The Current members of the Committee are:

Adrian Grace, Chair

Jim Pettigrew

David Bennett

Fiona MacLeod (Appointed 5 November 2018)

All members of the Committee are independent Non-Executive Directors who serve on the Committee for a minimum three-year term and a maximum of six years. The Committee is chaired by Adrian Grace and it held six scheduled meetings during the financial year. Two ad hoc meeting were arranged for decisions required outside scheduled meetings.

The table below shows the Committee members during the year to 30 September 2018 and their attendance at scheduled Committee meetings. David Browne retired from the Board and the Committee on 30 June 2018. Fiona MacLeod has been appointed as a member of the Committee with effect from 5 November 2018.

	Number of scheduled Committee meetings eligible to attend	Number of scheduled Committee meetings attended
Committee Chair		
Adrian Grace	6	6
Committee members		
David Bennett	6	5
Jim Pettigrew	6	5
Former Committee members		
David Browne	4	4

By invitation, other attendees will include: the Chief Executive Officer; the Group Human Resources Director; the Head of Reward and Pensions and the Group Chief Financial Officer, except when issues relating to their own remuneration are being discussed. PricewaterhouseCoopers LLP (PwC) the Committee's independent remuneration adviser also attend meetings where invited. The Company Secretary attends meetings to record minutes.

In addition, representatives from the Risk Committee may attend where appropriate to provide the Remuneration Committee with detailed risk assessments.

Committee role and responsibilities

During the year, the Committee revised its Charter which sets out the role and responsibilities of the Committee. The Charter of the Committee can be found on the Company's website www.cybg.com/about-us/corporate-governance/

Committee performance evaluation

During the year the Committee made progress on key findings of the in-depth Board performance evaluation carried out in 2017 which included an assessment of the Committee's effectiveness.

The Committee has adopted a continuous improvement approach to its performance evaluation and considers at the end of each meeting the effectiveness of the meeting and the quality of the reports that were presented.

Matters considered and actions taken by the Committee

The significant matters addressed by the Committee during the financial year ended 30 September 2018 and in evaluating the 2018 Annual Report and Accounts are described below:

Fixed and variable pay issues	2018 short and 2017 long-term incentive arrangements	Considered and approved discretionary incentives, performance measures and structures for delivery
	2018 total remuneration outcomes	Approved variable remuneration awards for Executive Directors, other senior management, MRT and all colleagues for 2018 financial year. Approved the release of deferred bonus awards. Approved forfeiture of bonus for the COO upon stepping down from the Board.
	All colleague 2017 and 2018 pay mandate and Executive Directors' Pay	Considered all colleague pay and executive pay arrangements. Recommended change to COO's base salary.
	Chairman's fee	Considered external market insight and recommended change.
	MRT termination and commencement awards	Considered all commencement awards and termination payments made during 2018, including that of the COO. Delegated authority to approve awards and release payments below a *de minimis* level to Group Human Resources Director and CEO.
	Non-regulatory bonus deferral	Removal of the requirement for non-MRT and MRT below the *de minimis* threshold to defer bonus.
Governance, risk and other matters	MRTs	Reviewed and approved changes and confirmed MRT population throughout the year.
	Regulatory developments	Considered regulatory remuneration requirements and approved compliance review.
	Implementation of the Remuneration policy	Approved the implementation of the Policy for 2019.
	2018 risk adjustments	Approved the Group's approach to risk and control adjustments for incentive arrangements and periodic review thereof.
	2018 performance assessment (CEO, CFO, COO & LT)	Reviewed Executive Director and Executive Leadership Team individual scorecards.
	Scheme rules and terms of the DEP & LTIP	Approved the terms of the DEP and LTIP plans for 2017 and 2018.
	Annual remuneration disclosures	Approved the submission of the remuneration policy statement to the PRA and FCA. Approved the 2017 Directors' remuneration report including Pillar 3 requirements.
	Investors and regulator feedback	Considered investor feedback and AGM outcomes and any impact on future structure of Executive Directors' remuneration.
	Pension arrangements	Considered retirement arrangements for members of the Leadership Team and other colleagues impacted by the pension Life Time Allowance/Annual Allowance.

Governance

Directors’ remuneration report

Annual report on remuneration continued

Advisers to the Committee

Following a selection process carried out by the Remuneration Committee prior to the IPO of the Group, the Committee engaged the services of PwC as independent remuneration adviser. During the financial year, PwC advised the Committee on all aspects of the Directors’ remuneration policy for members of the Executive Leadership Team. PwC also provide professional services in the ordinary course of business including assurance, advisory, tax and legal advice. The Committee is notified of other remuneration work that is undertaken by PwC. In addition, there are processes in place to ensure no conflict of interest exists in the provisions of these services.

PwC is a member of the Remuneration Consultants Group, whose voluntary code of conduct is designed to ensure objective and independent advice is given to remuneration committees. Fees of £198,000 excluding VAT (2017: £139,000) were paid based on the time spent on advice provided to the Remuneration Committee in respect of Directors’ remuneration for the financial year. The increase in fees in 2018 reflects additional time spent as a result of activity related to the acquisition of Virgin Money.

Statement of voting at general meeting

The proposals in relation to the Group’s remuneration policy, which were effective during 2018, were detailed within the Directors’ remuneration report for 2016 and were approved at the AGM on 31 January 2017.

The implementation of remuneration policy and the remuneration offered to Executive Directors for 2018 were detailed in the 2017 Directors’ remuneration report and were approved at the AGM on 31 January 2018. The shareholder votes submitted at the meeting, either directly, by mail or by proxy, were as follows:

	Votes for		Votes against		Votes withheld
	Number of shares	% of votes	Number of shares	% of votes	Number of shares
Directors’ Remuneration Policy (2017 AGM)	594,488,715	99.23%	4,592,820	0.77%	1,524,064
Directors’ Remuneration Report (2018 AGM)	605,457,056	98.88%	6,862,295	1.12%	552,298

Changes to the Board – Group Chief Operating Officer’s remuneration arrangements on departure

Debbie Crosbie stepped down from the Board with effect from 19 November 2018 and after a handover period will be placed on gardening leave until her employment with the Company ceases on a date to be agreed. In line with her contractual arrangements and the circumstances of her termination, she will not receive any compensation for loss of office.

From her departure date she will be paid in lieu of notice for the balance of her 12-month notice period until 18 November 2019 (or such earlier dates as may be agreed). She will receive her salary, car cash allowance, cash in lieu of pension and benefit funding as detailed on page 99, including her increase effective 1 October 2018, up to her departure date. Service contracts for Executive Directors include express provisions for the use of monthly phased payments, with a requirement for the departing Executive Director to seek to mitigate any loss and a reduction in amounts paid if they obtain alternative paid employment. No other remuneration payments will be made in connection with her departure.

In accordance with the rules of the 2018 Bonus Plan and the 2018 Long Term Incentive Plan, she will forfeit her bonus and she will not receive an LTIP award for the performance year 2018. In addition, as per the rules of the CYBG DEP and CYBG LTIP, approved by shareholders at the 2017 AGM, Debbie’s outstanding 2017 deferred bonus, 2015 Demerger Award, 2016 LTIP and 2017 LTIP will lapse on her departure from the Company.

Her right to receive an award in relation to the legacy 2013 and 2014 NAB Executive Long Term Incentives Performance Rights Grant, detailed on page 91, will be determined by the NAB Board in accordance with the plan rules and any remuneration she may receive will be detailed in next year’s Directors’ remuneration report (2019) alongside her single total figure of remuneration for the year ending 30 September 2019.

Implementation of the policy in 2019

At a glance – Executive Directors' remuneration structure in 2019 summary

For the 2019 performance year the annual incentive award (bonus) will be up to 118% of salary for the CEO and 117% for the CFO. Executive Directors will also be eligible to receive a LTIP award of up to 177% (CEO) and 176% (CFO) of salary in respect of the 2018 performance year. The COO will not be entitled to either award as her employment will terminate before the performance year end. The level of LTIP vesting will be based on performance measured over financial years 2019, 2020 and 2021 (the period 1 October 2018 to 30 September 2021). In combination, bonus and LTIP will not exceed the regulatory ratio between variable to fixed pay, when discounted using the EBA Discount Factor.

2019 2020 2021 2022 2023 2024 2025 2026 2027	Implementation for 2019
Base salary	David Duffy – £1,020,000 (2% increase aligned with all colleagues). Ian Smith – £510,000 (2% increase aligned with all colleagues). Debbie Crosbie – £475,000 (5.6% increase from 2018).
Benefits and allowances	Benefits and allowances include: pension, car, medical cover and life assurance arrangements David Duffy – £216,351. Ian Smith – £105,420. Debbie Crosbie – £93,737.
FY19 Annual incentive (bonus) Performance period (2019); Awarded (50% in shares 50% cash) (2020); Vesting (2023); Potential share deferral and phased release (2024–2027)	Maximum 118% (CEO) and 117% (CFO) of salary and linked to the delivery of 2019 business strategy. At least 50% delivered in shares. Delivered in December 2019. Part of the bonus may be deferred to ensure that, in combination with the LTIP award, regulatory requirements for deferral are met.
FY18 LTIP Awarded (2020); Performance period (2020–2022); Vesting (2023); Deferral and phased release (2024–2027) Award subject to 12-month holding period in line with regulatory requirements.	Maximum 177% (CEO) and 176% (CFO) of salary and linked to the delivery of business strategy over the financial years 2019 to 2021. It is expected that awards will be granted in December 2019. Award deferred for a total of seven years, with vesting in equal tranches over years three to seven with one year additional holding requirement.

The following sets out how the Directors' remuneration policy will be applied in 2019. The remuneration policy will be operated as set out above. In particular:

- a salary change for the COO is intended from 1 October 2018 and was approved prior to her resignation. This will be paid until her departure;
- the 2019 annual bonus and the 2018 LTIP opportunities for Executive Directors for the financial year 2019 increase as we evolve aspects of the way we implement our approved Policy this year. The differences in quantum for each Executive Director can be attributed to the different proportion of their fixed pay (salary plus pension and car allowances) used to calculate the regulatory cap;
- for the purpose of calculating the ratio between the variable and fixed components of remuneration for Executive Directors we will use the European Banking Authority's (EBA) Discount Factor;
- Non-Executive Directors' fees for 2019 have been reviewed and will increase for the first time since 2016. This reflects the changes in the nature of a Non-Executive Director's role and responsibilities as a result of the acquisition of Virgin Money; and
- dividends will not accrue on deferred bonus and LTIP awards made in relation to FY2019. The number of deferred bonus shares/LTIP awards granted may be based on a share price discounted by reference to the expected dividend yield over the vesting period.

Governance

Directors' remuneration report

Annual report on remuneration continued

FY2019 annual bonus

Opportunity	118% (CEO) and 117% (CFO) of salary (2017: 100% of base salary). In line with policy 80% of the award will be based on the performance of the Group against key financial and non-financial measures and 20% will be based on personal performance and behaviours.
Performance measures and targets	The Committee has yet to determine the final measures, weightings and targets for 2019 plan. The timing of the acquisition presents several additional considerations when it comes to the application of our Policy for 2019 and the development of our variable pay arrangements for the coming year. We intend to maintain the general technical design of our Bonus again this year but are not in a position to confirm the quantitative metrics, and weightings of the plan at this time and until we are able to integrate both the financial and non-financial performance indicators for the combined Group. We expect that the metrics will remain largely the same as in previous years and that we will maintain a similar mix of financial and non-financial items aligned with our strategic priorities. We will take the same approach to calibration and set stretching targets aligned with our new medium-term performance targets once these are finalised and communicated to the market. The Committee will provide the targets alongside the level of payout relative to the performance achieved in next year's Directors' remuneration report.

FY2018 long-term incentives

Opportunity	LTIP awards will be granted over shares worth 177% (CEO) and 176% (CFO) of salary (2017: 100% of salary).
Performance measures and targets	The Committee has yet to determine the final measures, weightings and targets for 2018 plan. As per the annual bonus plan the timing of the acquisition means that until we are able to integrate both the financial and non-financial performance indicators for the combined Group we will not be in a position to confirm the quantitative metrics, weightings and targets of the plan. We expect that our approach to LTIP will continue to be based on a balanced scorecard approach that will include the same metrics as we currently have in the four areas of sustainable customer growth, efficiency, risk and compliance and customer focused culture. We will replace the IRB metric from the 2017 plan as IRB Accreditation was achieved in 2018. Again we will take the same approach to calibration and set stretching targets aligned with our new medium-term performance targets once these are finalised and communicated to the market. We will provide a robust set of metrics and targets on a combined Group basis and we commit to consulting with our investors on these measures in the early part of 2019. We intend to make the award as normal in December, as we believe that the current framework continues to provide high levels of alignment between the interests of our Executive Leadership Team and investors and continues to act as a significant reward and retention tool for our Executive Directors.
Vesting terms	The performance period will be the three years commencing 1 October 2018. An assessment of individual performance in the financial year preceding the date of the grant will be taken into account before awards are made. We anticipate that we will make the grant in November 2019. To the extent that the performance conditions are met, awards will release from the third anniversary of the date of grant and are released annually in equal tranches to the seventh such anniversary. At each release date the resultant number of shares (post taxation) will be subject to a further 12 month regulatory retention period.

Outcomes for 2018

Executive Directors – single total figure of remuneration (audited)

The table below sets out the single total figure of remuneration and breakdown for each Executive Director in respect of the financial year to 30 September 2018.

	David Duffy		Ian Smith		Debbie Crosbie	
£000s	2018	2017	2018	2017	2018	2017
Salary	**1,000**	1,000	**500**	460	**450**	450
Benefits and allowances	**32**	56	**9**	11	**8**	10
Pension and pension allowance(1)	**180**	180	**94**	87	**81**	100
Total fixed remuneration	**1,212**	1,236	**603**	558	**539**	560
Annual bonus (2)	**620**	820	**310**	377	**–**	369
LTIP vesting in year (3)	**–**	–	**–**	–	**–**	–
Other awards (4)	**1**	–	**1**	–	**1**	–
Total remuneration	**1,833**	2,056	**914**	935	**540**	929

(1) David Duffy, Ian Smith and Debbie Crosbie opted out of the Group's defined contribution pension scheme and receive a cash allowance in lieu of the Group's pension contributions for 2018.
(2) Includes the cash, upfront retained and deferred bonus elements.
(3) No CYBG PLC LTIP awards or legacy NAB LTIP awards vested during 2017 or 2018.
(4) Each of the Executive Directors also received £500 of free shares in November 2017. Debbie Crosbie's free shares will lapse upon her termination date.

Former Executive Directors and payments to past Directors (audited)

No Executive Directors left during the year.

Executive Director's payments for loss of office (audited)

No payments were made during this or the previous year.

Total pension entitlements (audited)

David Duffy, Ian Smith and Debbie Crosbie have each opted out of the Group's defined contribution pension plans and receive cash allowances in lieu of pension contributions. Debbie Crosbie participated in the Group's defined benefit scheme until 31 July 2017, when the plan was closed to future accrual.

Details of the pension accrued in the Group's defined benefit pension scheme by Debbie Crosbie in respect of qualifying services are shown below. The value of the pension is calculated using the HMRC method.

Values relating to DB Scheme	Accrued pension at year end £000	Normal Retirement Date	Additional value of pension on early retirement £000	Pension value in the year from the DB Scheme £000	Pension value in the year from cash allowance £000	Total £000
Debbie Crosbie	42	30 March 2035	–	–	81	81

Taxable benefits (audited)

– Executive Directors receive private medical cover, health assessment and life assurance.

– The CEO receives an annual car cash allowance of £30,000 and the other Executive Directors each receive an annual allowance of £6,840.

Governance

Directors' remuneration report

Annual report on remuneration continued

Annual bonus

The following annual bonus awards were made in respect of the 2018 financial year; these were agreed by the Committee having reviewed the Group's results. Details of the targets used to determine annual bonus in respect of the 2018 financial year and the extent to which they were satisfied are shown in the table below. These figures are used for determining part of the Group element of Executive Directors' bonus awards and are included in the single figure table on the previous page. No allowance was made for the acquisition of Virgin Money on determining the company performance element.

Executive Directors Underlying performance measures		Weighting	Threshold	Target	Stretch	Actual	Award as % salary[2] (audited)
Sustainable returns	Underlying PBT[1]	16.00%	£318m	£352m	£384m	£331m	**6%**
	Customer lending growth	13.34%	4.6%	5.6%	6.6%	4.7%	**5%**
	NPS	5.34%	14.0%	15.5%	17.0%	10.0%	**0%**
	Digital adoption	5.34%	41.5%	43.5%	45.5%	46.5%	**5%**
Efficiency	Total costs	8.00%	£650m	£640m	£630m	£635m	**6%**
	Underlying CIR	8.00%	62.0%	60.0%	58.0%	63.1%	**0%**
Capital optimisation	Underlying RoTE	16.00%	8.90%	9.25%	9.50%	10.6%	**16%**
Customer-focused culture	Colleague engagement	8.00%	72%	77%	82%	76%	**4%**
		80%					**42%**

(1) The underlying profit before tax (PBT) excludes exceptional items which have reduced the statutory PBT by £495m (a reconciliation of underlying profit before tax to statutory profit before tax is provided in the Financial results section). The reduction is largely driven by legacy conduct issues in respect of PPI. The underlying PBT was not adjusted by the incremental year on year change in the prudent valuation adjustment (PVA) figure for 2018. The PVA figure reduced by £0.7m year on year from £4m in 2017 to £3.3m in 2018. .

(2) Following the assessment by the Board's Risk Committee of *ex ante* and *ex post* risks the Remuneration Committee did not consider it necessary to make a risk adjustment to the arithmetic outcome of the award.

Personal Awards (20% weighting) David Duffy

- Under David's strong leadership CYBG has continued to focus on the strategy and transformation of the business delivering a strong underlying performance for 2018 underpinned by sustainable, above-market customer lending growth in both mortgages and SME. The majority of financial targets have been met with costs ahead of plan at £635m and the achievement of a double-digit Return on Tangible Equity. The Group's strong performance enabled the Board to recommend a significant year on year increase in the ordinary dividend, with CYBG now on the path to delivering a sustainable return on equity for shareholders.
- Our digital transformation has also continued at pace, with the new iB platform now being fully leveraged to improve the customer experience with c,2m retail customers migrated to the platform and SME customers in progress. It is Open Banking ready and delivering innovations in the marketplace that will stand out in the marketplace.
- The Group's execution of its strategy and consistent delivery against all the targets it has set has enabled the Group to undertake the acquisition of Virgin Money. The successful completion of the transaction with c.99% shareholder approval on both sides enables the Group to embark on its next phase of growth. This transaction, the UK's first major bank acquisition since the financial crisis, has also been executed while continuing to deliver the demanding organic strategy and targets.
- The Cultural transformation continues at pace underpinned by the Group's Values which are now deeply embedded in all aspects of the colleague life cycle. When compared to other organisations going through similar levels of transformation (Transitional Companies norm) our colleague engagement scores continue to outperform this norm on seven of the ten comparable categories and on questions measuring how we lead ourselves through change we exceed the norm significantly. Against a backdrop of ongoing, considerable change this is a significant achievement.
- Strength and depth of succession plans and leadership capability continue to be an area of focus and improvement. This has enabled ambitious inorganic growth and delivered the first major public bank acquisition since the financial crisis.
- The reputation of the Company has also been enhanced through David's appointment by the UK Government as Fintech Envoy for the north of England which aligns well to our ambition to support the Northern Powerhouse strategy.

2018 Final outcome: 20% out of a maximum 20%

Personal Awards (20% weighting) Ian Smith

- Ian has played a critical role in the delivery of the strategic and financial goals of the business. The business has delivered a strong performance with underlying profit growth of 13% in the year and cost savings ahead of guidance at £635m. In addition, following a further year of progress on the IRB project, a critical strategic milestone was achieved in October 2018, with the delivery of IRB Accreditation for the Group's Mortgage and SME portfolios.
- The strong underlying performance provided the capacity for the Board to recommend a significant year on year increase in the ordinary dividend (3.1p vs 1p in 2017), with CYBG now on the path to delivering a sustainable return on equity for shareholders.
- The financial delivery over the past few years has positioned the Group for its next phase of growth and enabled the acquisition of Virgin Money to be undertaken. The successful acquisition of Virgin Money, the UK's first major bank acquisition since the financial crisis, has also been executed while continuing to deliver a very busy BAU agenda.
- A critical strategic milestone has been achieved in the delivery of IRB Accreditation for both mortgages and SME.
- The financial control environment remains strong as attested to by both audit and external review.

2018 Final outcome: 20% out of a maximum 20%

Executive Director (audited)	Personal award % salary	Group award % salary	Total Award % salary	Total award
David Duffy	20%	42%	62%	£620,000
Ian Smith	20%	42%	62%	£310,000
Debbie Crosbie(1)	–	–	–	–

(1) In line with the rules of the CYBG bonus plan, Debbie will not receive a bonus this year.

In assessing the Group's performance, the Committee reviewed a report from the Chair of the Risk Committee on any risk issues within the business and determined that no adjustments were required to the individual bonus awards for Executive Directors.

Deferral of bonus (audited)

In line with regulatory requirements, a portion of the bonus award is subject to deferral to the extent to which the required deferral is not fully met by the LTIP award. Half of the upfront and deferred elements are also subject to a retention period. As such the Executive Directors' awards were made as follows.

	David Duffy	Ian Smith	Debbie Crosbie
Upfront cash	£310,000	£155,000	–
Upfront shares(2)	£310,000	£155,000	–
Deferred shares	–	–	–
Total	£620,000	£310,000	–

(2) Awarded as conditional rights to CYBG PLC shares which will be released at the end of the 12-month retention period.

Governance

Directors' remuneration report

Annual report on remuneration continued

LTIP awards

2018 LTIP

The following awards will be made to Executive Directors to reflect their performance in 2018 and align their interests with those of shareholders.

2018 LTIP award	Percentage of salary(1)	Face value of award	Type of interest awarded	End of performance period	Percentage receivable for threshold performance(2)	Percentage receivable for target performance(2)
David Duffy	177%	£1,770,000	Conditional rights to CYBG PLC shares	30 Sep 2021	TBC	TBC
Ian Smith	176%	£880,000				
Debbie Crosbie(3)	–	–				

(1) The award is based on a percentage of salary as at 30 September 2018 which takes account of the EBA discount factor.
(2) Vesting for threshold and target performance will be confirmed once metrics, relative weightings and targets are established.
(3) As Debbie Crosbie's employment will terminate she will not receive an award for 2018.

The award will vest based on the performance of the Group over the period 1 October 2018 to 30 September 2021 (2019 to 2021 financial years). As previously outlined on page 100 of this report, we expect that our approach to the design of the LTIP will continue to be based on a balanced scorecard approach that will include the same metrics as we currently have in the four areas of sustainable customer growth, efficiency, risk and compliance and customer focused culture. We will replace the IRB metric as that has been successfully delivered in 2018. We believe that this framework continues to provide high levels of alignment between the interests of our Leadership Team, customers and investors and continues to act as a significant reward and retention tool for our Executive Directors.

We will take the same approach to calibration and set stretching targets aligned with our new medium-term performance targets once these are finalised and communicated to the market. We will provide a robust set of metrics and targets on a combined Group basis and we commit to consulting with our investors on these measures in the early part of 2019.

Past LTIP awards

As a result of the recent acquisition of Virgin Money, the Committee has given consideration to the impact of this on the performance targets of the existing incentive awards (i.e. the LTIP awards granted in March 2017 and November 2017). However, due to the timing of the acquisition, it has not been possible to determine the extent to which the performance targets should be adjusted to take account of the Combined Group at this time.

At the point the Committee determines the LTIP metrics in respect of the 2018 LTIP, the Remuneration Committee will, at that stage, determine the extent to which any adjustments are necessary to the performance targets of the existing incentive awards. In determining any adjustments, the underlying principle will be that any revised targets are no more or less stretching than the original targets. The Committee is committed to consulting with investors at this time, with full disclosure of any adjustments being made in the 2019 Annual Report.

For information, the original measures and performance targets determined at the time of grant for each of the March 2017 and November 2017 LTIP awards have been detailed below.

2017 LTIP awards (audited)

2017 LTIP award	Percentage of salary(1)	Face value of award	Number of shares awarded(2)	Type of interest awarded	End of performance period	Percentage receivable for threshold performance(3)	Percentage receivable for target performance(4)
David Duffy	100%	£1,000,000	319,284	Conditional rights to CYBG PLC shares	30 Sep 2020	21%	67%
Ian Smith	100%	£460,000	146,871				
Debbie Crosbie	100%	£450,000	143,678				

(1) The award is based on a percentage of salary as at 30 September 2017.
(2) The award price of £3.132 was calculated based on the average middle-market share price over the three days before grant.
(3) 21% reflects nine of the measures vesting at 25% for threshold performance and two vesting at 0%.
(4) 67% reflects nine of the measures vesting at 60% for target performance and 20% vesting at 100% for target performance.

The award was granted in 24 November 2017 and will vest based on the performance over the 2018 to 2020 financial years as set out below.

Underlying performance measures		Weighting	Threshold	Target	Stretch
Sustainable customer growth	Retail NPS	8.33%	21	24	27
	Customer lending growth	8.33%	4.0%	5.0%	6.0%
	Digital adoption	8.33%	50.0%	52.5%	55.0%
Efficiency	CIR(2)	20.0%	58.0%	55.0%	52.0%
	RoTE(2)(3)(5)	20.0%	10.0%	11.0%	12.0%
	IRB accreditation(1)	10.0%		Achieved	
Risk and compliance	Bad and doubtful debt/average loans(1)	6.67%		<30bps	
	Cumulative operational risk losses(4)	6.67%	<£30m	<£25m	<£20m
	Complaints per 1,000	6.67%	3.7	3.5	3.3
Customer-focused culture	Colleague engagement	2.5%	72	77	82
	Senior leadership diversity	2.5%	38%	40%	42%

(1) IRB accreditation (based on the full roll out) and bad and doubtful debt/average loans are all or nothing measures with 100% vesting if achieved for these elements.
(2) CIR and RoTE are targeted on an underlying basis.
(3) Three-year average.
(4) Cumulative figure for 2018, 2019 and 2020.
(5) CET1 ratio has been removed as a measure for 2018, but will underpin RoTE. CET1 must achieve >12% before the RoTE element is assessed.

In line with regulatory changes to deferral periods the LTIP awards to Executive Directors will be released over three to seven years from the date of grant, with each release subject to a further holding period.

2016 LTIP awards (audited)

2016 LTIP award	Percentage of salary(1)	Face value of award	Number of shares awarded(2)	Type of interest awarded	End of performance period	Percentage receivable for threshold performance(3)	Percentage receivable for target performance(4)
David Duffy	100%	£1,000,000	375,897	Conditional rights to CYBG PLC shares	30 Sep 2019	20%	68%
Ian Smith	100%	£460,000	172,912				
Debbie Crosbie	100%	£450,000	169,153				

(1) The award is based on a percentage of salary as at 30 September 2016.
(2) The award price of £2.6603 was calculated based on the average middle-market share price over the three days before grant.
(3) 20% reflects 80% of the measures vesting at 25% for threshold performance and 20% vesting at 0%.
(4) 68% reflects 80% of the measures vesting at 60% for target performance and 20% vesting at 100% for target performance.

The award was granted in 9 March 2017 and will vest based on the performance over the 2017 to 2019 financial years as set out below.

Performance over the period will be assessed against the following measures:

2016 LTIP measures		Weighting	Threshold	Target	Maximum
Sustainable customer Growth	Clydesdale and Yorkshire Bank NPS	10%	22.5%	25.0%	27.5%
	Digital adoption	10%	45.0%	50.0%	55.0%
Efficiency	CIR(2)	25%	60.0%	57.5%	55.0%
Capital optimisation	CET1 ratio(1)(2)	10%		>12%	
	RoTE(2)	30%	8.0%	9.0%	10%
	IRB accreditation for mortgage book(1)	5%		Achieved	
Prudent risk management and governance	Bad and doubtful debt/average loans(1)(3)	5%		<25bps%	
	Cumulative operational risk losses(4)	5%	<£25m	<£20m	<£15m

(1) CET1 ratio, IRB accreditation for mortgage book and bad and doubtful debt/average loans are all or nothing measures with 100% vesting if achieved for these elements.
(2) CIR and RoTE are targeted on an underlying basis.
(3) Three-year average.
(4) Cumulative figure for 2017, 2018 and 2019.

Governance

Directors' remuneration report

Annual report on remuneration continued

2015 demerger LTIP award (audited)

Following the demerger from NAB an award was made to recognise the Executive Directors' contribution to the success of the demerger, with performance measured against a cumulative underlying PBT target over 2016 to 2018. Details of the underlying PBT targets will be disclosed alongside details of the value at vesting in the 2019 Directors' remuneration report. The PBT outcome will be adjusted by the incremental year on year change in the prudent valuation adjustment figure during this period.

2015 demerger LTIP	Percentage of salary[1]	Face value of award	Number of shares awarded[2]	Type of interest awarded	End of performance period[3]	Percentage receivable for threshold performance	Percentage receivable for target performance
David Duffy	150%	£1,500,000	768,560	Conditional rights to CYBG PLC shares	30 Sep 2018	0%	100%
Ian Smith	100%	£450,000	230,568				
Debbie Crosbie	100%	£450,000	230,568				

(1) The award was based on a multiple of salary as at 30 September 2015.
(2) The award price of £1.9517 was calculated based on the average middle-market share price over the three days before grant.
(3) Awards will vest in February 2019. The final decision on the level of vesting will be taken by the CYBG Board, with value at the date of vesting included in the Directors' single table figure in the year they vest.

Non-Executive Directors (audited)

The table below sets out the single total figure of remuneration and breakdown for each Non-Executive Director for the year ending 30 September 2018.

	Fees		Benefits		Total	
	2018 £000	2017 £000	**2018 £000**	2017 £000	**2018 £000**	2017 £000
Clive Adamson	**110**	104	**–**	–	**110**	104
David Bennett	**195**	190	**–**	–	**195**	190
Paul Coby	**80**	78	**–**	–	**80**	78
Adrian Grace	**100**	100	**–**	–	**100**	100
Fiona MacLeod	**85**	81	**–**	–	**85**	81
Jim Pettigrew	**365**	365	**–**	–	**365**	365
Dr Teresa Robson-Capps	**80**	80	**–**	–	**80**	80
Tim Wade	**110**	107	**–**	–	**110**	107
David Browne[1]	**75**	100	**–**	–	**75**	100
Richard Gregory[2]	**–**	45	**–**	–	**-**	45
Total	**1,200**	1,250	**–**	–	**1,200**	1,250

(1) David Browne retired from the Board on 30 June 2018.
(2) Richard Gregory retired from the Board on 10 January 2017.

Non-Executive Directors' annual fees

The following fees are payable to Non-Executive Directors for the year ending 30 September 2019 in line with the rates approved by the CYBG Board in October 2018. The Non-Executive Directors are reimbursed for expenses they incur in performing their duties. Any tax arising on such reimbursed expenses is borne by the Group.

	CYBG 2019	**CYBG 2018**
Chairman[1]	£375,000	£350,000
Non-Executive Director	£75,000	£70,000
Deputy Chairman	£60,000	£60,000
Senior Independent Director	£30,000	£30,000
Chair Audit Committee	£35,000	£30,000
Chair Risk Committee	£35,000	£30,000
Chair Remuneration Committee	£35,000	£30,000
Member Audit Committee	£15,000	£10,000
Member Risk Committee	£15,000	£10,000
Member Remuneration Committee	£15,000	£10,000
Chair Governance and Nomination Committee	£35,000	£5,000
Member Governance and Nomination Committee	£15,000	£5,000

(1) Paid as a combined fee for the role as Chairman and Chair of the Governance and Nomination Committee.

CYBG Non-Executive Directors' fees were set in November 2015 in preparation for and payable from listing of CYBG in February 2016 and whilst they have been reviewed annually they have not changed. From 15 October 2018, being the point the Scheme of Arrangement in relation to CYBG's offer for Virgin Money became effective, the CYBG Non-Executive Directors have been appointed Non-Executive Directors of Virgin Money plc. There are additional Virgin Money plc Board Committee roles for some Non-Executive Directors. To recognise the additional responsibilities and time commitment required from Non-Executive Directors in relation to Virgin Money plc, Non-Executive Directors will be paid an additional fee for a transitional period. The following fees are payable to Non-Executive Directors in relation to Virgin Money plc roles for the year ending 30 September 2019 in line with the rates approved by the Board in October 2018.

	2019
Chairman	£20,000
Non-Executive Director	£10,000
Chair Audit Committee	£25,000
Chair Risk Committee	£25,000
Member Audit Committee	£10,000
Member Risk Committee	£10,000

Former Non-Executive Directors and payments to past Non-Executive Directors (audited)

Richard Gregory retired from the Board on 10 January 2017. David Browne retired from the Board on 30 June 2018. No additional fees were paid to either Director by the Group for their services to the Group upon termination.

Non-Executive Directors' payments for loss of office (audited)

No payments were made during the current or previous year.

Statement of Directors' shareholding and share interests (audited)

Executive Directors are required to build up a holding of the Group's shares to the value of 150% of base salary (200% for the CEO). To support this, Executive Directors are required to retain 60% of the net shares received from variable pay awards after the payment of tax and National Insurance until the shareholding requirement is met.

Detailed below are the beneficial holdings of ordinary shares as at 30 September 2018 for each Executive Director, together with details of their vested and unvested awards under the CYBG PLC share plans.

Director	Ordinary shares(1)(2)	Vested awards(3)	Unvested DEP awards(4)(6)	Vested LTIP awards	Unvested LTIP awards(5)(6)	Maximum total shares and awards	Expected value net of tax(7) £000
David Duffy	213,438	168,975	849,019	–	695,181	1,757,638	3,341
Ian Smith	138,158	–	267,541	–	319,783	725,482	1,455
Debbie Crosbie	140,771	–	266,774	–	312,831	720,376	1,450

(1) Ordinary shares beneficially owned, vested awards during the year and holdings of connected persons. This includes shares held via the CYBG plc SIP – David Duffy (415), Ian Smith (1,306 including 526 shares purchased through the partnership scheme during the year ending 30 September 2018) and Debbie Crosbie (415). Since the year ending 30 September 2018 Ian Smith purchased 47 partnership shares on 1 October 2018 and 54 Partnership shares on 1 November 2018. At the date of the Report he held at total of 1,407 shares in the CYBG PLC SIP.

(2) Includes CHESS Depositary Interests (CDIs) which represent interests in ordinary shares beneficially owned by David Duffy (4,080) and Ian Smith (4,502). Values are based on 30 September 2018 closing price of AUS$27.810 (1499.17p) and the average exchange rate on the day (AUS$:GBP 0.5532).

(3) Gross number of conditional rights awards which have vested (net shares from this award are included in ordinary shares total).

(4) Includes the 2015 Demerger LTIP (awarded under the DEP) and 2017 Deferred Bonus. Unvested bonus awards are subject to continued employment with no business performance conditions. The 2015 Demerger LTIP is subject to business performance conditions and continued employment.

(5) Includes the 2016 LTIP and 2017 LTIP awards. These are subject to continued employment and the achievement of business performance conditions.

(6) The unvested 2015 demerger LTIP (awarded under the DEP), 2016 LTIP and 2017 LTIP awards have been included at 100% of their face value in line with current accounting assumptions. Values are based on 30 September 2018 closing price of 323.8p.

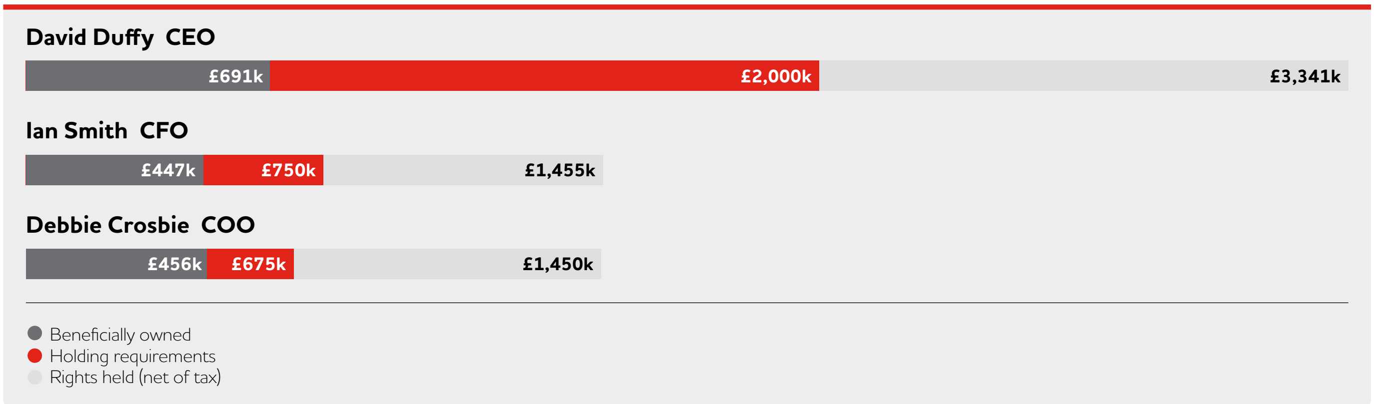
(7) Assumes 47% is deducted from unvested rights to reflect the tax and National Insurance due on the release of shares.

Governance

Directors' remuneration report

Annual report on remuneration continued

The chart below shows the Executive Directors' current shareholdings and net number of shares they would receive if all the unreleased rights (vested and unvested) shown above vested in full against their shareholding requirements applicable for Executive Directors:



For the purpose of assessing the Executive Directors' holdings against the shareholding requirements at 30 September 2018 unvested awards are excluded.

Director	Base salary	Requirement as % of base salary	Shares and vested rights(1)	Face value(2)	Shareholding requirement met?
David Duffy	£1,000,000	200%	213,438	£691,112	No
Ian Smith	£500,000	150%	138,070	£447,071	No
Debbie Crosbie	£450,000	150%	140,771	£455,816	No

(1) Includes vested awards over CYBG PLC shares which have not yet been released.
(2) Values are based on 30 September 2018 closing price of 3.238p.

One Executive Director (Ian Smith) purchases shares via the SIP and currently purchases £150 worth of shares per month.

Non-Executive Directors' shareholding (audited)

The beneficial interests of the Non-Executive Directors and their connected persons who held office at 30 September 2018 in the shares of the Group and as at 30 September 2017 are shown below:

Non-Executive Directors	Ordinary shares beneficially owned at 30 September 2018 or date of appointment if later	Ordinary shares beneficially owned at 30 September 2017 (or date of cessation if earlier)
Clive Adamson	–	–
David Bennett	16,386	16,334
Paul Coby	–	–
Adrian Grace	16,220	16,220
Fiona MacLeod	7,000	7,000
Jim Pettigrew	50,000	50,000
Dr Teresa Robson-Capps	–	–
Tim Wade	20,000	–

None of the Non-Executive Directors holds any awards under the CYBG PLC share plans (2017: none).

One Non-Executive Director (Tim Wade) bought shares on 22 November 2017. David Bennett had an automatic reinvestment of dividends of 52 shares on 21 February 2018.

One Non-Executive Director (Jim Pettigrew) bought 50,000 shares (22 November 2018) between 30 September 2018 and the date of this report. None of the other Non-Executive Directors, or their connected persons, bought or sold shares between 30 September 2018 and the date of this report.

Executive Directors' shareholdings under each of the Group's share plans

The Group operates four share plans which were approved prior to the demerger, being:

- Deferred Equity Plan (DEP);
- Long Term Incentive Plan (LTIP);
- Share Incentive Plan (SIP); and
- Save As You Earn Plan (SAYE).

As CYBG is no longer part of the NAB Group, no details of outstanding NAB awards are included within this section.

DEP and LTIP

Awards were made to Executive Directors under the DEP and LTIP.

DEP and LTIP awards	Start of year	Awarded during the year	Vested during the year(1)	Lapsed during the year	Unvested at year end(2)	Date of grant	Grant price(3)	Market value at date of grant(3) £000	Notes
David Duffy	768,560	–	–	–	768,560	11 Feb 16	195.17	1,500	2015 Demerger LTIP
	78,299	–	78,299	–	–	09 Mar 17	266.03	–	2016 Deferred Bonus
	–	171,135	90,676	–	80,459	24 Nov 17	313.2	536	2017 Deferred Bonus
	375,897	–	–	–	375,897	09 Mar 17	266.03	1,000	2016 LTIP
	–	319,284	–	–	319,284	24 Nov 17	313.2	1,000	2017 LTIP
Ian Smith	230,568	–	–	–	230,568	11 Feb 16	195.17	450	2015 Demerger LTIP
	36,086	–	36,086	–	–	09 Mar 17	266.03	–	2016 Deferred Bonus
	–	78,671	41,698	–	36,973	24 Nov 17	313.2	246	2017 Deferred Bonus
	172,912	–	–	–	172,912	09 Mar 17	266.03	460	2016 LTIP
	–	146,871	–	–	146,871	24 Nov 17	313.2	460	2017 LTIP
Debbie Crosbie	230,568	–	–	–	230,568	11 Feb 16	195.17	450	2015 Demerger LTIP
	35,296	–	35,296	–	–	09 Mar 17	266.03	–	2016 Deferred Bonus
	–	77,010	40,804	–	36,206	24 Nov 17	313.2	241	2017 Deferred Bonus
	169,153	–	–	–	169,153	09 Mar 17	266.03	450	2016 LTIP
	–	143,678	–	–	143,678	24 Nov 17	313.2	450	2017 LTIP

(1) The 2017 upfront retained bonus award vested on 24 November 2017 when granted.
(2) The 2015 Demerger LTIP (awarded under the DEP) is due to vest in 2019.
(3) The value of awards granted under the DEP and LTIP were based on the three-day mid-market closing price over the preceding three days.

LTIP

An award was made on 24 November 2017 in relation to the 2017 LTIP.

SIP

An award of 159 shares was made on 24 November 2018 to each of the Executive Directors through the SIP. One Executive Director (Ian Smith) currently participates in the monthly purchase of shares through the SIP.

SAYE

No offers under the CYBG PLC SAYE plan have been made (2017: none).

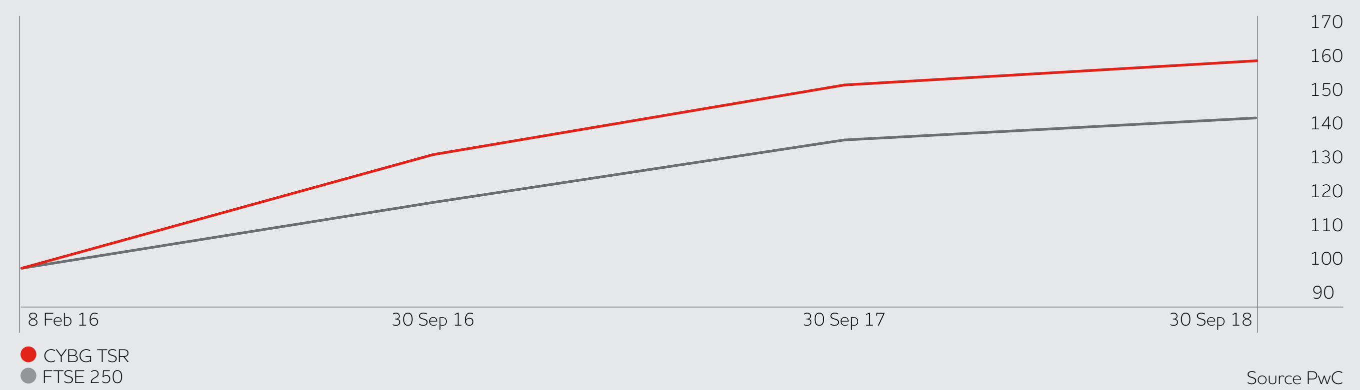
Governance

Directors' remuneration report

Annual report on remuneration continued

Total Shareholder Return (TSR) performance

The graph below shows the value of £100 invested in the Group's shares since listing, compared with the total returns of the FTSE 250 Index. The graph shows the TSR generated by both the movement in share value and the reinvestment over the same period of dividend income. The Committee considers the FTSE 250 as representative of the current market capitalisation of the Group.



CEO historic remuneration

The table below sets out the total remuneration delivered to the Chief Executive Officer over 2018:

Chief Executive Officer	2018	2017
Total single figure (£000)	**1,833**	2,056
Annual short-term incentive payment level achieved (% of maximum opportunity)	**62%**	82%
Long-term incentive vesting level achieved (% of maximum opportunity)(1)	**–**	–

(1) No CYBG LTIP awards vested during 2016, 2017 or 2018.

Relative importance of spend on pay

The table below sets out the relative importance of spend on pay in the 2018 financial year:

Overall spend	Disbursements from profit in 2018 financial year £m	Disbursements from profit in 2017 financial year £m
Dividend(1)	**44**	9
Overall spend on pay including Executive Directors(2)	**223**	166

(1) The Directors have recommended a final dividend in respect of the year ended 30 September 2018 of 3.1p per ordinary share in the Company (2017: 1p) to be paid subject to approval of shareholders at the 2018 Annual General Meeting.
(2) 2017 and 2018 figures as per note 2.4 of the consolidated financial statements.

Change in the CEO's remuneration compared with colleagues

The table below shows the percentage change in remuneration for the CEO between 2017 and 2018 compared with the percentage change in the average remuneration of colleagues.

Remuneration compared with colleagues	Salary 2017 to 2018	Benefits(3) 2017 to 2018	Bonus 2017 to 2018
CEO(1)	0%	-43%	-24%
Colleagues(2)	1.7%	5%	-16%

(1) Reflects annual salary at 30 September and average for respective years.
(2) Reflects average annual FTE salary of colleagues employed at both 30 September 2017 and 30 September 2018 and average bonus awards for 2017 and 2018.
(3) Taxable benefits and other allowances excluding employer pension contributions.

Other remuneration disclosures

Our remuneration policy for all colleagues
The Group has implemented a firm-wide remuneration policy that is designed to attract and retain high-calibre individuals who will promote the delivery of our long-term strategy in line with our business, values and risk appetite. While the levels and elements of the remuneration may differ from that of the Executive Directors, they are based on the same principles, aligning remuneration, which shall not be excessive, and ensuring that variable pay is appropriate, balanced and calibrated for any impact of risk.

Element	Objective	Operation
Base salary	Recruit, reward, retain and recognise scope of role.	Base salaries are reviewed annually and reflect Group and individual performance, skills, experience and the scope of the role.
Benefits	To provide benefits consistent with role.	The Group provides access to a range of benefits which may vary according to seniority.
Pension	To provide benefits consistent with role.	The Group operates a defined contribution pension scheme for all colleagues. The defined benefit scheme closed to new entrants in 2004, with the Scheme closing to future accrual on 31 July 2017 for the majority of colleagues. For members of the Leadership Team who are affected by the Annual and Lifetime Allowances for pension saving, the Bank introduced two options in addition to participation in the defined contribution pension scheme under the standard terms. The two options are a cash allowance in lieu of pension contributions from the Bank or a combination of pension contributions and cash of an equivalent value.
Bonus	The annual bonus is designed to reward Group and personal performance in line with strategic objectives.	The Group has a single firm-wide short-term incentive plan. This is discretionary and is based on Group performance. For certain more senior colleagues and leadership team members below Executive Director level individual performance within the year is also a factor. The determination of measures and their weighting are set annually and awards are determined by the Remuneration Committee at the end of the financial year.
LTIP	Delivery of the Group's strategy and growth in shareholder value.	In line with Executive Directors, the Group's Executive Leadership Team is able to influence the Group's performance and they are incentivised to do so through eligibility to equity-based compensation. Awards are based on a three-year performance period reflecting a basket of business and shareholder measures aligned with strategic goals. Awards will vest a minimum of three years after being awarded, or longer where required by the PRA Remuneration Code. Awards may be subject to a discount in determining total variable remuneration under the rules set by the PRA and European Banking Authority.
Other share plans	Offers opportunity to acquire shares in CYBG.	As well as the DEP and LTIP, the Group operates: – a SIP under which colleagues may purchase Partnership Shares and the Group may offer free shares; and – the Group may in the future offer a SAYE plan.
Commencement, retention and guaranteed awards	Buy-out of unvested equity from a previous employer.	The amount, timing and performance hurdles are based on those being forfeited and satisfactory evidence. Guaranteed incentives or bonus are not provided to existing colleagues.

Directors' remuneration report

Other remuneration disclosures continued

Total reward consists of both fixed and variable components:

- fixed remuneration provided as cash and benefits (including employer pension); and
- variable remuneration reflects both individual and business performance.

The mix of fixed and variable reward is balanced to ensure that fixed remuneration provides a sufficient level of remuneration so that the variable reward components can be fully flexible, including the possibility of paying no variable reward. The remuneration mix at target is based on market information and practices. In any year, the actual mix may vary from target, given the overlay of business performance and individual performance where applicable.

All variable pay awards to MRTs are subject to malus and clawback in line with regulatory requirements.

Control functions

Colleagues engaged in control functions (i.e. Risk, Internal Audit and Compliance colleagues) are critical to effective management of risk across the Group. Independence from the business for these colleagues is assured through:

- setting the reward mix so that variable reward is not significant enough to encourage inappropriate behaviours, while remaining competitive with the external market; and
- scorecards which are specific to the function.

The Committee reviews remuneration structures for control function colleagues.

Risk adjustment

In addition to the Committee's review of *ex ante* and *ex post* risks that impact on the level of the bonus pool and the application of malus and clawback as outlined above, individual bonus awards are also subject to meeting all compliance requirements and awards made can be reduced to nil where these are not met, or where colleagues are subject to disciplinary sanction.

Deferral arrangements

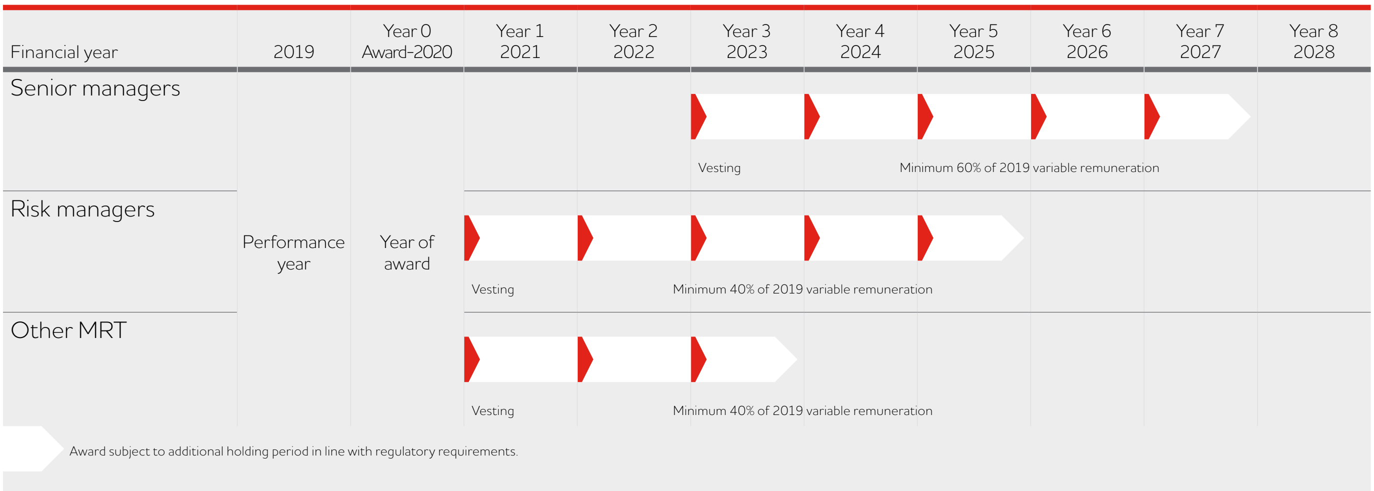
Variable rewards (bonus, LTIP and retention awards) are subject to deferral and retention for all MRTs in line with UK regulation:

- at least 60% of total variable reward will be deferred where the total variable reward is £500,000 or more; and
- at least 40% of total variable reward will be deferred where the MRT does not meet *de minimus* conditions.

The period of deferral ranges from one to three years to three to seven years depending on role in line with UK legislation.

The tables below set out the deferral arrangements for those roles classed as MRTs under Articles 2, 3 and 4 of the European Banking Authority Guidelines. These have been grouped under the three classifications within Strengthening Individual Accountability in Banking:

- Senior Manager Function (SMF) roles under the Senior Manager Regime. This includes Executive Directors, SMF Non-Executive Directors (Chairman, Senior Independent Non-Executive Director and the Chairman of Remuneration, Risk, Audit and Nomination Committees) and other SMF leadership team members and senior managers;
- Risk Manager roles which includes (but not exclusively) Leadership Team members not classified as SMF, the senior management responsible for material business units, for management of specific risk categories such as liquidity, operational or interest rate risk, and for control functions who are responsible for the day-to-day management of the business, its risks, or its control functions; and
- other MRT which are roles considered to have material impact on the risk profile of the Group.



Remuneration of MRTs for 2018

This section discloses the remuneration awards made by the Group to 147 MRTs (2017: 157) in respect of the 2018 performance year. Additional information summarising the Group's decision-making policies for remuneration are also provided. These disclosures deliver the requirements of Capital Requirements Regulation (CRR) Article 450.

The following groups of individuals have been identified as meeting the criteria for MRTs including those who may have a material impact on the Group's risk profile:

- senior management, Executive Directors, members of the Executive Leadership Team;
- Non-Executive Directors; and
- other individuals whose activities could have an impact on the Group's risk profile.

Aggregate remuneration of MRTs by business area	Banking(1)	Independent control functions(2)	Corporate functions(3)	Total
Number of MRTs	41	76	30	147
Total fixed remuneration (£m)	5.6	12.3	4.3	22.2

(1) Includes colleagues in the Customer Banking Division and the Customer Banking Director.
(2) Includes Executive Directors, Non-Executive Directors and colleagues within Risk, Internal Audit and Compliance functions.
(3) Includes Human Resources, Finance, Marketing, Products and other corporate functions.

Total value of MRTs remuneration awards	Senior management £m(1)	Other MRTs £m(2)	Total £m
Number of MRTs	22	125	147
Fixed remuneration(3)	6.7	15.5	22.2
Variable remuneration (cash)	1.5	3.5	5.0
Variable remuneration (shares)	1.3	0.3	1.6
Deferred remuneration (cash)(4)	–	–	–
Deferred remuneration (shares)(5)	–	–	–
Long-term incentive (shares)(5)(6)	6.6	2.3	8.9
Total variable remuneration(7)	9.4	6.1	15.5
Total remuneration	16.1	21.6	37.7

(1) Includes the Executive Directors, members of the Executive Leadership Team and those holding a Senior Management Function under the Senior Management Regime.
(2) Includes Non-Executive Directors, colleagues identified as MRTs under the FCA/PRA criteria and any colleagues who the Group considers to have responsibility and accountability for activities that could have a material impact on the Group's business risk profile or credit exposure and colleagues in independent Risk, Internal Audit and Compliance function roles.
(3) Excludes termination awards made under the Group redundancy policy together with Payment in lieu of notice (PILON) and any pension augmentation.
(4) Deferred bonuses awarded in cash.
(5) All awards are made as conditional rights to the Group's shares.
(6) Reflects the face value of the 2018 LTIP award.
(7) Includes current year commencement awards.

Governance

Directors' remuneration report

Other remuneration disclosures continued

Deferred remuneration	Senior management £m	Other MRTs £m	Total £m
Deferred remuneration at 30 September 2018[1]			
Outstanding vested	1.7	1.8	3.5
Outstanding unvested	12.7	5.4	18.0
Awarded during the financial year[2]	6.5	4.3	10.7
Released/paid out during the financial year[3]	1.3	1.2	2.4
Reduced through performance adjustments[4]	–	–	–

(1) Value at date of award. Figures including 2016 and 2017 deferred awards (LTIP, Bonus and commencement) plus 2018 awards.
(2) Includes 2016 and 2017 deferred bonus awards, 2016 and 2017 LTIP and 2018 commencement awards.
(3) Reflects deferred elements of 2016 and 2017 bonuses.
(4) This figure does not include the adjusted value of awards which were forfeited by colleagues upon leaving the Group.

Other remuneration	Senior management	Other MRTs	Total
Commencement awards (£m)[1]	–	0.2	0.2
Number of beneficiaries	–	2	2
Highest award to single beneficiary (£m)	–	0.1	
Termination awards (£m)[2]	–	0.6	0.6
Number of beneficiaries	–	4	4
Highest award to single beneficiary (£m)	–	0.3	

(1) Current year commencement awards and prior year buyout awards granted in 2018.
(2) Awards made under the Group redundancy policy together with PILON and any pension augmentation.

Remuneration band (€m)[1]	Senior management	Other MRTs	Total
More than €3.5m	–	–	–
€3.0m – €3.5m	1	–	1
€2.5m – €3.0m	–	–	–
€2.0m – €2.5m	–	–	–
€1.5m – €2.0m	–	–	–
€1m – €1.5m	5	–	5
€0.5m – €1.0m	4	3	7
Less than €0.5m	12	122	134

(1) Total remuneration has been calculated including fixed remuneration, allowances, variable remuneration (including 2018 LTIP at face value) in relation to the performance year, and fees for Non-Executive Directors. Variable remuneration includes the annual short-term incentive award in respect of the 2018 financial year. Bands have been converted using a rate of 1 GBP =1.1226 EUR, consistent with the European Commission's currency converter for September 2018.

Directors' report

Corporate governance report

The Corporate governance report, found on pages 48 to 114, together with this report of which it forms part, fulfils the requirements of the Corporate Governance Statement for the purpose of the FCA's Disclosure and Transparency Rules (DTR).

Company background

The Company was incorporated in England and Wales on 18 May 2015 as a public company limited by shares under the Companies Act 2006 with the name Pianodove PLC. Pianodove PLC changed its name to CYBG PLC on 1 October 2015. The registered office of the Company is at 20 Merrion Way, Leeds, West Yorkshire, LS2 8NZ with the Head Office and principal place of business of the Company being 30 St Vincent Place, Glasgow, G1 2HL.

Directors

The Directors of the Company who served during the year and their biographical details are shown on pages 53 to 57 together with David Browne, who retired as an independent Non-Executive Director on 30 June 2018 and Debbie Crosbie who stepped down as an Executive Director of the Company on 19 November 2018.

Particulars of Directors' emoluments and interests in shares in the Company are given on pages 96 to 110 of the Directors' remuneration report.

During the year, no Director had a material interest in any contract of significance to which the Company or a subsidiary undertaking was a party.

Annual general meeting (AGM)

The Company's 2019 AGM will be held at 10.00am (Melbourne time – AEDT) on Wednesday 30 January 2019 at the Melbourne Convention and Exhibition Centre, 1 Convention Centre Place, South Wharf, Melbourne, Victoria, 2006, Australia. Details of the meeting venue and the resolutions to be proposed, together with explanatory notes, are set out in a separate Notice of AGM which is published on the Company's website www.cybg.com

Board composition changes

Changes to the composition of the Board since 1 October 2017, and up to the date of this report, are shown in the table below. Further details of Board changes can be found on page 63 of the Corporate governance report and on page 70 of the Governance and Nomination Committee report.

Name	Role	Date of appointment	Date of retirement/ stepped down
David Browne	Independent Non-Executive Director		30 June 2018
Geeta Gopalan	Independent Non-Executive Director	15 October 2018	
Darren Pope	Independent Non-Executive Director	15 October 2018	
Amy Stirling	Non-Executive Director	15 October 2018	
Debbie Crosbie	Executive Director		19 November 2018

Election and re-election of Directors at the forthcoming AGM

The Company's Articles of Association provide that each Director is subject to election at the first AGM following their appointment; Non-Executive Directors Geeta Gopalan, Darren Pope and Amy Stirling will be seeking election as Directors at the 2019 AGM. Following recommendations from the Governance and Nomination Committee, the Board considers all Directors continue to be effective, committed to their roles and have sufficient time available to discharge their duties.

In accordance with the Code, all other current Directors will retire and seek re-election at the 2019 AGM.

Directors' indemnities

The Directors have each entered into individual deeds of access, insurance and indemnity with the Group which, among other things and subject to certain exceptions, indemnify the Directors to the maximum extent permitted by law and regulation against liabilities to a person other than the Company or an associated company that they may incur as an officer of the Company and any other subsidiary of the Group. Each such provision constitutes a 'third-party indemnity provision' and a 'qualifying indemnity provision' for the purposes of section 234 to 236 of the Companies Act 2006. These provisions are in force for the benefit of the Directors at the date of this report, and were in force when this report was approved and during the financial year to which this report relates. Such deeds are available for inspection at the Company's registered office.

The Group has an insurance policy in place for the benefit of all trustees, colleagues, Directors, officers, members and partners of the Company while acting in the capacity of a trustee or administrator of employee benefit or pension plans. This policy indemnifies the Directors of Yorkshire and Clydesdale Bank Pension Trustee Limited and YCB DC Trustee Limited (each a 'Trustee Company'), the trustees and administrators of the two occupational pension schemes operated by the Group, against liability incurred by them in connection with the management and administration of the pension schemes. This insurance policy constitutes a 'pension scheme indemnity provision' and a 'qualifying indemnity provision' for the purposes of sections 235 to 236 of the Companies Act 2006. These provisions are in force for the benefit of the Directors of Trustee Companies at the date of this report, and were in force when this report was approved and during the financial year to which this report relates. Such policy is available for inspection at the Company's registered office.

In addition, the Group had appropriate Directors' and Officers' Liability Insurance cover in place throughout the financial year.

Governance

Directors' report

Profits and appropriations

The Group loss before tax for the financial year ended 30 September 2018 amounted to £114m (2017: profit of £268m). The loss attributable to the ordinary shareholders for the year ended 30 September 2018 amounted to £133m (2017: profit of £146m). As at 30 September 2018, the distributable reserves of the Company were £1,005m (2017: £1,002m).

Dividends

The Directors recommend a final dividend of 3.1p per ordinary share in the Company in respect of the year ended 30 September 2018 (2017: £0.01) which will be subject to approval by shareholders at the 2019 Annual General Meeting.

Amendment to the Articles of Association

The Company may only amend its Articles of Association if its shareholders pass a special resolution to that effect.

Share capital, control and Directors' powers

Shares in the Company are listed on both the London Stock Exchange (LSE) and the ASX (in the form of CHESS Depositary Interests (CDIs)) and therefore the Company is required to comply with the disclosure requirements of both listing regimes.

Details of the movements in allotted share capital during the year, together with the rights and obligations attaching to the Company's shares, are shown in note 4.1 to the consolidated financial statements.

There are no restrictions on voting rights of securities in the Company. The Notice of AGM specifies deadlines for determining attendance and voting entitlements at the AGM.

Where participants in an employee share incentive plan operated by the Company are the beneficial owners of shares but not the registered owners, the voting rights are normally exercised at the discretion of participants.

With the exception of restrictions on the transfer of ordinary shares under the Company's SIP, while the shares are subject to the rules of the plan, there are no restrictions which exist on the transfer or holding of securities in the Company under its Articles of Association and there are no shares carrying special rights with regards to the control of the Company.

Subject to the Articles of Association and provisions of relevant statutes, the Board may exercise all powers of the Company.

Acquisition of own shares

At the AGM of the Company held on 31 January 2018 a resolution was passed that the Directors were authorised to purchase up to a maximum of 88,494,877 ordinary shares representing approximately 10% of the issued ordinary share capital. A renewal of authority will be sought at the 2019 AGM. Further information is set out in the Notice of AGM.

Political donations

The Group did not give any money for political purposes nor did it make any political donations to political parties or other political organisations, or to any independent election candidates, or incur any political expenditure during the year. At the Annual General Meeting in 2018, shareholders gave authority under Part 14 of the Companies Act to make political donations and incur political expenditure up to a maximum aggregate amount of £100,000. This authorisation was sought for prudence as it is the Group's policy not to make any political donations to political parties or incur political expenditure within the ordinary meaning of those words. Given the wide definition of donations and expenditure within the Companies Act, activities which form part of the regular operations of the Group such as communicating with government at local, national and European level and funding events to which politicians are invited, may be covered.

Financial risk management objectives and policies

Information about internal controls and financial risk management systems in relation to financial reporting and Board review can be found on page 66 of the Corporate governance report.

Information about financial risk management objectives and policies in relation to the use of financial instruments can be found in the Risk report on pages 121 to 170.

Post-balance sheet events

On 10 October 2018, the Group received IRB accreditation from the PRA for both its mortgage and SME portfolios. The Group continues to progress its Retail unsecured lending IRB application.

On 15 October 2018, CYBG PLC acquired all of the voting rights in Virgin Money by means of a Scheme of Arrangement under Part 26 of the UK Companies Act 2006 for a purchase consideration of £1.6bn. Following completion, the Bank subsequently acquired all the voting rights in Virgin Money for a consideration of £1.6bn.

On 26 October 2018 the High Court ruled on a landmark pensions case relating to the defined benefits pension schemes operated by Lloyds Banking Group. The Group is currently assessing the impact of this recent ruling on its defined benefit pension scheme, and will work with its key advisors to ensure compliance with the recent findings as appropriate.

For further details of events after the balance sheet, refer to note 5.5 of the financial statements.

Information included in the Strategic report

The following information that would otherwise be required to be disclosed in this report and which is incorporated into this report by reference can be found on the following pages of the Strategic report.

Subject matter	Page reference
Future developments	15
Colleague engagement	26 and 27
Emissions reporting	30

Equality of employment opportunities

It is the policy of the Group to promote equality of employment opportunities by giving full and fair consideration to applications from people with disabilities. If existing colleagues become disabled, every effort is made to retain them within the workforce wherever reasonable and practicable. The Group also endeavours to provide equal opportunities in the training, promotion and general career development of disabled persons.

Substantial shareholdings

Information provided to the Company pursuant to the FCA's DTR is published on Regulatory Information Services and on the Company's website.

As at 19 November 2018, being the latest practicable date prior to the publication of this document, the following information has been received, in accordance with DTR 5, from holders of notifiable interests in the Company's issued share capital. The information provided below was correct at the date of notification; however, the date received may not have been within the current financial year. It should be noted that these holdings are likely to have changed since the Company was notified. However, notification of any change is not required until the next notifiable threshold is crossed.

	Total number of shares	% of issued capital with rights to vote in all circumstances at general meetings(1)
Virgin Group Holdings Limited	188,083,550	13.18%
Perpetual Limited and subsidiaries	60,787,499	4.26%
Investors Mutual Limited	53,659,761	3.76%
Cooper Investors Pty Ltd	46,743,994	3.28%
Schroders PLC	44,572,459	3.12%
Pendal Group Limited	43,383,902	3.04%

(1) Percentage correct as at 19 November 2018.

Going concern

The Group's Directors have made an assessment of the Group's ability to continue as a going concern and are satisfied that the Group has the resources to continue in business for the foreseeable future.

The Group's use of the going concern basis for preparation of the accounts is discussed in note 1.4 of the Group's consolidated financial statements.

Viability statement

In accordance with the Code, the Directors have assessed the prospects of the Group over a three-year period to 30 September 2021.

The Directors have determined that a three-year period is an appropriate period over which to perform the assessment. This is the period over which forecasts have a greater level of certainty. The Board monitors a longer-term strategic and financial plan which extends beyond the three-year period. This longer-term strategic and financial plan provides less certainty of outcome, but provides a robust planning tool against which strategic decisions can be made.

The Directors have considered the current state of the balance sheet, principal and emerging risks which could impact the performance of the Group and the Group's strategic and financial plan. The strategic and financial plan makes certain assumptions about the performance of the Group and the economic, market and regulatory environments in which it operates. To support the planning process, downside scenario analysis has been performed to consider how the Group's performance would be affected by changing economic and market conditions throughout the planning period.

In making this assessment, the Directors have considered a wide range of information, including the Directors' robust review and challenge of the outcomes of the latest Internal Capital Adequacy Assessment Process (ICAAP) and the Internal Liquidity Adequacy Assessment Process (ILAAP), which assess the Group's future projections and stress testing of capital adequacy, liquidity and funding. The Board has also considered available capital and liquidity planning information for the Combined Group.

Information relevant to this assessment can be found in the following sections of the Annual Report and Accounts:

- a financial summary, including a review of the latest income statement and balance sheet is provided in the Financial results section pages 34-43;
- the Group's capital position is included in the Balance sheet and prudential regulation risks section of the Risk report pages 144-152;
- the Group's liquidity position is described in the Balance sheet and prudential regulation risks section of the Risk report pages 152-163;
- the Group's principal risks and policies and processes for managing those risks are described in the Risk report and summarised on pages 16 and 17;
- the Group's business model and strategy are described in the Strategic report pages 12-15; and
- the Group's approach to stress testing and reverse stress testing is described in the Risk report on page 128.

Governance

Directors' report

Based upon this assessment, the Directors have concluded that there is a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the three years to 30 September 2021.

Disclosure of information under Listing Rule (LR) 9.8.4R

Additional information required to be disclosed by LR9.8.4R, where applicable to the Group, can be found in the following sections of this report:

Subject matter	Page reference
Publication of unaudited financial information	The disclosures within the Risk report (pages 121 to 170) are unaudited unless otherwise stated.
Allotment of equity securities	227
Significant contracts	243

Research and development activities

The Group does not undertake formal research and development activities although it does invest in new platforms and products in each of its business lines in the ordinary course of business. In addition to new products and services the Group also invests in internally generated intangible assets including software and computer systems. Further details can be found in note 3.10 of the Group's consolidated financial statements.

Change of control

The Group is not party to any significant agreements that are subject to change of control provisions in the event of a takeover bid, other than the following:

– a Conduct Indemnity Deed with NAB under which NAB has agreed, subject to certain limitations, to provide CYBG with a capped indemnity in respect of certain historic liabilities relating to relevant conduct matters. The capped indemnity will not automatically cease to apply nor will it automatically terminate upon any takeover. However, prior to any change of control, the parties must cooperate in good faith to facilitate an assessment by the PRA to determine whether the capped indemnity should continue at the same amount or whether it should be terminated in whole or part. Any such assessment will be at the sole discretion of the PRA; and

– a Trade Mark Licence Agreement with Virgin Enterprises Limited (Virgin) under which Virgin has granted a licence to CYBG to use the 'Virgin' and 'Virgin Money' trademarks. Virgin has the right to terminate the agreement within 30 days of a change of control of CYBG unless it is Permitted Change of Control. A Permitted Change of Control is one arising from (a) an IPO on a recognised stock exchange or (b) any other sale of shares of CYBG which has been pre-approved by Virgin in writing. Virgin can withhold consent only in the event that the third-party purchaser is a direct competitor of Virgin or another Virgin licensee in the UK, or it is involved in any activity or possesses a reputation or financial standing which would be likely to materially damage the value or reputation of the Virgin brand.

There is a very small number of senior colleagues who are entitled to an enhanced redundancy payment if redundancy arises within the initial period of employment and is a result of a change of control. The Group has share schemes under which change of control may apply, albeit this is not considered to be significant.

Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and the Group and Company financial statements in accordance with applicable law and regulations. Company law requires the Directors to prepare financial statements for each financial year. Under that law, they are required to prepare the Group financial statements in accordance with IFRSs as adopted by the EU and applicable law and have elected to prepare the parent company financial statements on the same basis. Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Company and of the profit or loss of the Group and Company for that year. In preparing these financial statements the Directors are required to:

– select suitable accounting policies in accordance with International Accounting Standard (IAS) 8: Accounting Policies, Changes in Accounting Estimates and Errors and then apply them consistently;

– present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;

– provide additional disclosures when compliance with the specific requirements of IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the financial performance; and

– state that the Group and Company have complied with IFRSs, subject to any material departures disclosed and explained in the financial statements.

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

Under applicable law and regulations, the Directors are also responsible for preparing a Strategic report, Directors' report, Directors' remuneration report and Corporate governance statement that comply with that law and those regulations.

Responsibility statement of the Directors in respect of the Annual Report and Accounts

The Directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the Group and the undertakings included in the consolidation taken as a whole; and
- the Strategic report includes a fair review of the development and performance of the business and the position of the Company and the Group, together with a description of the principal risks and uncertainties that they face.

The Directors consider the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's and Group's position and performance, business model and strategy.

Independent auditor and audit information

In accordance with section 485 of the Companies Act 2006, a resolution to reappoint Ernst & Young LLP, and to authorise the Audit Committee to agree their remuneration, will be proposed at the next AGM.

The Directors who were members of the Board at the time of approving the Report of the Directors are listed on page 51 (excluding Debbie Crosbie who stepped down from the Board on 19 November 2018). Having made enquiries of fellow Directors and of the Group's auditor, each of these Directors confirms that:

- to the best of each Director's knowledge and belief, there is no information relevant to the preparation of their report of which the Group's auditor is unaware; and
- each Director has taken all the steps a Director might reasonably be expected to have taken to be aware of relevant audit information and to establish that the Group's auditor is aware of that information.

On behalf of the Board:

Lorna McMillan
Company Secretary
26 November 2018

CYBG PLC. Registered No. 09595911

Risk report

Risk report

"Effective management of risk is a key capability for a successful financial services provider and is fundamental to the Group's strategy. The Group has continued to advance and strengthen its risk management capabilities, evolving in line with industry developments and best practice."

Risk principles

The Group's approach to risk management is based on the principle that risk management capability must be embedded across all areas of the Group to be effective. This overriding principle embodies the following concepts:

- commercial decisions are made on the basis of proactive consideration of risk and the potential impact on customers;
- business managers use the RMF to support decision making involving risk and reward trade-offs; and
- colleagues are responsible for risk management in their day-to-day activities.

Risk culture

Central to the risk culture is the safety and soundness of the Group, the fair treatment of customers and meeting obligations to stakeholders, including shareholders, regulators and colleagues. The Board and senior management are responsible for setting and clearly communicating a strong risk culture through their actions and words, and proactively addressing any identified areas of weakness or concern.

Culture is shaped by many aspects including tangible components such as: the Group's code of conduct; operating principles; policies; standards; the risk management operating model; and an approved articulation of risk appetite that aligns to, and supports, the strategic objectives of the Group. The Group strives to instil a culture that supports compliance with all relevant laws, codes and policies and builds constructive regulatory relationships.

Initiatives that support appropriate risk culture include: the performance management framework with all areas required to have a risk management objective, messaging from the CEO and members of the Executive Leadership Team emphasising the importance of risk identification, management and mitigation and the formal whistleblowing framework that allows colleagues to raise concerns about matters of conduct in confidence and anonymously.

Underpinning the RMF and at the heart of the Group's risk culture, is the concept of personal accountability for risk management at source. This is enabled through a risk management accountability model and a formal delegation framework through which colleagues are able to make risk-based decisions.

Risk strategy

The Group has a clearly defined strategy in order to manage and mitigate risk in the daily course of its business. The strategy consists of:

- ensuring all principal, top and emerging risks are identified and assessed;
- ensuring risk appetite is clearly articulated and influences the Group's strategic plan;
- a clearly defined risk culture which emphasises risk management throughout all areas of the business while maintaining independent oversight;
- ongoing analysis of the environment in which the Group operates to proactively address potential risk issues as they arise; and
- supporting commercial decisions and people with appropriate risk processes, systems and controls.

RAS

Risk appetite is defined as the level and types of risk the Group is willing to assume to achieve its strategic objectives. The RAS articulates and supports communication of the Group's appetite to stakeholders. This is important as it provides the definitive view of risk taking activity the Board is comfortable with the Group undertaking and allows decision makers (including those with delegated authority and also those providing oversight) to exercise judgement with greater confidence and speed.

The RAS aligns to the risks identified and defined in the RMF. The design and structure of the RAS has taken into consideration best practice articulated by the European Central Bank which is aimed at ensuring Boards should be strongly involved in the validation process and monitoring of the RAS.

The Group's RAS is prepared by the Group Chief Risk Officer with consideration of the strategic objectives and business model, as well as the environment in which the Group operates. Reporting to Executive Committees and Board includes details of performance against relevant RAS settings, breaches and trends.

Risk policies and procedures

The policy framework is a key component of the Group's RMF providing structure and governance for the consistent and effective management of policies. In developing the policy framework the Group sets the tone that demonstrates the risk culture expected across the organisation. This aligns with the behavioural expectations for all colleagues which form a core part of our performance management approach. Policy statements and supporting policy standards define the minimum control requirements which must be observed across the Group to manage material sources of risk within risk appetite.

Achievements in 2018

Progressing the IRB journey

In April 2017, the Group submitted an application to the PRA for permission to adopt the IRB approach for the calculation of Credit Risk Weighted Assets (RWAs). This was followed with model submissions for mortgages, SME/corporate, Specialist Lending (Commercial Real Estate) and Unsecured Retail portfolios. Approval for the use of the IRB models for the mortgage and SME/corporate portfolios was obtained in October 2018. The programme has also supported the credit impairment element of the IFRS 9 requirements developing the required model and calculation engine capability to support implementation from 1 October 2018.

TSA exits

Significant progress has been made across all TSA exit projects. These projects are to complete the migration from legacy systems provided by the Group's former parent company NAB. The exit of the TSA for the calculation and reporting of RWAs was completed on schedule in November 2017 through implementation of a new Credit Risk Engine. The key remaining projects are in respect of Treasury related systems and are due to be completed around the end of 2018.

Structural reform

Throughout 2018, the Group has been taking steps to manage the impact of structural reform requirements (ring-fencing and operational continuity in resolution). There is very little impact on customers arising from the Group's structural reform compliance activities because there is no need for material change to business operations or corporate structures.

Cyber resilience

The Group continues to invest in our people, processes and systems to mitigate the growing and continued risks posed by cyber criminals. While the Group has been subject to external attack over the course of the year, its defences have proven effective and it has minimised any disruption to customers and colleagues.

Refresh of the Risk Management Framework (RMF)

The Group has ensured that the RMF remains fit for purpose for the evolving nature of its activities through the introduction of improvements to the way that it manages identified issues and has also initiated an end to end view of the risks associated with critical processes. It has also refreshed and updated its range of Policies and Policy Standards, most notably in relation to Change Management, Third-Party Management and Data Management, to continue to minimise risk exposure through consistent application of minimum controls.

Regulatory developments

The Group implemented a wide programme of systems and process changes to comply with new regulations and requirements from its relevant regulators and also enhanced information and services for its customers. The Group has maintained good progress on past remediation commitments and its plan for closure of these issues.

Acquisition of Virgin Money

The Group's regulators approved the application for Change in Control relative to the acquisition of Virgin Money and related entities. This was testament to the quality of the submission and the detailed planning undertaken in advance.

Ongoing maintenance of Financial Crime Framework

The Group's Financial Crime Framework has been maintained and improved through the introduction of additional systems and controls to mitigate the ongoing risks. A key outcome of these changes has been improvements in customer experience.

Priorities for 2019

Integration of Virgin Money

2019 will be a period of planning for integration and this will include how the RAS and RMF is applied across the combined Group. It is of paramount importance the Group achieves integration of risk frameworks that maintain the strength and stability of the Group for the safety and soundness of our customers.

IRB journey

The Group will continue to embed management of its business as an IRB firm, supporting business growth in a prudent and sustainable manner. This will include leveraging IRB capabilities to augment and strengthen credit measurement techniques, systems, decisioning capabilities and risk/return considerations at both portfolio and transactional level. PRA approval for use of the Retail Unsecured IRB models in the calculation of regulatory capital is being targeted for 2019.

Balance sheet risks

The Group remains focused on maintaining balance sheet strength with particular attention being paid to the regulatory developments that are completing CRD IV and MREL.

RMF enhancement

The Group will continue to enhance the core elements of the RMF to ensure that it remains fit for purpose for the changing internal landscape and for the dynamic, and at times unpredictable, external environment. For FY2019 the Group has made more explicit references to key risk areas such as vulnerable customers, data privacy and model risk, as well as re-enforcing the expected control monitoring and testing activity that should be completed by the business areas, and the additional assurance expectations of policy standard owners over key controls.

Risk report

Conduct risk
The Group will continue to develop its approach and capabilities for managing conduct risks, and remain focused on completing legacy remediation, including addressing PPI complaints through to the FCA deadline in August 2019.

Cyber resilience
In order to support the Group's digital ambitions, it will continue to invest in its cyber resilience defences. The Group engages in cross industry forums and government initiatives to ensure that it can assess and quickly address new threats and it regularly stress tests its controls and response frameworks in order that it is ready in the event of a material incident occurring.

Regulatory change
The Group continues to respond positively to the changing regulatory requirements and seeks to comply with all regulations as they continue to evolve, and as customer expectations continue to develop.

The Group is subject to ring-fencing legislation. There is very little impact on customers arising from the Group's ring-fencing compliance activities because there is no need for material change to business operations or corporate structures. Ring-fencing legislation applies from 1 January 2019.

The Group intends to continue improving its capabilities and service offerings for its customers through its principal customer channels and will continue to invest to meet all further new regulatory requirements that continue through 2019.

Economic crime
In December 2017, the Home Office introduced a series of measures to reform economic crime. Consequently, the Group continues to respond positively to a challenging timeline of legal and regulatory change and reform. Industry engagement relative to these changes is ongoing and is key to ensuring there is appropriate analysis, impact assessment and consistency of approach.

Principal risk categories

See page 17 in the Strategic report for details on the Group's principal risk categories.

Top and emerging risks

The Group monitors the environment in which it operates to identify top and emerging risks that may have an impact on its operations and strategy. The Group currently considers its top and emerging risks to be:

Geopolitical and macroeconomic environment
The Group is exposed to a variety of downstream risks resulting from the geopolitical environment, which have significant business relevance. With a predominantly UK-based customer profile, the Group continues to monitor credit portfolios closely. Regular assessments of strategic plans, risk appetite and risk sensitivity analysis are undertaken to minimise and negate potential impacts.

The UK vote to leave the EU (Brexit)
There is ongoing monitoring of the UK's withdrawal from the EU, with negotiations creating significant economic uncertainty and a potential negative impact for the UK macroeconomy. The Group continues to consider all potential consequences for its customers, products and operating model with mitigating actions in place as appropriate. The uncertainty and related pace of change is being monitored closely and the Group will react appropriately having given consideration to both potential and actual outcomes, customer and other stakeholder implications.

Competition
The financial services industry is a highly competitive environment. The emergence of new entrants and regulatory initiatives, such as Open Banking, may lead to material changes in the future provision of financial services. The Group recognises both the risks and opportunities resulting from the changes and continues to develop strategies, products and technologies to ensure it can take strategic advantage where possible and mitigate any corresponding risks.

Consumer credit
The Group maintains an awareness of the risk of significant credit losses occurring within a short time period which would have a detrimental impact on earnings and profitability. Credit risk strategies, appetite and tolerance levels are reviewed and approved by the Board and regular monitoring of the credit portfolio, including risk sensitivity analysis and reviews of asset quality metrics, is undertaken to ensure early identification and mitigation of potential risks. Unsecured consumer lending is an area of considerable regulatory focus and one where the Group is particularly alert to the potential regulatory, economic and customer impacts. New strategies have been delivered in response to revised regulatory requirements and reviews are underway to address further, future change.

Cybersecurity and IT
With increasing levels of attempted cyber attacks across the industry, the Group remains vigilant, and acknowledges the potential risks of such attacks including; service interruption, data loss, customer and financial detriment and reputational damage. The Group continues to enhance and invest in the control environment, recognising the changing cyber landscape, and the increased focus on digital capabilities, as well as the changing risk profile of the business.

Financial crime (including cybercrime)
The Group, in conjunction with the wider industry, continues to be subject to increasing fraud attacks. In response, the Group continues to enhance its fraud defences with particular focus on behavioural analysis tools. The management of financial crime remains a key area of regulatory focus and the Group continues to enhance its framework for monitoring, management and mitigation of financial crime.

Regulatory capital change

The Group, in common with the financial services industry as a whole, continues to face a significant agenda of regulatory and legislative change, including those pertaining to taxes. The Group continues to monitor the emerging requirements and ensure it is well placed to respond with effective regulatory change management. The Basel Committee published their final Basel III framework in December 2017. A key objective of the revisions is to reduce excessive variability of RWAs and improve the comparability of banks' capital ratios. Implementation dates range from 2022 to 2027 and the Committee has introduced transitional arrangements to ensure an orderly and timely implementation. The Group will be advised of its final MREL requirements by 2020 and the outcome may result in additional costs to those that have already been incorporated into the Group's Strategic Plan.

Integrating Virgin Money

The risks associated with the acquisition of Virgin Money have been described in detail in the prospectus to the transaction. The acquisition represents a significant programme of change requiring prudent management in order to deliver the benefits from the transaction. There is a risk that issues arise during integration that may lead to additional costs or a delay in the realisation of benefits. The integration programme places customers' interests at the centre of all aspects of change.

Customer detriment

The Group acknowledges the continued risk of historic customer detriment and the risk of issues not being accurately identified at an early stage due to failures to adhere to, or maintain, a robust control framework, leading to potential customer treatment or fairness issues. The Group ensures that the underlying framework is robust and continues to work closely with its Regulators.

Service interruption and operational resilience

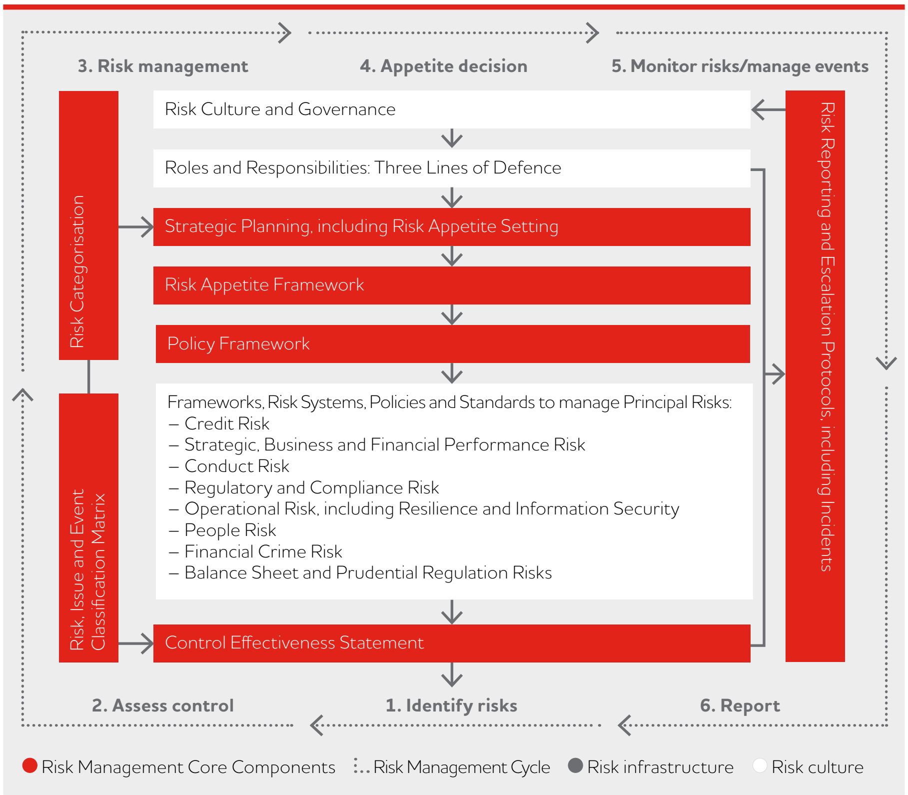
There is a reputational risk and/or adverse impact on customer confidence which may result from service interruption to critical operational services. The Group continues to strengthen resilience in its platforms and make upgrades to its core data networks in a bid to mitigate this risk.

Third-party suppliers

The Group acknowledges an increased risk associated with the use of third parties to perform core functions. The Group continues to enhance its third-party management framework and ensures that the procurement of service providers adheres to these requirements.

Risk Management Framework (RMF)

The Group identifies and manages risk using the RMF (see diagram below), which is the totality of systems, structures, policies, processes and people that identify, measure, evaluate, control, mitigate, monitor and report all internal and external sources of material risk.



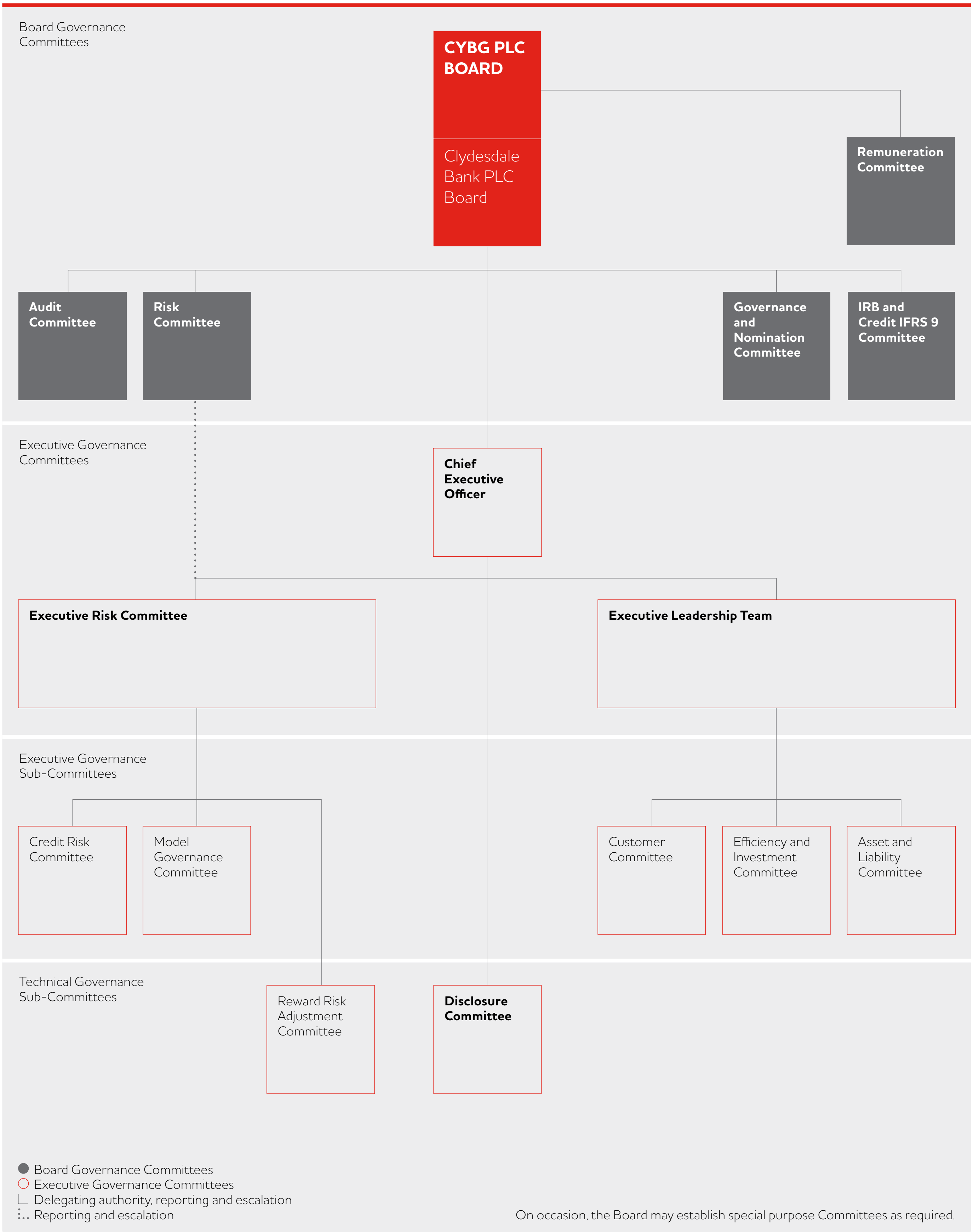
Risk governance and oversight

The Group's risk governance structure strengthens risk evaluation and management, while also positioning the Group to manage the changing regulatory environment in an efficient and effective manner.

The Group's risk management is governed via a series of committees, as represented within the diagram which follows.

During the year the Group completed a review of the executive committee layer in the risk governance structure to ensure it balances regulatory, legal and compliance obligations while making timely, customer focused decisions that drive the business forward.

Risk report


Board Governance Committees
CYBG PLC BOARD
Clydesdale Bank PLC Board
Remuneration Committee
Audit Committee
Risk Committee
Governance and Nomination Committee
IRB and Credit IFRS 9 Committee
Executive Governance Committees
Chief Executive Officer
Executive Risk Committee
Executive Leadership Team
Executive Governance Sub-Committees
Credit Risk Committee
Model Governance Committee
Customer Committee
Efficiency and Investment Committee
Asset and Liability Committee
Technical Governance Sub-Committees
Reward Risk Adjustment Committee
Disclosure Committee
Board Governance Committees
Executive Governance Committees
Delegating authority, reporting and escalation
Reporting and escalation
On occasion, the Board may establish special purpose Committees as required.

The following Executive level Committees have been established under the authority of the CEO:

Committees	Risk focus
Executive Leadership Team	The Executive Leadership Team supports the CEO to lead the Group to be a strong, customer-focused bank for its communities, by focusing on three business priorities: sustainable growth; efficiency; and capital optimisation.
Executive Risk Committee	The Executive Risk Committee supports the CEO in respect of risk and control accountabilities and serves to provide leadership focus on key risk issues, including: – endorsing the RAS for approval by the Board; – overseeing and challenging the enterprise wide risk performance and control environment of the Group and business units, including the effective use of policy, frameworks and tools; – monitoring the status of regulatory relationships, the reputation of the Group in relation to its regulators and the changing state of the regulatory landscape, including the impacts for and readiness of the Group; – monitoring the strength of risk capability and capacity, including risk training and education plans to ensure an effective risk and control framework; and – reviewing and endorsing risk policies, frameworks and tools for use across the Group.
Disclosure Committee	The Disclosure Committee is responsible for ensuring the Group complies with its continuous disclosure obligations for exchanges on which it has equity and debt securities listed.

The Executive Risk Committee is supported by the following committees:

Credit Risk Committee	The Credit Risk Committee is responsible for ensuring that the Credit RMF and associated policies remain effective. The committee has oversight of the quality, composition and concentrations of the credit risk portfolio and recommends strategies to adjust the portfolio to react to changes in market conditions.
Model Governance Committee	The Model Governance Committee supports the Board in fulfilling its governance responsibilities for material models and rating systems. The Committee oversees the integration and ongoing use of models across the Group, specifically considering the fitness for purpose, usability and scalability of models.
Reward Risk Adjustment Committee	The Reward Risk Adjustment Committee is responsible for considering and providing feedback to the Boards' Risk Committee and the Remuneration Committee in relation to risk events which may affect awards of variable pay and therefore ensuring that the Group complies with its regulatory requirements in respect of establishing and maintaining a robust risk adjustment process.

The Executive Leadership Team is supported by the following committees:

Customer Committee	The Customer Committee is responsible for overseeing the service and commercial performance of the Group to ensure that customer needs are being met in line with the Group's strong customer-focused culture and sustainable growth ambitions. It considers the optimal mix of customer-focused products and is responsible for ensuring that the Group operates within a robust conduct and pricing framework.
Efficiency and Investment Committee	The Efficiency and Investment Committee is responsible for overseeing the management of sustainable costs across the Group while supporting its growth ambitions, aligned to risk appetite.
Asset and Liability Committee (ALCO)	ALCO is responsible for monitoring the performance of the Group against the Board approved capital and funding plans. The committee focuses on the Group's non-traded market risks including capital, funding, liquidity and interest rate risk to ensure that the Group's activity complies with regulatory and corporate governance requirements and also delivers Group policy objectives. The impact of pension risk on capital is also assessed by ALCO.

Risk report

Three Lines of Defence

Effective operation of a Three Lines of Defence model is integral to the Group's approach to risk management and is based on the overriding principle that risk capability must be embedded within the first line of defence teams to be effective. This principle embodies the following concepts:

– risk management responsibilities are clearly understood by all colleagues when carrying out their day-to-day activities;

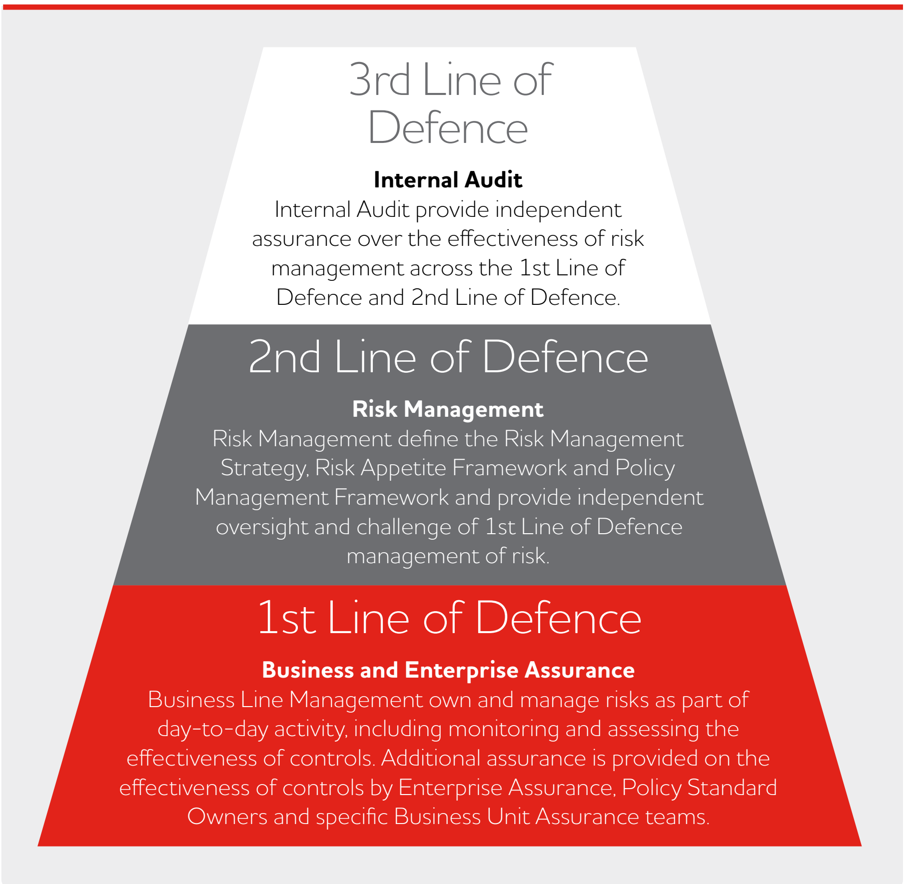
– commercial decisions are made on the basis of proactive consideration of risk and the impact on customers;

– management must use the RMF to support decision making involving risk and reward trade-offs;

– risk management activities are focused on enhancing sustainable business performance; and

– regular assessments are undertaken to confirm the effectiveness of the risk and control frameworks in relation to both the current and emerging risk profile.

Control is exercised through a clearly defined delegation of authority, with communication and escalation channels throughout the Group.



Risk management and internal controls

Assessment of principal risks
The Board is responsible for determining the nature and extent of the risks it is willing to take in order to achieve its strategic objectives.

In line with the UK Corporate Governance Code (the Code) requirements, the Directors have performed a robust assessment of the risks facing the Group, including those that would threaten its business model and future performance, solvency or liquidity.

The principal risks the Group actively monitors and manages are described on page 17 of the Strategic report.

Risk management and internal controls
The Board actively monitors the Group's risk management and internal control systems. A review of the effectiveness of those systems has been performed incorporating all material controls, including financial, operational and compliance controls.

Stress testing
Stress testing is an important and recognised risk management tool, used to assess the vulnerability of financial institutions through the modelling of adverse scenarios. The Group uses stress testing to support the identification of risks and potential vulnerabilities under adverse economic scenarios or specific events. Risk appetite, risk mitigation and contingency planning are informed by stress testing processes.

In addition to supporting risk appetite, stress testing is used within strategic planning, capital funding and liquidity plans and for more detailed deep-dive analysis within specific portfolios.

The Group undertakes stress testing following the Basel Committee principles and utilising, where appropriate, scenarios provided by the BoE.

The Board and senior management are actively involved in the consideration of stress testing. This involvement works through all aspects of stress testing from the consideration of scenarios or events to be tested to the outcomes and mitigating actions. The involvement of the Board and senior management is considered to be essential for the effective operation of stress testing and the manner in which the results can then inform strategic planning and risk appetite. Reverse stress testing is also undertaken to assess the types of risks that would pose fundamental threats to the viability of the Group's business model.

Risk classes

Risk report

Credit risk

Strongly performing credit portfolios, well-positioned for growth

Close monitoring, robust policies and a well-controlled framework support the credit operations of the Group.

Credit risk is the risk that a borrower or counterparty fails to pay the interest or capital due on a loan or other financial instrument.

Credit risk manifests itself in the financial instruments and/or products that the Group offers, and those in which the Group invests (including, among others, loans, guarantees, credit-related commitments, letters of credit, acceptances, inter-bank transactions, swaps and bonds). Credit risk can be found both on- and off-balance sheet.

Risk appetite

The Group controls its levels of credit risk by placing limits on the amount it is willing to take within credit risk capacity in order to achieve its business objectives. This involves a defined set of qualitative and quantitative limits in relation to its credit risk concentrations to one borrower, or group of borrowers, and to geographical, product and industry segments. The management of credit risk within the Group is achieved through ongoing approval and monitoring of individual transactions, regular asset quality reviews and independent oversight of credit decisions and portfolios across the Group.

Credit strategies and policies

Credit risks associated with lending are managed through the application of detailed lending policies and standards which outline the approach to lending, underwriting criteria, credit mandates, concentration limits and product terms. Credit risk is managed and monitored using the credit models that underpin the recent IRB approval for the mortgage and SME/ corporate portfolios. The Group maintains a dynamic approach to credit management and aims to take necessary steps if individual issues are identified or if credit performance deteriorates, or is expected to deteriorate, due to borrower, economic or sector-specific weaknesses.

Roles and responsibilities for the management, monitoring and mitigation of credit risk within the Group are clearly defined in line with the Group's RMF.

Significant credit risk strategies and policies are approved, and reviewed annually, by the Credit Risk Committee. For complex credit products and services, the Head of Business Risk, Head of Retail Risk and Credit Risk Committee provide a policy framework which identifies and quantifies risks and establishes the means of mitigating such risks. These policies and frameworks are delegated to, and disseminated under the guidance and control of executive management, with appropriate oversight through governance committees.

Exposures

Credit risk exposures are categorised as Retail (secured and unsecured) and SME. In terms of loans and advances, credit risk arises both from amounts loaned and commitments to extend credit to customers. To ensure appropriate credit limits exist, especially for SME lending, a single large exposure policy is in place and forms part of the risk appetite measures that are monitored and reported on a monthly basis. The overall composition and quality of credit portfolio exposures are monitored and periodically reported to the Board and, where required, to the relevant supervisory authorities.

Exposures are also managed in accordance with the large exposure reporting requirements of the CRR.

Unless otherwise noted, the amount that best represents the maximum credit exposure at the reporting date is the carrying value of the financial asset.

Measurement

The Group uses a combination of strategies and statistical models that utilise internal and external data to measure the exposure to credit risk within the portfolios.

Portfolios are assessed using segmentation for measurement, reporting and monitoring purposes.

In October 2018, the Group obtained permission to use IRB models to measure the credit risk of loans and advances to customers in its mortgage and SME/ corporate portfolios. The Group will continue to embed the IRB standard through advanced monitoring and governance of its credit models.

As at 30 September 2018, all exposures were measured under the standardised approach for regulatory capital.

Note 3.6 provides details of the Group's approach to the impairment of financial assets and the calculation of impairment charge.

Key credit metrics (audited)

	2018	2017
Impairment charge on credit exposures (£m)		
SME lending (including lease finance)	**15**	33
Retail lending	**26**	15
	41	48
Of which		
Specific charge for impairment losses	**43**	46
Collective (release)/charge for impairment losses	**(2)**	2
	41	48
Impairment provisions held on credit exposures (£m)		
SME lending (including lease finance)	**136**	154
Retail lending	**59**	56
	195	210
Of which		
Specific provision	**43**	56
Collective provision	**152**	154
	195	210
Credit risk adjustments held on loans at fair value (£m)		
SME lending	**8**	11
Of which		
Individually assessed credit risk adjustments	**1**	2
Collectively assessed credit risk adjustments	**7**	9
	8	11
Impairment credits on loans held at fair value	**(3)**	(6)
Past due and impaired assets (£m)		
90+ days past due (DPD) assets	**178**	161
Impaired assets(1)	**125**	179
Asset quality measures (%)		
90+ DPD plus impaired assets to customer loans	**0.91%**	1.06%
Specific provisions to impaired assets(2)	**35.5%**	32.6%
Net write-offs to customer loans(3)	**0.17%**	0.18%
Total provision to customer loans(4)	**0.61%**	0.69%
Total impairment charge to average customer loans (cost of risk)(5)	**0.12%**	0.14%

(1) Impaired assets for September 2018 and September 2017 includes £2m and £4m of impaired fair value loans respectively.
(2) Total specific provision includes the individually assessed credit risk adjustments on loans at fair value.
(3) Net write-offs includes loans at fair value.
(4) Total provision to customer loans includes the credit risk adjustments on loans at fair value through profit and loss.
(5) Total impairment charge to average customer loans includes loans held at fair value through profit and loss.

Risk report

Credit risk

The Group's appetite for lending is strictly defined and adhered to and the strength of the loan book is underpinned by the continued focus on, and maintenance of, high underwriting standards plus early and proactive identification of customers experiencing financial difficulty. The strong lending growth in the year has been delivered in the context of a benign economic environment, which together have contributed to a reduction in the level of impaired loans from £179m to £125m and resulted in the 90+ DPD plus impaired asset ratio falling from 1.06% to 0.91%. While a level of sensitivity to economic shocks remains, no material effects have yet been observed, however, it is accepted a more challenging credit environment is likely to lead to increased impairment from the current low levels.

The decrease in impairment charge, from £48m to £41m, reflects a lower charge taken on our SME exposures offsetting an increase in the charge for Unsecured Retail exposures. The cost of risk has consequently decreased by 2bps.

Within the Retail portfolio, the level of impaired mortgage lending remains modest against a growing book. This reflects the strong credit quality of the portfolio, supported by the low interest rate environment and stable house price indices. The level of 90+ DPD has seen an increase for both secured and unsecured portfolios.

SME asset quality measures continued to improve reflective of the focus on responsible credit decisions and controlled risk appetite which leads to a well-balanced and diverse portfolio. This portfolio will be most susceptible to any material economic downturns following Brexit, in particular any industry specific shocks, e.g. agriculture.

The ratio of total provisions to customer loans reduced by 8bps to 0.61% in the year, driven by the reduced level of specific provisions held for amortised cost loans and lower collective provision for assets held at fair value.

Maximum exposure to credit risk (audited)

The table below shows the maximum exposure to credit risk, including derivatives. The maximum exposure is shown gross, before the effect of mitigation through use of master netting and collateral agreements. The table also shows the maximum amount of commitments from the Group's banking operations.

	2018 £m	2017 £m
Cash and balances with central banks (note 3.1)	**6,573**	6,937
Due from other banks	**836**	1,174
Financial assets available for sale (note 3.2)	**1,562**	2,076
Other financial assets at fair value (note 3.3)	**362**	477
Derivative financial assets (note 3.4)	**262**	282
Loans and advances to customers (note 3.5)	**32,744**	31,293
Due from customers on acceptances	**4**	4
	42,343	42,243
Contingent liabilities (note 5.1)	**119**	111
Other credit commitments (note 5.1)	**7,016**	8,408
Maximum credit risk exposure	**49,478**	50,762

Mitigation

The management and mitigation of credit risk within the Group is achieved through both approval and monitoring of individual transactions and asset quality, analysis of the performance of the various credit risk portfolios, and the independent oversight of credit portfolios across the Group. Portfolio monitoring techniques cover such areas as product, industry or geographic concentrations and delinquency trends.

There is regular analysis of the borrower's ability to meet their interest and capital repayment obligations with early support and mitigation steps taken where required. Credit risk mitigation is also supported, in part, by obtaining collateral, and corporate and personal guarantees where appropriate.

Other mitigating measures are described below:

Specialist expertise
Credit quality is managed and monitored by skilled teams including, where required, specialists who provide dedicated support for customers experiencing financial difficulty.

Credit decisions utilise credit scoring techniques and manual underwriting, as appropriate. These tasks are performed by skilled and competent specialists acting within agreed delegated authority levels set in accordance with their experience and capabilities.

Credit policy and adherence to policy standards
Specialist teams oversee credit portfolio performance as well as adherence to credit risk policies and standards. Activities include targeted risk-based reviews, providing an assessment of the effectiveness of internal controls and risk management practices. Bespoke assignments are also undertaken in response to emerging risks and regulatory requirements. Independent assurance reviews are also regularly undertaken by Internal Audit.

Portfolio oversight
Portfolios of credit and related risk exposures and the key benchmarks, behaviours and characteristics by which those portfolios are managed in terms of credit risk exposures, are regularly reviewed. This entails the production and analysis of regular portfolio monitoring reports for review by senior management.

Controls over rating systems
The Group has an Independent Model Validation Unit that sets common minimum standards. The standards are designed to ensure risk models and associated rating systems are developed consistently, and are of sufficient quality to support business decisions and meet regulatory requirements.

Stress testing
Stress test scenarios are regularly prepared with the outcomes reviewed and relevant actions taken. Outputs will typically include impairment charges, RWA, and write-offs. Management will consider how each stress scenario may impact on different components of the credit portfolio. The primary method applied uses migration matrices, modelling the impact of PD rating migrations and changes in portfolio default rates to changes in macroeconomic factors, to obtain a stressed position for the credit portfolios. Loss given default (LGD) is stressed based on asset price movements.

The Group also utilises other instruments and techniques across its wider balance sheet. These are summarised below:

Derivatives
The Group maintains control limits on net open derivative positions. At any one time, the amount subject to credit risk is limited to the current fair value of instruments that are favourable to the Group (i.e. assets where their fair value is positive), which, in relation to derivatives, may only be a small fraction of the contract, or notional values used to express the volume of instruments outstanding. This credit risk is managed as part of the customers' overall exposure together with potential exposures from market movements.

Master netting agreements
The Group further restricts its exposure to credit losses by entering into master netting arrangements with counterparties with whom it undertakes a significant volume of transactions. Master netting arrangements do not generally result in an offset of balance sheet assets and liabilities, as transactions are usually settled on a gross basis. However, credit risk associated with the favourable contracts is reduced by a master netting arrangement to the extent that, if any counterparty failed to meet its obligations in accordance with the agreed terms, all amounts with the counterparty are terminated and settled on a net basis. Derivative financial instrument contracts are typically subject to the International Swaps and Derivatives Association (ISDA) master netting agreements, as well as Credit Support Annexes (CSA), where relevant, around collateral arrangements attached to those ISDA agreements. Derivative exchange or clearing counterparty agreements exist where contracts are settled via an exchange or clearing house.

Credit assessment and mitigation for Retail and SME customers

The Group uses a variety of lending criteria when assessing applications for Retail customers. The approval process uses credit scorecards, as well as manual underwriting, and involves a review of an applicant's previous credit history using information held by credit reference agencies.

The Group also assesses the affordability of the borrower under stressed scenarios for retail secured lending, including increased interest rates. In addition, the Group has in place quantitative thresholds, such as maximum limits on the level of borrowing to income and the ratio of borrowing to collateral. Some of these limits relate to internal approval levels and others are hard limits above which the Group will reject the application.

For residential mortgages, the Group's policy is to accept only standard applications with a LTV less than 95%. The Group has maximum percentage LTV limits which depend upon the loan size. Product types such as BTL and residential interest-only mortgages are controlled by transactional limits covering both LTV and value.

For SME customers, credit risk is managed in accordance with lending policies, the Group's risk appetite and the RMF. Lending policies and performance against risk appetite are reviewed regularly. Credit risk is further mitigated by focusing on business sectors where the Group has specific expertise and through limiting exposures on higher value loans and to certain sectors. When making credit decisions for SME customers the Group will routinely assess the primary source of repayment,

Risk report

Credit risk

most typically the cash generated by the customer through its normal trading cycle. Secondary sources of repayment are also considered and while not the focus of the lending decision, collateral will be taken when appropriate. The Group seeks to obtain security cover, and where relevant, personal guarantees from borrowers.

Monitoring

Credit policies and procedures, which are subject to ongoing review, are documented and disseminated in a form that supports the credit operations of the Group.

- *Credit Risk Committee (CRC):* The CRC ensures that the credit RMF and associated policies remain effective. The Committee has oversight of the quality, composition and concentrations of the credit risk portfolio and considers strategies to adjust the portfolio to react to changes in market conditions.
- *RAS measures*: Measures are monitored monthly and reviewed bi-annually, at a minimum, to ensure that the measures accurately reflect the Group's risk appetite, strategy and concerns relative to the wider macro environment. All measures are subject to extensive engagement with the Executive Leadership Team and the Board, and are subject to endorsement from executive governance committees prior to Board approval. Regulatory engagement is also scheduled as appropriate.
- *Risk concentration:* Concentration of risk is managed by client/counterparty, product, geographical region and industry sector. In addition, single name exposure limits exist to control exposures to a single entity/ counterparty. Concentrations are also considered through the RAS process focusing particularly on comparing the portfolio against market benchmarks.
- *Single large exposure excesses:* All excesses are reported to the Transactional Credit Committee (TCC) and relevant Head of Risk. Any exposure which continues or is expected to continue beyond 30 days will also be submitted to the TCC with proposals to correct the exposure within an agreed period, not to exceed 12 months.

Concentrations

Industry concentration of assets

The following tables show the levels of industry concentration of credit risk as at 30 September:

Gross loans and advances to customers including loans designated at fair value through profit or loss (audited)(1)	2018 £m	2017 £m
Property – mortgage	**24,540**	23,480
Agriculture, forestry, fishing and mining	**1,676**	1,743
Instalment loans to individuals and other personal lending (including credit cards)	**1,239**	1,165
Manufacturing	**853**	724
Wholesale and Retail	**779**	778
Property – construction	**246**	212
Financial, investment and insurance	**116**	90
Government and public authorities	**41**	32
Other commercial and industrial	**3,791**	3,743
	33,281	31,967

Contingent liabilities and credit-related commitments (audited)	2018 £m	2017 £m
Property – mortgage	**1,937**	2,305
Agriculture, forestry, fishing and mining	**294**	375
Instalment loans to individuals and other personal lending (including credit cards)	**1,800**	1,945
Manufacturing	**587**	588
Wholesale and Retail	**477**	606
Property – construction	**–**	154
Financial, investment and insurance	**84**	290
Government and public authorities	**276**	426
Other commercial and industrial	**1,680**	1,830
	7,135	8,519

(1) Includes balances due from customers on acceptances and excludes accrued interest.

Credit quality of customer lending

An assessment of the credit quality of loans and advances to customers is shown below:

Distribution of loans and advances to customers by credit quality (audited)

As at 30 September 2018	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending[1] £m	Total £m
Gross loans and advances:							
Neither past due nor impaired	**48**	**365**	**749**	**24,131**	**636**	**6,301**	**32,230**
Past due but not impaired	**7**	**16**	**18**	**370**	**23**	**130**	**564**
Impaired	**–**	**–**	**–**	**39**	**1**	**83**	**123**
	55	**381**	**767**	**24,540**	**660**	**6,514**	**32,917**

As at 30 September 2017	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending[1] £m	Total £m
Gross loans and advances:							
Neither past due nor impaired	51	384	635	23,104	572	6,054	30,800
Past due but not impaired	7	12	16	327	22	129	513
Impaired	–	–	–	49	–	126	175
	58	396	651	23,480	594	6,309	31,488

(1) SME lending includes business overdrafts.

Credit risk categorisation	Description
Neither past due nor impaired	Loans that are not in arrears and where there is no objective evidence of impairment.
Past due but not impaired	Loans that are in arrears but have not been individually assessed as impaired.
Impaired	Loans which have been individually assessed for impairment as there is objective evidence of impairment, including changes in customer circumstances.

Movement in gross impaired loan balances throughout the year (unaudited)

	2018 £m	2017 £m
Opening balance	**175**	214
New	**39**	72
Write-off	**(38)**	(49)
Returned to performing	**(53)**	(62)
Closing balance	**123**	175

In addition to the gross impaired loans, there were also £2m impaired fair value (2017: £4m).

Loans and advances which were past due but not impaired

Loans and advances that are past due but not impaired are classified as such for secured lending, where the net current market value of supporting security is sufficient to cover all principal, interest and other amounts (including legal, enforcement, realisation costs etc.) due on the facility.

Unsecured retail lending and credit cards are written off when they reach 180 DPD and are not designated as impaired, in compliance with the EU Payment Accounts Directive.

Risk report

Credit risk

The distribution of gross loans and advances that are past due but not impaired is analysed below:

2018 (audited)	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending[1] £m	Total £m
1 to 29 DPD	**6**	**8**	**7**	**174**	**23**	**77**	**295**
30 to 59 DPD	**–**	**2**	**4**	**40**	**–**	**15**	**61**
60 to 89 DPD	**–**	**2**	**2**	**18**	**–**	**8**	**30**
Past due 90 days and over	**1**	**4**	**5**	**138**	**–**	**30**	**178**
	7	**16**	**18**	**370**	**23**	**130**	**564**

2017 (audited)	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending[1] £m	Total £m
1 to 29 DPD	5	6	6	142	22	88	269
30 to 59 DPD	1	2	3	32	–	10	48
60 to 89 DPD	–	1	2	30	–	2	35
Past due 90 days and over	1	3	5	123	–	29	161
	7	12	16	327	22	129	513

Movement in impairment provisions throughout the year

2018 (audited)	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending[1] £m	Total £m
Opening balance	**4**	**7**	**12**	**33**	**2**	**152**	**210**
Charge for the year	**3**	**8**	**14**	**1**	**–**	**15**	**41**
Amounts written off	**(4)**	**(10)**	**(16)**	**(2)**	**–**	**(36)**	**(68)**
Recoveries of amounts written off in previous years	**2**	**3**	**4**	**–**	**–**	**4**	**13**
Other[2]	**–**	**–**	**–**	**–**	**–**	**(1)**	**(1)**
Closing balance	**5**	**8**	**14**	**32**	**2**	**134**	**195**
Specific	**–**	**–**	**–**	**12**	**–**	**31**	**43**
Collective	**5**	**8**	**14**	**20**	**2**	**103**	**152**
	5	**8**	**14**	**32**	**2**	**134**	**195**

2017 (audited)	Retail overdrafts £m	Credit cards £m	Other retail lending £m	Mortgages £m	Lease finance £m	SME lending[1] £m	Total £m
Opening balance	3	6	10	39	2	155	215
Charge for the year	2	6	9	(2)	–	33	48
Amounts written off	(4)	(9)	(13)	(4)	–	(45)	(75)
Recoveries of amounts written off in previous years	3	4	6	–	–	5	18
Other[2]	–	–	–	–	–	4	4
Closing balance	4	7	12	33	2	152	210
Specific	–	–	–	13	–	43	56
Collective	4	7	12	20	2	109	154
	4	7	12	33	2	152	210

(1) SME lending includes business overdrafts.
(2) Other includes the recognition of certain impaired loans which were previously recorded at fair value through profit or loss, the unwind of net present value elements of specific provisions and other minor movements.

Collateral

Collateral held as security and other credit enhancements

The Group evaluates each customer's creditworthiness on a case by case basis. The amount of collateral obtained, if deemed necessary by the Group upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held can vary, but may include:

- specific charges over defined assets of the counterparty;
- a floating charge over all assets and undertakings of an entity, including uncalled capital and called but unpaid capital;
- specific or interlocking guarantees; and
- loan agreements which include affirmative and negative covenants and in some instances guarantees of counterparty obligations.

Generally, the Group does not take possession of collateral it holds as security or call on other credit enhancements that would result in recognition of an asset on its balance sheet.

It is the Group's policy to dispose of repossessed properties with the proceeds used to reduce or repay the outstanding balance. In general, the Group does not occupy repossessed properties for its own business use.

The LTV ratio of Retail mortgage lending, coupled with the relationship of the debt to customers' income, is key to the credit quality of these loans. The table below sets out the indexed LTV analysis of the Group's Retail mortgage stock.

LTV (audited)(1)	2018 %	2017 %
Less than 50%	**31**	33
50% to 75%	**51**	49
76% to 80%	**6**	7
81% to 85%	**5**	4
86% to 90%	**4**	4
91% to 95%	**2**	1
96% to 100%	**–**	–
Greater than 100%	**–**	–
Unknown	**1**	2
	100	100

(1) LTV of the mortgage portfolio is defined as mortgage portfolio weighted by balance and indexed using the MIAC Acadametrics indices at a given date. Unknown represents loans where data is not currently available due to front book data matching still to be completed and a de minimis amount due to weaknesses in historic data capture processes.

Residential mortgages

Residential property is the Group's main source of collateral and means of mitigating loss in the event of the default credit risk inherent in its residential mortgage portfolios. All lending activities are supported by an appropriate form of valuation using either professional or indexed (subject to policy rules and confidence levels) valuations.

Commercial property

Commercial property is the Group's main source of collateral on SME lending and means of mitigating loss in the event of default. Collateral for the majority of commercial loans comprises first legal charges over freehold or long leasehold property (including formal Companies House registration where appropriate).

Non-property related collateral

In addition to residential and commercial property based security, the Group also takes other forms of collateral when lending. This can involve obtaining security against the underlying loan through the use of cash collateral and/or netting agreements, both of which reduce the original exposure by the amount of collateral held, subject to volatility and maturity adjustments where applicable.

The Group also operates a policy of obtaining security against the underlying loan via the use of guarantees, which can be either limited or unlimited, making the guarantor liable for only a portion or all of the debt.

The following table shows the total non-property collateral held by sector at 30 September in terms of cash, guarantees (these guarantors are predominantly other financial institutions who are considered to be of a high credit quality) and netting. The exposure amount shown below is the total gross exposure (before any credit risk mitigation and credit conversion factors have been applied where applicable) for arrangements which have some form of associated collateral held against it and is not the total exposure for each asset class, as disclosed elsewhere in this section.

Risk report

Credit risk

2018 (audited)	Cash £m	Guarantee £m	Netting £m	Total £m	Exposure £m
Central government or central banks	**3,057**	**–**	**–**	**3,057**	**4,525**
Corporates	**28**	**15**	**75**	**118**	**180**
Financial institutions	**–**	**–**	**–**	**–**	**–**
Exposures in default	**–**	**–**	**–**	**–**	**1**
Regional government or local authorities	**–**	**–**	**83**	**83**	**83**
Secured by mortgages on commercial real estate	**–**	**–**	**–**	**–**	**38**
Secured by mortgages on residential property	**–**	**–**	**–**	**–**	**4**
	3,085	**15**	**158**	**3,258**	**4,831**

2017 (audited)	Cash £m	Guarantee £m	Netting £m	Total £m	Exposure £m
Central government or central banks	3,264	–	–	3,264	4,629
Corporates	27	25	42	94	104
Financial institutions	874	–	–	874	970
Exposures in default	–	–	–	–	4
Regional government or local authorities	–	–	59	59	59
Secured by mortgages on commercial real estate	3	–	31	34	74
Secured by mortgages on residential property	1	–	3	4	9
	4,169	25	135	4,329	5,849

The decrease in cash collateral held and corresponding exposure is due to movement within repurchase (repo) and similar transactions outstanding at 30 September 2018 (including TFS drawings), reflected within Central Governments or Central Banks. The decrease in cash collateral held and corresponding exposure in financial institutions is due to the maturity of a repurchase (repo) and no outstanding reimbursement receivable from NAB previously held in relation to the conduct indemnity deed (described further in note 3.14).

Corporates is the largest sector utilising other risk mitigation techniques, with all three methods utilised dependent on credit quality. The extent to which these will be used is dependent on the specific circumstances of the customer.

Retail secured credit by loan size concentration (audited)	2018		2017	
	£m	%	£m	%
£0–£99k	**3,976**	**16.2%**	4,207	17.9%
£100k–£249k	**7,081**	**28.9%**	6,962	29.7%
£250k–£499k	**7,431**	**30.3%**	7,004	29.8%
£500k–£999k	**4,699**	**19.1%**	4,259	18.1%
£1m–£2.49m	**1,289**	**5.2%**	1,006	4.3%
> = £2.5m	**64**	**0.3%**	42	0.2%
Total	**24,540**	**100%**	23,480	100%

Retail secured credit average LTVs by loan size (unaudited)(1)	2018			2017		
	Residential	BTL	Total	Residential	BTL	Total
£0–£99k	**45.9%**	**51.1%**	**46.8%**	46.6%	52.9%	47.7%
£100k–£249k	**60.3%**	**58.7%**	**59.8%**	59.1%	58.6%	58.9%
£250k–£499k	**62.5%**	**61.5%**	**62.1%**	60.6%	60.7%	60.6%
£500k–£999k	**62.8%**	**58.8%**	**61.7%**	60.0%	58.2%	59.4%
£1m–£2.49m	**61.7%**	**51.9%**	**60.8%**	61.1%	48.7%	59.3%
> = £2.5m	**60.0%**	**43.7%**	**59.3%**	58.1%	44.7%	57.1%
Total	**58.6%**	**59.1%**	**58.8%**	56.9%	58.6%	57.5%

(1) LTV of the mortgage portfolio is defined as mortgage portfolio weighted by balance and indexed using the MIAC Acadametrics indices at a given date.

Forbearance

Forbearance is considered to take place when the Group grants concessions to assist customers who are experiencing, or who are about to experience, difficulties in meeting their financial commitments to the Group. The Group's forbearance policies and definitions comply with the guidance established by the European Banking Authority for financial reporting. Forbearance concessions include the granting of more favourable terms and conditions than those provided either at drawdown of the facility or which would not ordinarily be available to other customers with a similar risk profile. Forbearance parameters are regularly reviewed and refined as necessary to ensure they are consistent with the latest industry guidance and prevailing practice, as well as ensuring that they adequately capture and reflect the most recent customer behaviours and market conditions. The Group makes every effort to treat customers fairly and aligns its forbearance practices to that principle.

While forbearance alone is not necessarily an indicator of impaired status, it is a trigger for the review of the customer's credit profile and forbearance is only granted when there is a realistic prospect of the customer repaying all facilities in full. If there is any concern over future cash flows and the Group incurring a loss, then forborne loans will also be classified as impaired in accordance with the Group's impairment policy.

Exposures classified as forborne and performing at the date forbearance measures are granted, continue to be reported as subject to forbearance for a minimum period of two years from that date (the probation period). Exposures classified as forborne and which are non-performing when customers were granted forbearance cannot exit non-performing status for a minimum of 12 months from the date forbearance was granted, and cannot exit forbearance status for a further two years from the date of returning to performing status (three years in total).

The Group has identified a number of situations that in isolation are not considered to be forbearance:

- facilities that have been temporarily extended pending review and where no concession has been granted for reasons relating to the actual or apparent financial stress of a customer;
- a reduction in asset quality to a level where actual, or apparent, financial stress is not evident;
- where changes are made to the terms of a borrower's interest structure or repayment arrangement on a commercial basis; and
- late provision of financial information, in the absence of other indicators of financial difficulty, is not in all cases considered a non-commercial breach of non-financial covenants.

For both Retail and SME, where the Group has made a demand for repayment, the customer's facilities have been withdrawn or where a debt repayment process has been initiated, the exposure is classified as forborne if the debt is subject to any of the mentioned forbearance concessions.

Retail forbearance

The Group utilises various forbearance measures for retail customers, specific to the individual customer and their circumstances. Customers may potentially be subject to more than one forbearance strategy at any one time where this is considered to be the most appropriate course of action.

Debt management for mortgage customers in financial difficulty

To support customers who are encountering financial difficulties, cases are managed on an individual basis, with the circumstances of each customer considered separately and the action taken judged as being affordable and sustainable for the customer. Operationally, the provision and review of such assistance is controlled by various methods. These include the application of an appropriate policy framework, controls around the execution of policy, regular review of the different treatments to confirm that they remain appropriate, monitoring of customers' performance including the level of payments received, and management visibility of the nature and extent of assistance provided and the associated risk.

Help is provided through the Financial Care Team where tailored repayment programmes can be agreed. Customers are actively supported and referred to free money advice agencies when they have multiple credit facilities, including those at other lenders, that require restructuring.

One component of the Group's approach is to contact customers showing signs of financial difficulty to discuss their circumstances and offer solutions to prevent their accounts falling into arrears.

Risk report

Credit risk

The tables below summarise the level of forbearance in respect of the Group's mortgage portfolio at 30 September:

As at 30 September 2018 (audited)	Total Retail loans and advances subject to forbearance measures Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance on Retail loans and advances subject to forbearance measures Impairment allowance £m	Coverage %
Formal arrangements	**1,497**	**168**	**0.68**	**3.3**	**2.00**
Temporary arrangements	**1,275**	**161**	**0.66**	**2.3**	**1.45**
Interest-only conversion	**231**	**32**	**0.13**	**0.1**	**0.18**
Term extension	**150**	**12**	**0.05**	**0.1**	**0.48**
Other	**41**	**4**	**0.02**	**–**	**0.36**
Legal	**148**	**15**	**0.06**	**0.5**	**3.34**
	3,342	**392**	**1.60**	**6.3**	**1.61**

As at 30 September 2017 (audited)	Total Retail loans and advances subject to forbearance measures Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance on Retail loans and advances subject to forbearance measures Impairment allowance £m	Coverage %
Formal arrangements	1,614	164	0.69	3.9	2.43
Temporary arrangements	1,418	174	0.74	3.0	1.72
Interest-only conversion	202	30	0.13	0.2	0.56
Term extension	149	12	0.05	0.1	0.51
Other	29	2	0.01	–	0.61
Legal	167	16	0.07	0.9	5.66
	3,579	398	1.69	8.1	2.04

The Group also has a number of customers with interest-only mortgages past maturity, not subject to forbearance. The Group has formal processes embedded to proactively track and facilitate pre-maturity customer engagement to bring the cases to a formal conclusion, which is generally aimed to be achieved within six months after the loan has reached maturity. Complex cases can take longer than this to reach conclusion. At 30 September 2018, the Group had 117 (2017: 97) customers with interest-only mortgages not subject to forbearance and which were post six-month maturity with a total value of £19m (2017: £14m).

A further forbearance reserve of £4m (2017: £4m) is presently held within the overall collective provision. The effect of this on the above tables would be to increase the impairment allowance noted above to £10.3m (2017: £12.1m) and to increase overall coverage to 2.63% (2017: 3.05%). When all other avenues of resolution including forbearance have been explored, the Group will take steps to repossess and sell underlying collateral. In the year to 30 September 2018, there were 38 repossessions of which 16 were voluntary (2017: 50 including 13 voluntary).

Retail forbearance – unsecured consumer credit

The Group currently exercises limited forbearance strategies in relation to other types of consumer credit, including current accounts, unsecured loans and credit cards. The Group has assessed the total loan balances subject to forbearance on other types of consumer credit to be £12m at 30 September 2018 (2017: £11m), representing 1.02% of the unsecured Retail portfolio (2017: 1.02%).

Impairment provisions on forborne balances totalled £4.2m at 30 September 2018 (2017: £3.1m), providing overall coverage of 34.36% (2017: 27.18%).

SME lending

Credit quality of loans and advances

For SME lending, the Group has an internally developed credit rating system, as defined under the Group's credit risk management policy, which uses data drawn from a number of sources to assess the potential risk in lending to the Group's customers. This system assigns an indication of the PD for each customer and can be broadly mapped to external agencies rating scales. Impaired assets consist of SME lending and secured Retail lending where current circumstances indicate that losses of loan principal and/or interest may be incurred.

Description	eCRS[1]	PD
Senior investment grade	1 to 5	0 < 0.11
Investment grade	6 to 11	0.11 < 0.55
Sub-investment grade	12 to 23	0.55 < 99.99

(1) eCRS – electronic Customer Rating System.

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed by reference to the Group's standard credit rating system. The credit rating system is supported by a variety of financial analytics, combined with processed market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories and are derived in accordance with the Group's ratings policy.

The table below represents the credit quality of SME loans and advances that are neither past due nor impaired:

	Audited	
	2018 £m	2017 £m
Senior investment grade	**839**	946
Investment grade	**1,731**	1,807
Sub-investment grade	**4,367**	3,873
	6,937	6,626

Credit quality of loans held at fair value through profit and loss that are neither past due nor impaired:

	Audited	
	2018 £m	2017 £m
Senior investment grade	**1**	3
Investment grade	**157**	231
Sub-investment grade	**200**	237
	358	471

For Retail lending, the Group has developed specific credit rating systems for both origination of new lending and for ongoing customer and account management purposes. These systems assign risk estimates to all Retail lending and enable active management of customer exposures and portfolios.

SME forbearance

Forbearance is considered to exist for SME customers where one or more concessions are granted on a non-commercial basis. The Group reports SME forbearance at a customer level and at a value which incorporates all facilities and the related impairment allowance, irrespective of whether each individual facility is subject to forbearance. Authority to grant forbearance measures for SME customers is held by the Group's Strategic Business Services unit and is exercised, where appropriate, on the basis of detailed consideration of the customer's financial position and prospects.

Where a customer is part of a larger group, forbearance is exercised and reported across the Group at the individual entity level. Where modification of the terms and conditions of an exposure meeting the criteria for classification as forbearance results in derecognition of loans and advances from the balance sheet and the recognition of a new exposure, the new exposure shall be treated as forborne.

Risk report

Credit risk

The tables below summarise the total number of arrangements in place and the loan balances and impairment provisions associated with those arrangements.

As at 30 September 2018 (audited)	Total SME loans and advances subject to forbearance measures			Impairment allowance on SME loans and advances subject to forbearance measures	
	Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance £m	Coverage %
Term extension	**179**	**162**	**2.15**	**10.5**	**6.48**
Deferral of contracted capital repayments	**103**	**129**	**1.73**	**15.6**	**12.02**
Reduction in contracted interest rate	**2**	**1**	**0.01**	**–**	**4.05**
Alternative forms of payment	**4**	**25**	**0.33**	**7.5**	**30.46**
Debt forgiveness	**4**	**11**	**0.14**	**0.6**	**5.64**
Refinancing	**17**	**10**	**0.13**	**1.0**	**9.87**
Covenant breach/reset/waiver	**61**	**207**	**2.75**	**9.2**	**4.43**
	370	**545**	**7.24**	**44.4**	**8.14**

As at 30 September 2017 (audited)	Total SME loans and advances subject to forbearance measures			Impairment allowance on SME loans and advances subject to forbearance measures	
	Number of loans	Gross carrying amount £m	% of total portfolio	Impairment allowance £m	Coverage %
Term extension	206	190	2.58	12.8	6.71
Deferral of contracted capital repayments	109	141	1.91	20.4	14.47
Reduction in contracted interest rate	3	1	0.02	–	3.37
Alternative forms of payment	5	28	0.37	8.1	29.40
Debt forgiveness	3	11	0.15	1.4	12.70
Refinancing	19	33	0.44	4.4	13.41
Covenant breach/reset/waiver	50	155	2.11	8.1	5.24
	395	559	7.58	55.2	9.88

Included in other financial assets at fair value is a portfolio of loans that is included in the above table. The value of fair value loans subject to forbearance at 30 September 2018 is £15m (2017: £45m), representing 0.19% of the total SME portfolio (2017: 0.61%). Impairment allowances on these amounts totalled £2m (2017: £4m), a coverage of 11.66% (2017: 8.89%).

Other credit risks

The Group is exposed to credit risk on its other banking activities, which are subject to mitigation and monitoring. No provisions are currently held for these exposures.

The table below shows the maximum exposure to credit risk for the components of the balance sheet excluding loans and advances to customers and other financial assets at fair value. The maximum exposure is shown gross, before the effect of mitigation through use of master netting and collateral agreements. The table also shows the maximum amount of commitments from its banking operations.

Maximum exposure to credit risk (audited)

	2018 £m	2017 £m
Cash and balances with central banks (note 3.1)	**6,573**	6,937
Due from other banks	**836**	1,174
Financial assets available for sale (note 3.2)	**1,562**	2,076
Derivative financial assets (note 3.4)	**262**	282
	9,233	10,469
Contingent liabilities (note 5.1)	**119**	111
Other credit commitments (note 5.1)	**7,016**	8,408
Maximum credit risk exposure	**16,368**	18,988

£4.8bn of cash is held with the BoE. Due from other banks is all with senior investment grade counterparties. Available for sale financial assets and the credit rating of counterparties are discussed in note 3.2.

Offsetting of financial assets and liabilities

The Group does not have any financial assets or financial liabilities that are offset with the net amount presented on the balance sheet. This is because IAS 32 'Financial Instruments – Presentation' states that there should be both an enforceable right to set off and the intention either to settle on a net basis or to realise the asset and settle the liability simultaneously. Neither of these conditions are met by the Group. The table below illustrates the amounts for financial instruments that are covered by enforceable netting arrangements (i.e. offsetting agreements and any related financial collateral). The table excludes financial instruments not subject to offset and that are only subject to collateral arrangements (e.g. loans and advances).

The net amounts presented in the table are not intended to represent the Group's exposure to credit risk, as the Group will use a wide range of strategies to mitigate credit risk in addition to netting and collateral.

				Net amounts not offset on balance sheet		
2018 (audited)	**Gross amounts £m**	**Gross amounts offset on balance sheet £m**	**Net amounts presented on balance sheet[1] £m**	**Financial instruments £m**	**Cash collateral pledged/ received £m**	**Net amount £m**
Assets						
Derivative financial instruments[2]	**262**	**–**	**262**	**(99)**	**(26)**	**137**
Liabilities						
Derivative financial instruments[2]	**361**	**–**	**361**	**(99)**	**(234)**	**28**
Securities sold under repurchase agreement	**802**	**–**	**802**	**(802)**	**–**	**–**

				Net amounts not offset on balance sheet		
2017 (audited)	Gross amounts £m	Gross amounts offset on balance sheet £m	Net amounts presented on balance sheet[1] £m	Financial instruments £m	Cash collateral pledged/ received £m	Net amount £m
Assets						
Derivative financial instruments[2]	282	–	282	(72)	(21)	189
Liabilities						
Derivative financial instruments[2]	376	–	376	(72)	(203)	101
Securities sold under repurchase agreement	1,864	–	1,864	(1,864)	–	–

(1) Collateral amounts (cash and non-cash financial collateral) are reflected at their fair value; however, this amount is limited to the net balance sheet exposure in order to exclude any over collateralisation.
(2) Derivative financial instruments comprise both trading and hedging derivative assets and liabilities.

Derivative financial instrument contracts are typically subject to ISDA master netting agreements, as well as CSAs, where relevant, around collateral arrangements attached to those ISDA agreements, or derivative exchange or clearing counterparty agreements if contracts are settled via an exchange or clearing house. The amounts included in the Financial instruments column refer to amounts that are subject to relevant close out netting arrangements under a relevant ISDA agreement.

Risk report

Balance sheet and prudential regulation risks

Strong foundations supporting resilience and growth

A robust balance sheet position underpinned by the alignment of risk appetite to strategy and a proactive approach to addressing the impact of changing regulatory obligations.

Balance sheet risks in the financial services industry are highly regulated with ongoing changes in the regulatory environment expected to influence the risks and their management. The key risks include capital, liquidity and funding risks, market risk which in the case of the Group is non-traded market risk (incorporating interest rate and foreign exchange risks), pension risk and non-traded equity risk.

Risk appetite

The primary objective for the management of balance sheet risks is to maintain the risk profile within approved risk limits, to maintain the confidence of the Group's customers and other stakeholders. Balance sheet risks are also managed to protect current and future earnings from the impact of market volatility. The Group applies a prudent approach to balance sheet risks in order to safeguard the ongoing strength and resilience of the balance sheet.

Risk appetite is approved for balance sheet risks by the Board, with authority delegated to ALCO for subsequent implementation and monitoring. The Board has established a range of measures of risk appetite for capital including CET1, leverage and minimum holdings of capital. Measures for funding and liquidity risks consider the structure of the balance sheet and the Group's overall funding profile and Overall Liquidity Adequacy Rule (OLAR). The OLAR covers the Board's appetite in relation to regulatory liquidity requirements and also covers the need to maintain access to liquidity resources sufficient to accommodate outflows of funds in a range of stress scenarios over a three-month period.

The Group's participation in wholesale markets, along with its use of financial instruments, is to fund its banking activities and to manage the liquidity and interest rate risks arising from these activities. The Group establishes an appetite for these risks based on an overriding principle that the Group will not engage in proprietary risk taking.

Capital

Capital is held by the Group to protect its depositors, to cover inherent risks in a normal and stressed operating environment and to support the Group's strategy of sustainable growth. Capital risk is the risk that the Group has insufficient quantity or quality of capital to support its operations.

Measurement

The Group manages capital in accordance with prudential rules issued by the PRA and FCA, which implemented CRD IV legislation with effect from 1 January 2014. The Group's approach to Pillar 1 for the year ended 30 September 2018 was to use the standardised approaches to calculate RWAs. The standardised approaches are inherently conservative and the Group has been developing the capability to utilise IRB methods for the calculation of credit risk capital. A waiver to utilise IRB models was submitted to the PRA during 2017 and subsequently approved in October 2018 for its mortgage and SME/corporate portfolios.

A rigorous approach is taken to assess risks that are not adequately covered by Pillar 1, including interest rate risk and pension risk. The Group also undertakes a range of stress scenarios in order to test the impact on capital arising from severe yet plausible scenarios. These approaches to capital are thoroughly documented in the Group's ICAAP and this is subject to review, challenge and approval by the Board.

Capital buffers

The regulatory capital buffer framework is intended to ensure firms maintain a sufficient amount of capital above their regulatory minimum in order to withstand periods of stress. The UK is implementing the provisions on capital buffers outlined in the CRD to create combined capital buffers including a Capital Conservation Buffer (CCB); a Countercyclical Capital Buffer (CCyB); a Global Systemically Important Institution Buffer; and a Systemic Risk Buffer (SRB). In the UK, the CCB has been introduced with transitional provisions from 2016 (0.625%) to 2019 (2.5%).

CET1	LDR	LCR
10.5%	**115%**	**137%**
2017: 12.4%	2017: 115%	2017: 164%

The CCyB has been effective from 1 May 2014 and is dependent upon the BoE view of credit conditions in the economy. The CCyB was 0.5% of RWAs at 30 September 2018 with this rising to 1.00% in November 2018.

The Group's capital planning considers the impact of all relevant capital buffers.

The PRA's final rules on the approach to identifying other systemically important institutions (O-SII) were published in February 2016. In line with expectations, Clydesdale Bank PLC was not designated an O-SII. Similarly the Financial Policy Committee (FPC) issued its final framework for setting the SRB in May 2016. This confirmed that banks with total assets of less than £175bn (which includes the Group) will be subject to a 0% SRB.

Minimum requirement for own funds and eligible liabilities (MREL)

In November 2016, the BoE provided additional information on how MREL will be applied to firms that are subject to the use of resolution tools that the BoE would employ in the event of a firm entering resolution. From 1 January 2022, those firms, which include the Group, will be required to hold both their going concern requirements together with additional MREL of an amount equal to those going concern requirements. The timetable for meeting MREL has been extended to 2022 and the BoE will review calibration and transition by the end of 2020, before setting end-state MREL. Interim MREL has been established for the transitional period.

During 2018 the Group issued its second unsecured bond that, in addition to the Group's capital base, will contribute to meeting MREL requirements. This activity firmly established CYBG's name in the unsecured market with investors. The second bond takes total outstanding issuance to £0.8bn.

Monitoring

The capital plan is approved by the Board on an annual basis. The Group's ALCO monitors the capital plan and forecast positions on a monthly basis. This ensures that performance trends are appropriately reviewed and that there is transparency on the impact on capital ratios, risk appetite and the future outlook.

Mitigation

The Group's Capital Risk Policy Standard provides the framework for the manner in which capital is managed within the Group. The objectives of the policy standard are to efficiently manage the capital base to optimise shareholder returns while maintaining robust capital adequacy, meeting regulators' requirements, managing the rating agencies' assessment of the Group and ensuring that excessive leverage is not taken.

The Group is able to accumulate additional capital through the retention of profit over time, by cutting costs, by raising new equity via, for example, a rights issue or debt exchange, by reducing or cancelling distributions on capital instruments, and by raising AT1 and Tier 2 capital. The availability and cost of additional capital is dependent upon market conditions and perceptions at the time. The Group is also able to manage the demands for capital through management actions including adjusting lending strategy.

Capital optimisation remains a key strategic priority of the Group and a waiver application was submitted to the PRA during 2017 to utilise IRB models. Approval for the use of the IRB models for the mortgage and SME/corporate portfolios was subsequently obtained in October 2018.

Risk report

Balance sheet and prudential regulation risks

Capital position

The Group's capital position as at 30 September is summarised below:

Regulatory capital (unaudited)[1]

CET1 capital	2018 £m	2017 £m
Capital instruments	**89**	88
Retained earnings and other reserves	**2,637**	2,854
Regulatory adjustments and deductions		
Defined benefit pension fund assets[2]	**(138)**	(135)
Prudent valuation adjustment[3]	**(3)**	(4)
Intangible assets[4]	**(412)**	(339)
Deferred tax asset relying on future profitability[5]	**(99)**	(28)
Cash flow hedge reserve	**39**	1
	2,113	2,437
Tier 1 capital		
AT1 capital instruments	**450**	450
Total Tier 1 capital	**2,563**	2,887
Tier 2 capital		
Subordinated debt	**474**	473
Credit risk adjustments	**152**	154
Total Tier 2 capital	**626**	627
Total capital	**3,189**	3,514

(1) This table shows the capital position on a CRD IV 'fully loaded' basis.
(2) The defined benefit pension fund asset (net of deferred tax liabilities) does not qualify as capital for regulatory purposes.
(3) A prudent valuation adjustment is applied in respect of fair-valued instruments as required under regulatory capital rules.
(4) Intangible assets shall be deducted from capital for regulatory purposes.
(5) Under CRD IV, deferred tax assets that rely on future profitability are deducted from CET1 capital.

Reconciliation of statutory total equity to regulatory capital (unaudited)	2018 £m	2017 £m
Statutory total equity	**3,186**	3,402
Deductions from capital	**(553)**	(478)
Deferred tax asset relying on future profitability	**(99)**	(28)
Cash flow hedge reserve	**39**	1
Foreseeable AT1 dividends and charges	**(10)**	(10)
Regulatory Tier 1 capital	**2,563**	2,887

Regulatory capital flow of funds (unaudited)	CRD IV 2018 £m	CRD IV 2017 £m
CET1 capital		
CET1 capital at 1 October	**2,437**	2,397
Share capital: issued under employee share scheme	**1**	–
Retained earnings and other reserves (including structured entities)	**(217)**	181
Prudent valuation adjustment	**1**	3
Intangible assets	**(73)**	(83)
Deferred tax asset relying on future profitability	**(71)**	7
Defined benefit pension fund assets	**(3)**	(135)
Cash flow hedge reserve	**38**	67
CET1 capital at 30 September	**2,113**	2,437
Tier 1 capital		
Tier 1 capital at 1 October	**450**	450
Tier 1 capital at 30 September	**450**	450
Total Tier 1 capital	**2,563**	2,887
Tier 2 capital		
Tier 2 capital at 1 October	**627**	625
Credit risk adjustments	**(2)**	3
Other movements	**1**	(1)
Tier 2 capital at 30 September	**626**	627
Total capital	**3,189**	3,514

Minimum Pillar 1 capital requirements (unaudited)	2018 £m	2017 £m
Credit risk	**1,449**	1,420
Operational risk	**132**	130
Counterparty risk	**10**	11
Credit valuation adjustment	**17**	13
Tier 1 regulatory capital requirements	**1,608**	1,574

Risk report

Balance sheet and prudential regulation risks

RWA movements

RWA flow statement (unaudited)	2018 £m	2017 £m
RWAs at 1 October	**19,678**	19,029
Book size growth	**420**	529
Book quality deterioration/ (improvement)(1)	**4**	(28)
Methodology and policy	**–**	148
RWAs at 30 September	**20,102**	19,678

(1) The marginal deterioration in book quality in 2018 is primarily due to the continued diversification in the Liquid Asset Buffer.

Pillar 1 RWAs and capital requirements by business line (unaudited)

	At 30 September 2018			At 30 September 2017		
Capital requirements for calculating RWAs	**Capital required £m**	**RWA £m**	**Exposure £m**	Capital required £m	RWA £m	Exposure (restated) £m
Central governments or central banks	**–**	**1**	**11,361**	–	–	12,947
Regional governments or local authorities	**1**	**12**	**143**	2	19	156
Public sector entities	**–**	**2**	**155**	–	5	155
Multilateral development banks	**–**	**–**	**155**	–	–	205
Financial institutions	**11**	**136**	**630**	13	163	1,453
Corporates	**316**	**3,956**	**4,311**	273	3,418	3,791
Retail	**90**	**1,124**	**1,499**	72	905	1,207
Secured by mortgages on immovable property	**938**	**11,708**	**28,423**	961	12,001	28,203
Exposures in default	**45**	**562**	**465**	47	590	483
Collective investments undertakings	**–**	**1**	**1**	–	1	1
Equity exposures	**–**	**5**	**4**	–	5	3
Items associated with particularly high risk	**4**	**49**	**33**	3	40	26
Covered bonds	**5**	**61**	**615**	4	48	477
Other items	**39**	**487**	**715**	45	557	585
Total credit risk	**1,449**	**18,104**	**48,510**	1,420	17,752	49,692
Operational risk	**132**	**1,655**		130	1,621	
Counterparty risk	**10**	**125**		11	138	
Credit valuation adjustment	**17**	**218**		13	167	
	1,608	**20,102**		1,574	19,678	

The Exposure amounts disclosed above are post credit conversion factors and pre credit mitigation.

Capital position and CET1 (unaudited)	2018 £m	2017 £m
RWA(1)		
Retail mortgages	**9,002**	8,646
Business lending	**7,407**	7,359
Other retail lending	**981**	932
Other lending	**109**	148
Other(2)	**605**	667
Credit risk	**18,104**	17,752
Credit valuation adjustment	**218**	167
Operational risk	**1,655**	1,621
Counterparty risk	**125**	138
Total RWAs	**20,102**	19,678
Capital ratios		
CET1 ratio(3)	**10.5%**	12.4%
Tier 1 ratio	**12.7%**	14.7%
Total capital ratio	**15.9%**	17.9%

(1) RWAs are calculated under the standardised approach.
(2) The items included in the Other exposure class that attract a capital charge include items in the course of collection, cash in hand, fixed assets and deferred tax assets that are not deducted.
(3) CET1 capital is comprised of shares issued and related share premium, retained earnings and other reserves less specified regulatory adjustments.

The Group measures the amount of capital it requires and holds by applying the Capital Requirements Directive and Regulation (CRD IV) as implemented in the UK by the PRA and supplemented through additional regulation under the PRA Rulebook. The table below summarises the amount of capital in relation to RWAs the Group is currently required to hold, excluding any PRA Buffer. These ratios apply at the consolidated Group level.

Minimum requirements	As at 30 Sep 2018 CET1	Total Capital
Pillar 1(1)	4.5%	8.0%
Pillar 2A(2)	2.5%	4.5%
Individual capital guidance	**7.0%**	**12.5%**
Capital conservation buffer(3)	1.9%	1.9%
UK countercyclical capital buffer(4)	0.5%	0.5%
Total (excluding PRA buffer)(5)	**9.4%**	**14.9%**

(1) The minimum amount of total capital under Pillar 1 of the regulatory framework is determined as 8% of RWAs, of which at least 4.5% of RWAs is required to be covered by CET1 capital.
(2) Growth in RWAs at CYBG PLC has meant that at 30 September 2018 the Group's Pillar 2A total capital requirement, as set by the PRA's Individual Capital Guidance (ICG), has reduced from 4.6% to 4.5%. At least 56.25% of this needs to be met with CET1, equating to approximately 2.5% of RWAs.
(3) The capital conservation buffer (CCB) is being phased in over the period from 1 January 2016 to 1 January 2019. The CCB has been set at 2.5% of RWAs, with 1.875% applicable for 2018.
(4) The UK countercyclical capital buffer (CCyB) may be set between 0% and 2.5%. On 27 June 2018 the UK CCyB increased from 0% to 0.5% and the FPC reaffirmed that it expects to increase the UK CCyB from 0.5% to 1% from 28 November 2018. The FPC will conduct a comprehensive assessment of the resilience of the UK banking system in the 2018 stress test and review the adequacy of the 1.0% CCyB rate.
(5) The Group may be subject to a PRA buffer as set by the PRA but is not permitted to disclose the level of any buffer. A PRA buffer can consist of two components:
– A risk management and governance buffer that is set as a scalar of the Pillar 1 and Pillar 2A requirements.
– A buffer relating to the results of the BoE stress tests.

Underlying capital generation post AT1 distribution was 63bps (before the net impact of charges associated with the acquisition of Virgin Money, restructuring, separation from our former parent and legacy conduct issues). While the Group's CET1 ratio of 10.5% is below our guidance range of 12-13%, we continue to maintain a significant buffer to our transitional CRD IV minimum requirement of 9.4%, being a buffer of £221m.

Risk report

Balance sheet and prudential regulation risks

Pro forma IRB RWAs and Capital ratios

As announced on 11 October 2018, the Group has received IRB accreditation for both its mortgage and SME/corporate portfolios. The Group's estimated IRB RWAs and capital ratios, as at 30 September 2018, are as follows:

Capital position and CET1 (unaudited)	2018 £m
RWA	
Retail mortgages	**4,460**
Business lending	**6,598**
Other retail lending	**981**
Other lending	**109**
Other	**609**
Credit risk	**12,757**
Credit valuation adjustment	**218**
Operational risk	**1,655**
Counterparty risk	**125**
Total RWAs	**14,755**
Capital ratios	
CET1 ratio	**14.0%**
Tier 1 ratio	**17.1%**
Total capital ratio	**21.3%**

The Group's credit RWAs on an IRB basis would have been c.£4.5bn lower in the mortgage portfolio and c.£0.8bn lower in the SME/Corporate portfolio. These reductions would have resulted in a pro forma increase in CYBG's CET1 ratio of approximately 350 basis points to c. 14.0% as at 30 September 2018.

The Basel Committee published their final Basel III framework in December 2017. A key objective of the revisions is to reduce excessive variability of current RWAs and improve the comparability of banks' capital ratios. Implementation dates range from 2022 to 2027 and the Committee has introduced transitional arrangements to ensure an orderly and timely implementation. The Group's initial analysis suggests that the new requirements will not have a material impact on the total amount of capital it is required to hold.

Dividend

As announced in the Strategic report the Board has recommended a 3.1p per share dividend. The dividend would equate to approximately £44m of CET1 (equivalent to 22bps of CET1 based on RWAs as at 30 September 2018).

Leverage

Leverage ratio (unaudited)	2018 £m	2017 £m
Total Tier 1 capital for the leverage ratio		
Total CET1 capital	**2,113**	2,437
AT1 capital	**450**	450
Total Tier 1	**2,563**	2,887
Exposures for the leverage ratio		
Total assets as per published financial statements	**43,456**	43,231
Adjustment for off-balance sheet items	**1,763**	2,019
Adjustment for derivative financial instruments	**(134)**	(228)
Adjustment for securities financing transactions (SFTs)	**1,468**	1,461
Other adjustments	**(613)**	(505)
Leverage ratio exposure	**45,940**	45,978
CRD IV leverage ratio	**5.6%**	6.3%
UK leverage ratio(1)	**6.5%**	7.4%

(1) The Group's leverage ratio on a modified basis, excluding qualifying central bank claims from the exposure measure in accordance with the policy statement issued by the PRA in October 2017. The Group is currently excluded from the full reporting requirements of the UK leverage ratio framework.

The leverage ratio is monitored against a Board set RAS with the responsibility for managing the ratio delegated to ALCO, which monitors it on a monthly basis.

The leverage ratio is the ratio of Tier 1 capital to total exposure, defined as:

- capital: Tier 1 capital defined according to CRD IV on an end point basis (assuming the full impact of CRD IV requirements on Tier 1 capital were in force with no transitional provisions); and
- exposures: total on- and off-balance sheet exposures (subject to credit conversion factors) as defined in the delegated act amending CRR article 429 (Calculation of the Leverage Ratio), which includes deductions applied to Tier 1 capital.

Other regulatory adjustments consist of adjustments that are required under CRD IV to be deducted from Tier 1 capital. The removal of these from the exposure measure ensures consistency is maintained between the capital and exposure components of the ratio. The Group's leverage ratio is 5.6% which exceeds the Basel Committee's proposed minimum of 3%, applicable from 2018.

The UK leverage ratio framework, which came into force on 1 January 2016, is relevant to PRA regulated banks and building societies with consolidated retail deposits equal to or greater than £50bn. As at 30 September 2018 the Group was currently excluded from these requirements. On 3 October 2017, the PRA published a policy statement – 'UK Leverage Ratio treatment of claims on central banks'. The PRA Rulebook has been amended to:

- align with its July 2016 modification by consent to exclude central bank claims matched by deposits in the same currency and of identical or longer maturity from the definition of the total leverage exposure measure in the UK leverage ratio framework;
- increase the minimum leverage ratio requirement from 3% to 3.25% of total exposures; and
- align the UK leverage ratio reporting and disclosure requirements to the proposed definition of the total exposure measure and 3.25% minimum leverage ratio requirement.

If these modifications are applied to the Group, this results in an increase in the leverage ratio from 5.6% under CRD IV to 6.5% on the PRA modified basis as a result of the Group's significant exposures to central banks within its liquid asset portfolio and Note cover.

On 14 November 2018, the PRA published a policy statement – 'UK leverage ratio: Applying the framework to systemic ring-fenced bodies and reflecting the systemic risk buffer', confirming that from 1 January 2019 the UK leverage ratio framework will apply on a sub-consolidated basis to ring-fenced bodies in scope.

The Group's pro forma CRD IV leverage ratio, including the estimated impact of IRB accreditation at CYBG PLC, at 30 September 2018 was 5.5%.

Impact of acquisition of Virgin Money

Following the successful completion of the acquisition of Virgin Money the estimated Combined Group's new total capital requirement, including the estimated impact of IRB accreditation at CYBG PLC as described above, was set by the PRA as follows (excluding any PRA buffer):

Minimum requirements (1)	**CET1**	**Total Capital**
Pillar 1	4.5%	8.0%
Pillar 2A	3.6%	6.4%
Total capital requirement	**8.1%**	**14.4%**
Capital conservation buffer	1.9%	1.9%
UK countercyclical capital buffer	0.5%	0.5%
Total (excluding PRA buffer)	**10.5%**	**16.8%**

(1) Estimated Combined Group capital ratios have been calculated by adding the Risk Weighted Assets of CYBG PLC and Virgin Money at 30 September 2018 and applying the PRA's requirements which applied from 15 October 2018.

The increase in the percentage Pillar 2A requirement incorporates the reduction in RWAs as a result of IRB accreditation at CYBG PLC as described above. Furthermore, this component also reflects perceived risks relating to the integration of the two businesses. The Group expects that this will no longer be required once integration is complete. For comparison, the Pillar 2A total capital requirements for CB Solo Consolidated and Virgin Money are not impacted by this risk and were 5.7% and 5.4% respectively (on a post IRB basis).

Risk report

Balance sheet and prudential regulation risks

The estimated Combined Group's capital ratios, including the estimated impact of IRB accreditation at CYBG PLC, as described above, at 30 September were well in excess of the CRD IV requirements as follows:

Capital Ratio(1)	Estimated Combined Group
CET1	15.2%
Total Capital	21.6%
Leverage Ratio (2)	4.7%

(1) The unaudited estimated Combined Group financial information, which has been produced for illustrative purposes only, by its nature addresses a hypothetical situation and, therefore, does not represent the CYBG Group's actual financial position or results. Estimated Combined Group capital ratios are calculated using the weighted average of the requirements of CYBG PLC and Virgin Money based on their respective Risk Weighted Assets and Capital held at 30 September 2018. Capital held for the estimated Combined Group has been adjusted for the value of consideration of shares issued at the scheme record date. The Risk Weighted Assets and capital held for CYBG PLC have been adjusted to incorporate the estimated impact of IRB accreditation that was received in October 2018. The figures exclude any impact of acquisition accounting that will be completed during Q1 FY19.

(2) The unaudited estimated Combined Group financial information, which has been produced for illustrative purposes only, by its nature addresses a hypothetical situation and, therefore, does not represent the CYBG Group's actual financial position or results. Estimated Combined Group leverage ratio is calculated using the weighted average of the requirements of CYBG PLC and Virgin Money based on their respective Total Leverage Exposures and Tier 1 Capital held at 30 September 2018. Capital held for the estimated Combined Group has been adjusted for the value of consideration of shares issued at the scheme record date. Capital held for CYBG PLC has been adjusted to incorporate the estimated impact of IRB accreditation that was received in October 2018. The figures exclude any impact of acquisition accounting that will be completed during Q1 FY19.

The BoE has not yet advised the Combined Group's Final Minimum Requirement for Own Funds and Eligible Liabilities (MREL). The Group continues to expect that from 1 January 2020 until 31 December 2021 the Group will be required to hold 18% of risk-weighted assets in the form of MREL. From 1 January 2022, the Group will be subject to an end state MREL of two times Pillar 1 and Pillar 2A capital.

Funding and liquidity risk

Funding risk relates to the impact on the Group's strategy of being unable to raise funds from customers and the wholesale markets of sufficient quantity and of appropriate mix and tenor. An inability to raise sufficient funds may lead to a reduction in lending growth or a requirement to raise the price paid for deposits, both outcomes having an adverse effect on shareholder value. Where funding risk manifests itself in an adverse effect on mix and tenor, for example, a high proportion of short-term wholesale deposits, there is an increased liquidity risk to the Group.

Liquidity risk is the risk that the Group is unable to meet its current and future financial obligations as they fall due at acceptable cost. These obligations include the repayment of deposits on demand or at their contractual maturity dates, the repayment of borrowings and loan capital as they mature, the payment of operating expenses and tax, the payment of dividends and the ability to fund new and existing loan commitments.

Risk assessment

The framework for the Group's approach to funding risk leads to the development of a Group funding plan that is subject to approval by the Board and is consistent with risk appetite and the Group's strategic objectives. The development of the Group's funding plan is informed by the requirements of the Group's Balance Sheet Risk Policy Standards.

Liquidity risk exposures are subject to assessment under both regulatory and internal requirements. Exposures relate to the outflow of funds under a series of stress scenarios less the impact of inflows from assets, liquidation of high-quality liquid assets or through other actions instigated by the Group. Liquidity within the Group is managed in accordance with the ILAAP that is approved by the Board.

The Treasury function is responsible for the development and execution of strategy subject to oversight from the Risk Management function. In relation to funding and liquidity risk, the primary management committee is ALCO.

The Group continues to maintain its strong funding and liquidity position and seeks to achieve an appropriate balance between profitability, liquidity risk and capital optimisation. Funding is predominantly provided by Retail and SME customers and this is supported by medium-term secured funding issuance (e.g. the Group's Lanark securitisation programme), its Regulated Covered Bond platform and unsecured medium-term notes (the Group also raised funds through the TFS prior to the Scheme's closure to new drawings in early 2018). These funding programmes are a source of strength for the Group and leverage the Group's high-quality mortgage book as a source of collateral for secured funding.

Monitoring

Funding and Liquidity risks are subject to a range of measures contained within the Group's RAS and a series of limits agreed by ALCO. These measures provide a view of risks both under normal and stressed conditions with a focus on: cash outflows and inflows under stress; concentration risks; refinancing risks; readiness of mitigating action; and provide a short and long-term view of risks. An early warning framework is also operated to ensure quick escalation of any issues (see Contingency Funding Plan section below).

The Group operates a Funds Transfer Pricing (FTP) system. A key purpose of FTP is to ensure that liquidity risk is a factor in the pricing of loans and deposits.

Mitigation
The Group has several sources of funding which are well diversified in terms of the type of instrument and product, counterparty, term structure and market. Refinancing risks are carefully managed and are subject to controls overseen by ALCO.

The Group holds a portfolio of High Quality Liquid Assets (HQLA) that can be utilised to raise funding in times of stress. The size of the HQLA portfolio is calibrated based on a view of potential outflows under both systemic and idiosyncratic stress events. In addition, the Group can use the repo market to generate funds and can also participate in BoE operations through the Sterling Monetary Framework.

Contingency Funding Plan
A Contingency Funding Plan has been established for management of an escalated liquidity requirement if the Group experiences either restricted access to wholesale funding or a significant increase in the withdrawal of funds. The plan identifies triggers for escalation, details the action required, allocates the key tasks to individuals, provides a timeframe and defines a management committee to manage the action plan.

Sources of funding (audited)
The table below provides an overview of the Group's sources of funding as at 30 September.

	2018 £m	2017 £m
Total assets	**43,456**	43,231
Less: other liabilities	**(3,271)**	(3,509)
Funding requirement	**40,185**	39,722
Funded by:		
Due to customers	**28,904**	27,718
Due to other banks	**3,122**	3,817
of which:		
Securities sold under agreements to repurchase	**802**	1,864
Transaction balances with other banks	**29**	21
Deposits with other banks	**37**	31
Secured loans	**2,254**	1,901
Debt securities in issue	**4,973**	4,785
Equity	**3,186**	3,402
Total funding	**40,185**	39,722

The Group's funding objectives are to prudently manage the sources and tenor of funds in order to provide a sound base from which to support sustainable customer growth. At 30 September 2018, the Group had a funding requirement of £40,185m (2017: £39,722m) with the primary funding requirement being to support loans and advances to customers.

Due to customers
The majority of the Group's funding requirement was met by customer deposits of £28,904m (2017: £27,718m). Customer deposits are comprised of non-interest bearing demand deposits, interest bearing deposits and term deposits from a range of sources including Retail, SME and other corporate customers. The increase of £1,186m in 2018 was spread across interest bearing deposits £765m, term deposits £235m and non-interest bearing deposits £208m.

Due to other banks and debt securities in issue (wholesale funding)
Due to other banks of £3,122m (2017: £3,817m) is primarily comprised of: £802m of securities sold under agreement to repurchase; and £2,254m of secured loans.

Debt securities in issue of £4,973m (2017: £4,785m) was comprised of: £2,956m of residential mortgage-backed securities (RMBS) issued through the Group's Lanark programme; £742m of regulated covered bonds; £796m of senior debt; and £479m of subordinated debt.

Equity
Equity of £3,186m (2017: £3,402m) was also used to meet the Group's funding requirement. Equity is comprised of ordinary share capital, retained earnings, other equity investments and a number of other reserves. For full details on equity refer to section 4 of the Notes to the consolidated financial statements.

Risk report

Balance sheet and prudential regulation risks

External credit ratings

The Group's long-term credit ratings are summarised below:

	Outlook as at	As at	
	30 Sep 2018[1]	30 Sep 2018	30 Sep 2017
CYBG PLC			
Fitch	Stable	BBB+	BBB+
Standard & Poor's	Stable	BBB-	BBB-
Clydesdale Bank PLC			
Fitch	Stable	BBB+	BBB+
Standard & Poor's	Stable	BBB+	BBB+
Moody's[2]	On Review	Baa1	Baa2

(1) For detailed background on the latest credit opinions, by S&P and Fitch, please refer to the respective rating agency websites.
(2) Long-term deposit rating.

On 7 December 2017, Moody's upgraded the long-term deposit rating of Clydesdale Bank PLC by one notch to Baa1. This reflected Moody's view on the improvement in the Bank's management and risk and compliance frameworks, together with the delivery of the strategic plan and return to profitability. As part of the same rating action, Moody's revised the outlook on Clydesdale Bank PLC's long-term deposit rating to 'positive' in anticipation of ongoing senior unsecured issuance from CYBG PLC to meet MREL.

In November 2017, S&P revised their view of UK economic risk for the UK banking sector, which led to the outlooks for Clydesdale Bank PLC and CYBG PLC being revised from negative to stable. On 23 March 2018, S&P affirmed the ratings of Clydesdale Bank PLC and CYBG PLC with a stable outlook.

In June 2018, following the announcement of the Group's offer for Virgin Money, all three rating agencies released updates relating to the Group Baseline Credit Assessment. S&P and Fitch affirmed the Group's rating and outlook whilst Moody's placed Clydesdale Bank PLC's Adjusted Baseline Credit Assessment of Baa2, on review for upgrade, and its long-term Deposit Rating of Baa1, on review for downgrade. At the same time, Moody's placed Virgin Money's Baa2 long-term local-currency deposit ratings and Baa2 long-term issuer ratings on review for upgrade, as well as its Baa2 Baseline Credit Assessment and adjusted Baseline Credit Assessment.

Moody's noted that "The review for upgrade on both banks' Baseline Credit Assessments is driven by (i) the substantial potential for cost savings; (ii) the two banks' complementary business mixes, providing new revenue opportunities; and (iii) Moody's expectations that the combined entity will retain a strong capital position and stable funding profile."

As at 26 November 2018, there have been no changes to the enlarged Group's long-term credit ratings or outlooks since the report date.

Additional collateral to be provided in the event of a notch downgrade

The Group monitors the movements in its credit ratings and the related requirement to post collateral for payment systems and clearing houses. These figures are not considered material compared to the volume of unencumbered liquid assets.

Liquid assets

The quantity and quality of the Group's liquid assets are calibrated to the Board's view of liquidity risk appetite and remain at a prudent level above regulatory requirements. The Group was compliant with all internal and regulatory liquidity metrics at 30 September 2018.

The liquid asset portfolio provides a buffer against sudden and potentially sharp outflows of funds and liquid assets must therefore be of a high quality so they can be realised for cash and cannot be encumbered for any other purpose (e.g. to provide collateral for payments systems). Details on encumbered assets are provided in the following section.

The liquid asset portfolio is primarily comprised of cash at the BoE, UK Government Securities (Gilts) and listed securities (e.g. bonds issued by supra-nationals and AAA rated covered bonds).

Liquid asset portfolio	2018 £m	2017 £m
Cash and balances with central banks	**3,942**	4,367
UK government treasury bills and gilts	**513**	1,129
Other debt securities	**943**	829
Total	**5,398**	6,325

The volume of Gilts held by the Bank reduced over 2018 as shorter dated securities were sold or matured. Before investing in any security an assessment is completed for both the credit quality and the treatment for liquidity purposes. ALCO oversees the composition of the liquid asset portfolio.

Further information can be found in sections 3.1 and 3.2 of the Notes to the consolidated financial statements (Section 3.1 Cash and balances with central banks of £6,573m include £2,485m of assets that are encumbered to support issuance of Scottish bank notes and to support payments systems and £75m of mandatory central bank deposits; section 3.2 Financial assets available for sale of £1,562m includes £595m of UK Government Treasury Bills and Gilts, of which £36m is encumbered to support derivatives clearing and £46m is encumbered to support payment systems, and £943m of Other debt securities (listed securities).

Encumbered assets by asset category

Examples of reasons for asset encumbrance include, among others, supporting the Group's secured funding programmes to provide stable term funding to the Group, use of assets as collateral for payments systems in order to support customer's transactional activity, and providing security for the Group's issuance of Scottish bank notes. The Group monitors the level of asset encumbrance to ensure an appropriate balance is maintained.

Encumbered assets by asset category (audited)

	Assets encumbered with non-central bank counterparties					Other assets				
						Assets not positioned at the central bank				
September 2018	Covered bonds £m	Securi-tisations £m	Other £m	Total £m	Positioned at the central bank (including encumbered) £m	Readily available for encumbrance £m	Other assets capable of being encumbered £m	Cannot be encumbered £m	Total £m	**Total £m**
Cash and balances with central banks	–	–	–	–	2,809	3,764	–	–	6,573	**6,573**
Due from other banks	161	299	306	766	–	–	70	–	70	**836**
Investments – available for sale	–	–	36	36	46	1,468	5	7	1,526	**1,562**
Other financial assets	–	–	–	–	–	–	362	–	362	**362**
Derivatives	–	–	–	–	–	–	–	262	262	**262**
Loans and advances to customers	1,393	5,243	–	6,636	6,940	5,016	11,322	2,830	26,108	**32,744**
Intangible assets	–	–	–	–	–	–	–	412	412	**412**
Deferred tax assets	–	–	–	–	–	–	–	206	206	**206**
Other assets	–	–	–	–	–	–	95	404	499	**499**
Total assets	1,554	5,542	342	7,438	9,795	10,248	11,854	4,121	36,018	**43,456**

	Assets encumbered with non-central bank counterparties					Other assets				
						Assets not positioned at the central bank				
September 2017	Covered bonds £m	Securi-tisations £m	Other £m	Total £m	Positioned at the central bank (including encumbered) £m	Readily available for encumbrance £m	Other assets capable of being encumbered £m	Cannot be encumbered £m	Total £m	Total £m
Cash and balances with central banks	–	–	–	–	2,850	4,087	–	–	6,937	6,937
Due from other banks	46	358	338	742	–	–	432	–	432	1,174
Investments – available for sale	–	–	–	–	95	1,971	–	10	2,076	2,076
Other financial assets	–	–	–	–	–	–	477	–	477	477
Derivatives	–	–	–	–	–	–	–	282	282	282
Loans and advances to customers	1,347	5,841	–	7,188	6,294	5,940	8,906	2,965	24,105	31,293
Intangible assets	–	–	–	–	–	–	–	339	339	339
Deferred tax assets	–	–	–	–	–	–	–	154	154	154
Other assets	–	–	–	–	–	–	100	399	499	499
Total assets	1,393	6,199	338	7,930	9,239	11,998	9,915	4,149	35,301	43,231

Risk report

Balance sheet and prudential regulation risks

Assets and liabilities by maturity

The following tables represent a breakdown of the Group's balance sheet, according to the assets and liabilities contractual maturity. Many of the longer-term monetary assets are variable rate products, with behavioural maturities shorter than the contractual terms. Accordingly, this information is not relied upon by the Group in its management of interest rate risk. The Group has disclosed certain term facilities within loans and advances to customers with a revolving element at the maturity of the facility as this best reflects their contractual maturity.

2018 (audited)	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	**Total £m**
Assets							
Cash and balances with central banks	4,917	–	–	–	–	1,656	**6,573**
Due from other banks	307	529	–	–	–	–	**836**
Financial assets available for sale	–	5	79	658	810	10	**1,562**
Other financial assets at fair value	–	8	36	144	174	–	**362**
Derivative financial instruments	–	13	26	164	59	–	**262**
Loans and advances to customers	1,093	1,196	983	4,623	24,468	381	**32,744**
Due from customers on acceptances	–	4	–	–	–	–	**4**
All other assets	–	128	62	–	–	923	**1,113**
Total assets	6,317	1,883	1,186	5,589	25,511	2,970	**43,456**
Liabilities							
Due to other banks	53	519	300	2,250	–	–	**3,122**
Other financial liabilities at fair value	–	2	6	7	–	–	**15**
Derivative financial instruments	–	10	19	133	199	–	**361**
Due to customers	23,142	981	1,787	2,994	–	–	**28,904**
Liabilities on acceptances	–	4	–	–	–	–	**4**
Debt securities in issue	–	359	631	2,464	1,519	–	**4,973**
All other liabilities	2,254	89	109	–	–	439	**2,891**
Total liabilities	25,449	1,964	2,852	7,848	1,718	439	**40,270**
Off-balance sheet items							
Contingent liabilities	–	26	36	12	45	–	**119**
Other credit commitments	7,016	–	–	–	–	–	**7,016**
Total off-balance sheet items	7,016	26	36	12	45	–	**7,135**

2017 (audited)	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Assets							
Cash and balances with central banks	5,430	–	–	–	–	1,507	6,937
Due from other banks	701	473	–	–	–	–	1,174
Financial assets available for sale	–	3	256	1,334	473	10	2,076
Other financial assets at fair value	–	4	16	225	232	–	477
Derivative financial instruments	–	19	72	116	75	–	282
Loans and advances to customers	1,783	292	764	5,048	23,010	396	31,293
Due from customers on acceptances	–	4	–	–	–	–	4
All other assets	–	203	49	–	–	736	988
Total assets	7,914	998	1,157	6,723	23,790	2,649	43,231
Liabilities							
Due to other banks	45	1,172	700	1,900	–	–	3,817
Other financial liabilities at fair value	–	–	–	26	–	–	26
Derivative financial instruments	–	21	31	132	192	–	376
Due to customers	22,185	917	2,220	2,396	–	–	27,718
Liabilities on acceptances	–	4	–	–	–	–	4
Debt securities in issue	–	620	503	2,613	1,049	–	4,785
All other liabilities	2,197	174	–	–	–	732	3,103
Total liabilities	24,427	2,908	3,454	7,067	1,241	732	39,829
Off-balance sheet items							
Contingent liabilities	–	19	40	10	42	–	111
Other credit commitments	8,408	–	–	–	–	–	8,408
Total off-balance sheet items	8,408	19	40	10	42	–	8,519

Risk report

Balance sheet and prudential regulation risks

Cash flows payable under financial liabilities by contractual maturity

2018 (audited)	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	**Total £m**
Due to other banks	53	519	314	2,282	–	–	**3,168**
Other financial liabilities at fair value	–	3	6	8	–	–	**17**
Trading derivative financial instruments	–	13	31	40	17	–	**101**
Due to customers	23,143	981	1,788	2,995	–	–	**28,907**
Liabilities on acceptances	–	4	–	–	–	–	**4**
Debt securities in issue	–	364	696	2,746	1,665	–	**5,471**
All other financial liabilities	2,254	89	109	–	–	439	**2,891**
Hedging derivative liabilities							**–**
Contractual amounts payable	–	8	42	253	235	–	**538**
Total liabilities	25,450	1,981	2,986	8,324	1,917	439	**41,097**

2017 (audited)	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Due to other banks	44	1,173	708	1,912	–	–	3,837
Other financial liabilities at fair value	–	–	1	27	–	–	28
Trading derivative financial instruments	–	26	36	79	28	–	169
Due to customers	22,185	918	2,220	2,397	–	–	27,720
Liabilities on acceptances	–	4	–	–	–	–	4
Debt securities in issue	32	624	554	2,841	1,195	–	5,246
All other financial liabilities	2,197	174	–	–	–	732	3,103
Hedging derivative liabilities							
Contractual amounts payable	–	6	39	225	194	–	464
Total liabilities	24,458	2,925	3,558	7,481	1,417	732	40,571

The balances in the cash flow tables above will not agree directly to the balances in the consolidated balance sheet as the table incorporates all cash flows, on an undiscounted basis, related to both principal as well as those associated with all future coupon payments.

Market risk

Market risk is the risk associated with adverse changes in the fair value, or accrual income and expense, of assets and liabilities held by the Group as a result of movements in market factors such as interest rates, foreign exchange rates, volatility and credit spreads. The Group's balance sheet is predominantly UK based and is denominated in GBP, therefore foreign exchange risk is not a major part of the Group's risk profile.

Structural interest rate risk comprises the sensitivity of the Group's current and future net interest income and economic value to movements in market interest rates. The major contributors to interest rate risk are:

- the investment of non-interest bearing deposits and equity into interest-bearing assets;
- the mismatch between repricing dates of interest-bearing assets and liabilities;
- basis risk, for example, the inability of the pricing 'basis' for customer asset and liability products to be replicated in the financial markets or the risk arising from changing relationships between different interest rate yield curves; and
- customer optionality, e.g. the right to repay borrowing in advance of contract maturity dates.

Exposures

The focus of the Group's activity is to provide high-quality banking services to its customers. These services include the provision of foreign exchange products and derivative products to enable customers to manage risks within their businesses. As a result of these activities, the Group may be exposed to forms of market risk that would arise from movements in price on these products. Controls include the hedging of these products as and when they arise.

Measurement

Interest rate risk in the banking book (IRRBB) is measured, monitored, and managed from both an internal management and regulatory perspective. The RMF incorporates both market valuation and earnings-based approaches. In accordance with the Group IRRBB Policy Standard risk measurement techniques include: basis point sensitivity value at risk (VaR), earnings at risk (EaR), interest rate risk stress testing, repricing analysis, cash flow analysis, and scenario analysis.

The key features of the internal interest rate risk management model are:

- the use of basis point sensitivity analysis;
- VaR and EaR are measured on a statistical basis: 99% confidence level with appropriate holding periods depending on varying risk types;
- historical simulation approach utilising instantaneous interest rate shocks including parallel rate movements and twists in the yield curve to explore risks around exposures to movements in short- or long-term interest rates;
- static balance sheet (i.e. any new business is assumed to be matched, hedged or subject to immediate repricing);
- investment term for capital is modelled with a benchmark term agreed by ALCO;
- investment term for core non-interest bearing assets and liabilities is modelled on a behavioural basis with a benchmark term agreed by ALCO; and
- assumptions covering the behavioural life of products and customer behaviour for optionality are reviewed and approved by ALCO.

Foreign exchange risk is assessed based on the absolute exposure in each currency.

Risk report

Balance sheet and prudential regulation risks

Mitigation measures

Market risks are overseen by ALCO with delegation for day-to-day management given to Treasury. Treasury use a number of techniques and products to manage market risks including interest rate swaps, cash flow netting and foreign exchange. Basis risk is managed through a combination of wholesale market basis risk management products, pricing strategies and product innovation.

Fair value hedges

The Group hedges part of its existing interest rate risk, resulting from potential movements in the fair value of fixed rate assets and liabilities. The fair value of these swaps is disclosed in note 3.18. There were no transactions for which fair value hedge accounting had to be discontinued in the year.

Cash flow hedges

The Group hedges a portion of the variability in future cash flows attributable to interest rate and foreign currency risk. The interest and foreign currency risk arise from variable interest rate assets and liabilities which are hedged using cross currency and interest rate swaps, and material non-GBP denominated assets which are hedged using foreign exchange forward contracts. There were no transactions for which cash flow hedge accounting had to be discontinued in the period as a result of the highly probable cash flows no longer being expected to occur. The fair value of derivatives is disclosed in note 3.18.

Monitoring

Model parameters and assumptions are reviewed and updated on at least an annual basis. Material changes require the approval of ALCO. Oversight of market risk is conducted by the Group's balance sheet and liquidity risk oversight team that is independent of the Treasury function. The Board and Executive Risk Committee, through ALCO's oversight, monitors risk to ensure it remains within approved policy limits and Board requirements.

The VaR and EaR calculation parameters were changed effective from 31 March 2018 onwards. The changes improved the modelling and measurement and did not represent a change in the Group's risk appetite for Interest Rate Risk.

The changes consisted of three main elements:

1) changes to the modelling methodology of rate movements in a low rate environment;

2) history set revised from eight years to two years so that the measure is more responsive to recent rate movements; and

3) revisions to assumptions for interest rate yield curves used for valuing liquid asset securities to better capture asset swap spread risk.

The reported values for the first five months have been compared to the 2017 disclosures which were calculated on the same basis:

Interest rate risk (audited)

	Value at risk		Earnings at risk	
5 months to 28 February 2018	**2018 £m**	2017 £m	**2018 £m**	2017 £m
As at 30 September	**n/a**	25	**n/a**	4
Average value during the year	**26**	23	**5**	2
Minimum value during the year	**13**	15	**4**	1
Maximum value during the year	**36**	36	**7**	4

	Value at risk		Earnings at risk	
7 months to 30 September 2018	**2018 £m**	2017 £m	**2018 £m**	2017 £m
As at 30 September	**16**	n/a	**4**	n/a
Average value during the year	**11**	n/a	**4**	n/a
Minimum value during the year	**9**	n/a	**3**	n/a
Maximum value during the year	**16**	n/a	**5**	n/a

Principal financial assets and liabilities

The following table shows the Group's principal financial assets and liabilities and the main balance sheet risk types they are exposed to:

	2018 £m	Liquidity risk	Interest rate risk	Foreign exchange risk	Credit risk
Assets					
Cash and balances with central banks	**6,573**				●
Financial assets available for sale	**1,562**	●	●		●
Loans and advances to customers	**32,744**	●	●	●	●
Derivative financial instruments	**262**	●	●	●	●
Other financial assets at fair value	**362**	●	●		●
Liabilities					
Due to customers	**28,904**	●	●	●	
Due to other banks	**3,122**	●	●	●	
Derivative financial instruments	**361**	●	●	●	
Other financial liabilities at fair value	**15**	●	●		
Debt securities in issue	**4,973**	●	●	●	

	2017 £m	Liquidity risk	Interest rate risk	Foreign exchange risk	Credit risk
Assets					
Cash and balances with central banks	6,937				●
Financial assets available for sale	2,076	●	●		●
Loans and advances to customers	31,293	●	●	●	●
Derivative financial instruments	282	●	●	●	●
Other financial assets at fair value	477	●	●		●
Liabilities					
Due to customers	27,718	●	●	●	
Due to other banks	3,817	●	●	●	
Derivative financial instruments	376	●	●	●	
Other financial liabilities at fair value	26	●	●		
Debt securities in issue	4,785	●	●	●	

Foreign currency assets and liabilities split by type

The Group does not incur material foreign currency exposure.

Risk report

Balance sheet and prudential regulation risks

Repricing periods of assets and liabilities by asset/liability category

The following table shows the repricing periods of the Group's assets and liabilities as assessed by the Group. This repricing takes account of behavioural assumptions where material and the Group's policy to hedge capital in accordance with a benchmark term agreed by ALCO in order to reduce variability in net interest income.

Items are allocated to time buckets in the table below by reference to the earlier of the next contractual interest rate repricing date and the residual maturity date.

2018 (unaudited)	Overnight £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Non-interest bearing £m	Total £m
Assets							
Cash and balances with central banks	6,374	10	30	159	–	–	**6,573**
Due from other banks	835	1	–	–	–	–	**836**
Financial assets available for sale	189	393	–	300	680	–	**1,562**
Other financial assets at fair value	362	–	–	–	–	–	**362**
Loans and advances to customers	8,389	4,778	6,299	12,997	433	(152)	**32,744**
Other assets	–	–	–	–	–	1,379	**1,379**
Total assets	16,149	5,182	6,329	13,456	1,113	1,227	**43,456**
Liabilities							
Due to other banks	3,121	–	1	–	–	–	**3,122**
Due to related entities	–	–	–	–	–	–	**–**
Due to customers	11,495	1,281	3,465	12,662	1	–	**28,904**
Other financial liabilities at fair value	15	–	–	–	–	–	**15**
Debt securities in issue	–	3,698	–	475	800	–	**4,973**
Other liabilities	1,003	47	142	760	–	1,304	**3,256**
Equity	86	155	466	2,479	–	–	**3,186**
Total liabilities and equity	15,720	5,181	4,074	16,376	801	1,304	**43,456**
Notional value of derivatives managing interest rate sensitivity	(206)	2,203	596	(2,572)	(21)	–	**–**
Total interest rate gap sensitivity	635	(2,202)	1,659	(348)	333	(77)	**–**
Cumulative interest rate gap sensitivity	635	(1,567)	92	(256)	77	–	**–**

2017 (unaudited)	Overnight £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Non-interest bearing £m	Total £m
Assets							
Cash and balances with central banks	6,756	9	24	148	–	–	6,937
Due from other banks	1,125	49	–	–	–	–	1,174
Financial assets available for sale	234	362	100	1,020	360	–	2,076
Other financial assets at fair value	477	–	–	–	–	–	477
Loans and advances to customers	8,537	5,356	5,496	11,811	247	(154)	31,293
Other assets	–	–	–	–	–	1,274	1,274
Total assets	17,129	5,776	5,620	12,979	607	1,120	43,231
Liabilities							
Due to other banks	3,292	517	8	–	–	–	3,817
Due to customers	10,708	1,107	3,923	11,965	15	–	27,718
Other financial liabilities at fair value	26	–	–	–	–	–	26
Debt securities in issue	42	3,968	–	475	300	–	4,785
Other liabilities	1,285	44	116	711	–	1,327	3,483
Equity	–	165	441	2,796	–	–	3,402
Total liabilities and equity	15,353	5,801	4,488	15,947	315	1,327	43,231
Notional value of derivatives managing interest rate sensitivity	89	3,044	(478)	(2,767)	112	–	–
Total interest rate gap sensitivity	1,687	(3,069)	1,610	(201)	180	(207)	–
Cumulative interest rate gap Sensitivity	1,687	(1,382)	228	27	207	–	–

Risk report

Balance sheet and prudential regulation risks

Pension risk

The Group operates a defined benefit pension scheme, the Yorkshire and Clydesdale Bank Pension Scheme (the Scheme).

Clydesdale Bank PLC is the Scheme's principal employer and there are no other participating employers. Following a consultation process the Scheme was closed to future accrual on 1 August 2017 for the majority of members. A small number of members elected to keep defined benefit accruals subject to making an increased contribution to the Scheme and to also forego other remuneration benefits.

Defined benefit pension schemes provide a promise to pay members a pre-determined level of income at retirement which is independent of the contributions and investment returns (assets) used to fund these benefit promises (collectively the liabilities). As such, there are significant risks associated with managing a defined benefit scheme. These risks will continue until the Scheme is formally wound up, either in the event that all the liabilities are transferred to a third party (for example an insurer) or once all individual member benefits are paid.

The Scheme's assets are held under a separate trust and the Scheme is managed by a corporate Trustee Board independently of the Group, per the Scheme Trust Deed and Rules. Therefore, the Group's ability to directly manage the Scheme is limited to certain powers within the governing documentation. Aside from the Group's role to sponsor the Scheme to ensure there are sufficient assets to meet benefit payments as they fall due, the Group's focus is directed on mitigating the impact on capital and earnings through working with the trustee to implement risk reduction initiatives. Several activities have been implemented since 2003 with the specific aim of reducing risk in the Scheme, including a de-risking journey plan, benefit reforms and the outcome of the 2017 consultation on future accruals.

The principal cause of risk is the difference between the value and valuation methods of assets and liabilities. The assets are exposed to market valuation movements, within and between asset classes, while the liabilities are more sensitive to interest rate and inflation rate changes, and changes in other actuarial assumptions which may not be borne out in experience, for example life expectancy. There are various bases, with differing assumptions, for measuring the Scheme liabilities whereas Scheme assets are consistently valued at current market values. The two key bases used to value defined benefit scheme liabilities are IAS 19, a standardised accounting measure which is the basis for income statement, balance sheet and capital reporting, and the Trustee's Technical Provisions basis which determines the cash funding contributions to the Scheme to repair any deficit agreed as part of a triennial valuation.

The IAS 19 valuation is disclosed in note 3.16. The rate used to discount the liabilities on the IAS 19 basis is a key driver of volatility and, as prescribed by IAS 19, is based on yields on high-quality corporate bonds. Therefore, the IAS 19 valuation can move adversely because of low rates and narrowing credit spreads. Inflation is another key source of volatility. This is because member benefits have an element of index linking and therefore the liabilities increase with rises in long-term inflation assumptions, although in practice, over the long term, the relationship between interest and inflation rates tends to be negatively correlated resulting in a degree of risk offset. The triennial valuation (the valuation) uses the Trustee's actuarial assumptions and a liability discount rate based on gilt yields. The last scheme funding valuation was at 30 September 2016 with a calculated deficit of £290m. In the latest recovery plan dated 31 January 2018, the Group agreed to eliminate the deficit through the following scheduled contributions: a single contribution of £25m on 15 October 2018; thereafter, equal monthly contributions totalling £50m per annum until 31 March 2022; and £55m in the year to 31 March 2023.

Details of retirement benefit obligations are included in section 3.16 of the Notes to the consolidated financial statements.

Structural reform – ring-fencing

Throughout 2018, the Group has been taking steps to manage the impact of ring-fencing legislation that comes into effect from 1 January 2019. Ring-fencing legislation and the associated PRA Supervisory Statements apply to banks with core deposits greater than £25bn. Banks that meet this threshold must ring-fence their core banking from other activities. The Group is subject to ring-fencing legislation however there is very little impact on customers arising from the Group's compliance activities because there is no need for material change to business operations or corporate structures.

A systemic risk buffer (SRB) for ring-fenced banks will be applied to individual banks by the BoE and will be introduced from 2019. In accordance with current guidance, firms with balance sheet assets less than £175bn will have an SRB of 0% therefore although the framework applies to the Group there is currently no buffer impact. This position does not change with the acquisition of Virgin Money.

Regulatory, compliance and conduct risk

Effectively addressing legacy issues and building a platform for growth

The Group continues to address and eliminate legacy conduct issues while seeking to ensure that fairness is central to our current and future customer propositions and that we meet regulators' expectations.

Regulatory and compliance risk

Regulatory and compliance risk is the risk of: failing to understand and comply with relevant laws, regulations, licence conditions, supervisory requirements, self-regulatory industry codes of conduct and voluntary initiatives; failing to identify, monitor and respond to changes in the regulatory environment; damaging the Group's relationship with its regulators through non-compliance with requirements, not keeping regulators informed of relevant issues that affect (or which may affect) the Group, not responding effectively to the information requests and review findings of the regulators, by providing incorrect or inadequate information, not meeting regulatory deadlines or obstructing the regulator from fulfilling its role.

Risk appetite

The Group has no appetite for actions resulting in breaches of regulation or for inaction in addressing identified control failures that result in non-compliance.

Mitigation measures

- The Group has a regulatory engagement policy designed to ensure an open and cooperative relationship is maintained with regulators at all times, ensuring that all key interactions with regulators are managed, recorded and escalated as appropriate.
- All colleagues are required to achieve mandated standards of compliance learning including the Conduct Rules.
- Material changes to regulatory policies and protocols are approved by either the Executive Leadership Team or the Board.
- The Group CRO and Risk Leadership Team consider compliance risk topics when setting risk appetite and through ongoing risk assessment, profiling and reporting.

Monitoring

A risk management oversight and compliance monitoring plan is approved by Board's Risk Committee on an annual basis which independently assesses the control framework underpinning compliance with laws and regulations.

Conduct risk

Conduct risk is the risk of undertaking business in a way which is contrary to the interests of our customers resulting in the delivery of inappropriate customer outcomes, customer detriment, regulatory censure, redress costs and/or reputational damage.

Risk appetite

The Group is committed to acting in the interests of its customers, and has no appetite for conduct risk.

Mitigation measures

The Group has a conduct framework which recognises the key conduct risks inherent in the Group's strategy through which it seeks to apply high standards in the design and sale of products, and the treatment of its customers through continuous monitoring and responding to customer feedback and complaints. In addition, if things do go wrong, action is taken to ensure we put things right for our customers.

Products are designed and sold to meet customer needs and expectations with governance processes embedded to ensure those objectives are met.

Consideration of customer outcomes is embedded within the Group's operating processes, and metrics are regularly monitored to help ensure outcomes are appropriate.

Exposures

There continues to be a great deal of uncertainty and significant judgement is required in determining the quantum of conduct risk-related liabilities with note 3.14 reflecting the Group's current position in relation to redress provisions for PPI, interest rate hedging products (IRHPs) and other smaller historic conduct matters. The final amount required to settle the Group's potential liabilities for these matters is materially uncertain. The Group will continue to reassess the adequacy of provisions for these matters and the assumptions underlying the calculations at each reporting date based upon experience and other relevant factors at that time.

Monitoring

This is a principal focus of the Board, senior management and regulators, and the Group seeks to ensure customers are treated fairly and products are designed and sold to meet their needs. The Group also works to ensure that customer expectations are met and complaints are dealt with effectively and fairly. All Three Lines of Defence consider conduct risk as part of their oversight and assurance activities.

Risk report

Operational risk (including resilience and information security)

Proactive operational risk management with enhanced risk frameworks

The Group continues to strengthen business resilience, while identifying areas of operational efficiency, and ensuring the level of operational risk capital reflects our risk profile.

Operational risk (including resilience and information security) is the risk of loss resulting from inadequate or failed internal processes, people strategies and systems or from external events including, for example, the prospect of a cyberattack. It is a core component of the RMF and is embedded in day-to-day business activities. Responsibilities are set out in a structured operational risk framework that seeks to identify, assess, mitigate, monitor, and report the operational risks and events that could impact the achievement of business objectives or impact core business processes.

Business units are responsible for the day-to-day management of operational risk, with oversight from the risk management function, and independent assurance activities undertaken by internal audit.

The requirements of the operational RMF are defined in an overarching operational risk policy and related minimum standards, and reflect the Group's operational risk appetite.

Risk appetite

The Group is prepared to tolerate a level of operational risk exposure within agreed thresholds and limits. A level of resilience risk from internal and external events is tolerated however immediate steps must be taken to minimise customer disruption through recovery within defined timelines. Operational risks arise from day-to-day business activities, which may result in direct or indirect losses and could adversely impact the Group's financial performance, levels of customer care and reputation.

Approach to monitoring and mitigating exposures

Losses may result from both internal and external events, and are categorised using risk categories aligned to Basel II. The Basel II categories are used to ensure that data can be reported externally and compared with other industry data.

The Group has identified, assessed and is currently monitoring all key operational risks across the above noted categories, including undertaking an assessment of control effectiveness, monitoring trends in key risk indicators and escalating events, in accordance with policy requirements.

Stress testing

The Group develops and maintains a suite of operational risk scenarios using internal and external data. These scenarios provide insights into the stresses the business could be subject to given extreme circumstances. Scenarios cover all material operational risks including execution of change, failures to core processes or contagion risk from a third party. Scenarios are owned by senior management custodians with review and challenge provided by Risk Management, Executive Risk Committee and Board Risk Committee, as part of the ICAAP process. Management actions are agreed and monitored and linked with business resilience and continuity testing where appropriate.

Risk category	
Operational resilience risk	The risks associated with the ability of the Group to quickly adapt to disruptions while maintaining continuous business operations and safeguarding people, assets and overall brand equity, even in the face of adverse events, shocks and chronic or incremental changes. **How this risk is managed –** the Group has a well-defined and embedded resilience framework that is designed to both prevent disruptions from occurring and, where they do occur, to minimise the impact to customers and colleagues through speedy resolution.
Information security risk	The risks associated with inadequate and failed information technology processes and components (including hardware, software and networking components). **How this risk is managed –** the Group continues to enhance and invest in the control environment, recognising the changing cyber landscape and the increased focus on digital capabilities, as well as the changing risk profile of the business.
Change risk	The risks associated with a failure to execute and deliver change that could result in an inability to meet our strategic objectives, including failing to meet our customer, regulator, colleague, or shareholders' expectations, at a Group level and local management level. **How this risk is managed –** the Group maintains a centralised view of change to ensure that the risks of individual changes are managed effectively and that change is prioritised to minimise the overall risks to the organisation in line with risk appetite.
Third party risk	The risks associated with ensuring the Group's outsourced and offshoring arrangements are controlled effectively, including the risk of failure to service existing and new customers, and the potential cessation of specific activities, or the risk of personally identifiable information or Group sensitive data being exposed or exploited, or the risk of financial, reputational and regulatory censure if the third party enters into any illegal or unethical activities. **How this risk is managed –** the Group continues to strengthen its third party management framework and oversight, and ensures that the procurement of service providers adheres to these requirements.
Data risk	The risks associated with the accuracy, management and use of data that underpins decision-making at every level across the organisation. **How this risk is managed –** the Group has a data management framework for the development, use, monitoring, management and ownership of data. Data quality is assessed against three key attributes: completeness; appropriateness; and accuracy. Furthermore, the Group has strengthened its data protection management and GDPR compliance framework.
Integration risk	The operational risks associated with management of a large-scale integration plan including: the need for effective governance and clear accountability; increased threat of cybersecurity incident; risks associated with systems migration or inadequate testing or poor management of external and internal communications; and a poor risk culture. **How this risk is managed –** the Group will establish integration programme activities to mitigate the risks, including: – the preparation and delivery of the FSMA Part VII transfer; – the development, validation and implementation of Group rebranding requirements; – migration support for enterprise systems implementation; – inputs for ongoing programme management reporting, dependencies and resource management; and – Risk SME input to provide support and challenge to the overall programme.

Risk report

Financial crime risk

A strengthened and robust financial crime framework

The Group continues to invest in its systems and controls to prevent, detect, screen and report financial crime, demonstrating a tangible uplift in effectiveness.

Financial crime risk is the risk that the Group's products and services will be used to facilitate financial crime against the Group, its customers or third parties. It encompasses the risk of failing to understand and comply with relevant laws, regulations and supervisory requirements relating to money laundering, terrorism financing, bribery and corruption and sanctions and embargoes.

It also includes risks associated with external or internal acts intended to defraud, misappropriate, and circumvent policy, funds, information, regulations and property. The Group maintains an overarching financial crime policy and four policy standards aligned to each material financial crime risk. These are:

Sanctions – The Group has no appetite for non-compliance with the legal and regulatory obligations relating to sanctions and embargoes. To reflect the Group's risk appetite and to protect the Group from financial and reputational damage, including regulatory censure, fines and enforcement action, the Sanctions and Embargoes Policy articulates a set of minimum standards and requirements which must be complied with.

Anti-money laundering – The Group applies a prescribed high-risk customer model which sets out the types of customer it has no risk appetite to onboard, as well as customers with whom the Group is prohibited from entering into or maintaining a customer relationship. All other customers who are not proscribed shall be subject to controls commensurate with their risk.

Anti-bribery and corruption – The Group does not tolerate the direct or indirect offer, payment, solicitation or acceptance of bribes in any form. The Group has in place risk assessments, policies and guidelines on interacting with customers, suppliers and agents, including specific policies for gifts and hospitality. Senior managers across the business are required to complete an evaluation of risk areas as part of the risk assessment process.

Fraud – The Group accepts that, in order to conduct business in a commercially viable manner, it is willing to sustain fraud losses within an agreed set of parameters. The application of fraud risk management considers customer impacts, industry trends and financial impacts of fraud which, on occasion, provide conflicting priorities. Emerging risks are identified and assessed with action taken to mitigate them. An agreed loss plan is set and performance against this is overseen by the policy owner and reported through the appropriate governance committees. With regard to internal fraud, the Group recognises the risk of internal fraud but has no appetite for it. Consequently there is a control framework in place to mitigate that risk.

Exposures

There are currently no significant exposures to report. The Group continues to review the external environment for any change in regulatory or legislative direction, taking action as appropriate.

Mitigation measures

Risk assessments against the four financial crime policy standards take place on an annual basis. Over and above these assessments, regular oversight of higher-risk activities takes place as part of the formal oversight plan and embedded activity takes place throughout the year. Key performance metrics relative to critical financial crime systems are kept under review to ensure ongoing effectiveness. Third party tools are used to test system effectiveness where available and appropriate. Training completion and compliance is subject to annual oversight.

All standards are reflected in the Group policy and standards and financial crime prevention manual, the content of which is provided by financial crime risk and updated as appropriate.

Monitoring

The financial crime team is responsible for strategy, governance, standard setting, oversight, training and reporting to the competent authorities and governance committees/Board.

The control framework is owned by financial crime risk but management and execution of customer identity and verification, customer due diligence, enhanced due diligence, identifying high-risk customers, including correspondent banking relationships and record keeping is the responsibility of first line business units.

Account opening pass rates are reported on a monthly basis and overseen as part of a regular process undertaken by financial crime risk.

Higher-risk customers are referred to financial crime risk and senior management within Customer Banking for agreement and sign off that business is within appetite and then continue to be monitored on an ongoing basis.

Screening customers for sanctions or politically exposed persons and transaction monitoring is carried out by financial crime risk. Sanctions screening for payments is carried out by the Payments team in the first line. Critical financial crime systems oversight is independently tested by Internal Audit.

Strategic, business and financial performance risk

Robust strategy development and monitoring

Strategy is delivered within a well-defined risk appetite and RMF with continual monitoring in place.

Strategic, business and financial performance risk is the risk of significant loss of earnings or damage arising from business decisions that impact the long-term interests of the Group's stakeholders or from an inability to adapt to external developments.

Risk appetite

The Group intends to grow and increase share in target markets, and has clear strategies for its business model and for target customers and products, but it has no appetite to achieve its targets in an unsustainable fashion, or one which may result in damaging outcomes for the Group, its customers or other stakeholders.

Exposures

The Group operates amid intense, increasing competition. Peer and challenger banks, some with innovative business models and low cost bases, such as fast-growing peer-to-peer lenders and crowd funders, allied with rapid technological change, notably in payments and mobile banking, present a fast-evolving, challenging environment. These trends and new regulations also necessitate a large change agenda, which diverts management attention, imposes costs and which may not deliver expected benefits.

At the same time, the low interest rate environment constrains income, reduces margins and, by inhibiting capital generation, reduces strategic room for manoeuvre. As such, income growth and margin expectations over the Group's planning horizon are balanced, highlighting that this environment contributes to significant business risk, the risk that Group net income fails to grow as targeted, or falls.

Mitigation measures

CYBG was divested from NAB and listed in February 2016, but strategic changes necessary for success when independent were assessed over a prolonged prior period. Moreover, CYBG has a long history as a full service UK bank and benefits from an experienced Board and Executive Leadership Team, such that the overall strategy has evolved through a mature and robust process.

The Group's risk appetite represents a 'risk envelope' against which chosen strategies and financial plans are assessed and within which chosen strategies must operate. The RAS, and associated risk appetite framework, is therefore a key means of controlling strategic risk. The risk appetite framework comprises an extensive system of measures, thresholds and other controls, which together ensure that the Group operates within the Board's approved appetite for strategic risk.

Monitoring

A range of financial and non-financial metrics, including RoTE, lending growth, customer acquisition, NIM and others, are key performance indicators used to monitor performance relative to strategic objectives. They are monitored against the Financial Plan by the Group's Board and Executive Leadership Team, who react to deviations from targets and modify strategy accordingly.

Risk report

People risk

Supporting our colleagues to build a successful, customer-centric business

Continued embedding of the people framework ensures overall people risk is maintained within risk appetite during this period of significant change.

People risk is the risk associated with not having the right number of people in the right roles; appropriately trained and competent; engaged; motivated; clear on their responsibilities and accountabilities; who behave in an ethical way; and are treated fairly, with dignity and respect. People risk is inherent and controlled through a set of values, behaviours and policies.

Risk appetite

The Group is evolving its structure to enable it to deliver on the core objectives of becoming a commercially focused, high performing business. While the organisational structural changes being implemented to support the commercial objectives will drive an inherent increase in people risk, the Group is also focused on cultural transformation, which aims to create a high performing, customer-centric organisation and drive accountability and responsibility, alongside appropriate reward structures.

The Group will not accept a material increase in risk as a result of colleagues not conducting themselves in the manner expected, nor will the Group act in a manner that may affect the health and well-being of colleagues. The Group will not take intentional action that may impact on its ambition to build an inclusive culture and will continue to embed activities that support the required cultural change.

Approach to monitoring and mitigating exposures

People risk is managed in three core ways:

- Managing people risk across the Group: The changing internal and external environment raises challenges relative to the Group's ability to manage people risk, as part of the overall business strategy. The transformation of the banking industry is changing the demand for skills, particularly in relation to technology, information security, serving customers digitally and responding to market developments. The Group's operating controls, are effective in managing these risks and there is a focus on the Group's ability to plan and predict resource needs during this period of cost challenges, and increased use of technology.
- Managing the people management framework: Controls are deployed effectively by people leaders and senior management in the day-to-day management of people risk. People risk indicators are constantly reviewed to determine if any systemic issues exist and to agree appropriate remediation.
- The role of the HR function: HR partners support the CYBG Leadership Team and provides broader support to all colleagues regarding all matters impacting the colleague life cycle which runs from recruitment to leaving the Group. The Group has a three-tier model incorporating: ourPeople (web-based); HR Services, supported by specialist teams like Reward; Organisational Development, Payroll; and Case Management; and finally full business partnering to the CYBG Leadership Team.

The Group's operational controls are designed to mitigate the risks associated throughout each element of the colleague life cycle. Bank-wide systems provide tools and online guidance to all colleagues to support them in discharging their accountabilities.

Stress testing

The people risks associated within a stressed scenario are automatically captured and analysed through the Group's suite of operational risk scenarios. These scenarios consider both the colleagues needed to maintain business-as-usual services to customers as well as the key subject matter experts needed to keep critical functions operating while under duress.

Financial statements

Financial statements

Independent auditor's report to the members of CYBG PLC

Our opinion on the financial statements

In our opinion:

- the CYBG PLC Group financial statements and Parent company financial statements (the 'financial statements') give a true and fair view of the state of the Group's and of the Parent company's affairs as at 30 September 2018 and of the Group's loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the Parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

What we have audited
The CYBG PLC financial statements comprise:

Group	Parent company
Consolidated Income Statement for the year ended 30 September 2018	
Consolidated Statement of Comprehensive Income for the year ended 30 September 2018	
Consolidated Balance Sheet as at 30 September 2018	Company Balance Sheet as at 30 September 2018
Consolidated Statement of Changes in Equity for the year ended 30 September 2018	Company Statement of Changes in Equity for the year ended 30 September 2018
Consolidated Statement of Cash Flows for the year ended 30 September 2018	Company Statement of Cash Flows for the year ended 30 September 2018
Related notes 1.1 to 5.5 to the financial statements	Related notes 6.1 to 6.6 to the financial statements
Certain required disclosures have been presented elsewhere in the Annual Report and Accounts, rather than in the notes to the financial statements. These have been cross-referenced from the financial statements and are identified as audited.	

The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the Parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

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

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

Conclusions relating to principal risks, going concern and viability statement
We have nothing to report in respect of the following information in the Annual Report, in relation to which the ISAs (UK) require us to report to you whether we have anything material to add or draw attention to:

- the disclosures in the Annual Report set out on page 17 that describe the principal risks and explain how they are being managed or mitigated;
- the Directors' confirmation set out on page 66 in the Annual Report that they have carried out a robust assessment of the principal risks facing the entity, including those that would threaten its business model, future performance, solvency or liquidity;
- the Directors' statement set out on page 185 in the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, and their identification of any material uncertainties to the entity's ability to continue to do so over a period of at least 12 months from the date of approval of the financial statements;
- whether the Directors' statement in relation to going concern required under the Listing Rules in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit; or
- the Directors' explanation set out on page 117 in the Annual Report as to how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the entity will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Overview of our audit approach

Key audit matters	– PPI provision. – SME lending impairment provisions. – Revenue recognition – Effective interest method accounting.
Audit scope	– Our Group audit scope included the complete financial information of the CYBG PLC Group including all its subsidiaries. – All audit work performed for the purposes of the Group audit was undertaken by the primary team .
Materiality	– Overall Group materiality was £15m which represents 4.5% of underlying profit before tax.

Financial statements

Independent auditor's report to the members of CYBG PLC

Key audit matters

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

Key audit matters	Our response to the risk	Key observations communicated to the Board's Audit Committee
Payment Protection Insurance (PPI) Provision The Group has recorded £275m in relation to PPI redress provisions. Please refer to pages 72 to 78 (Audit Committee report), pages 213 to 215 (Provisions for liabilities and charges note), pages 231 and 232 (Contingent liabilities and commitments note). The Group has a material provision relating to its conduct towards its past and present customers linked to its historic practices of PPI sales. In 2016, the Group entered into a conduct indemnity deed, granted by its former parent, under which all qualifying remediation costs for past conduct issues were reimbursed up to a capped amount. As set out on page 215, the capped amount was reached during the first half of the year. Since that point, all further PPI related costs are fully borne by the Group. During the year, the Group completed its remediation exercise for previously closed PPI complaints. The FCA has set a deadline of 29 August 2019 for customers to lodge PPI related complaints. Significant judgements and assumptions are required to be made by the Directors in relation to the timing, volume and quantum of future redress payments and associated administration costs that will be required. The most significant assumption is the volume of future new PPI complaints. Details of this assumption, including the reduction in volumes anticipated in advance of the August 2019 time bar, are reported on page 214 in note 3.14.	We considered the results of the testing of key controls operating within the PPI and other conduct case handling and recording processes which supported the data used in the determination of key provision assumptions. We found that we could place reliance on these controls. We examined the models used by the Directors to determine a best estimate of the provisions for mis-sold PPI. We assessed the appropriateness of PPI provision model assumptions, including case volumes, redress per claim, up-hold rates and case processing costs, which were informed by the Group's historic experience. We tested the clerical accuracy of the Directors' provision calculations and sensitivity analysis. We determined an independent range of reasonable future PPI cost outcomes using the Group's historical experience of PPI claims, and we compared this range to the Directors' estimate. In evaluating the Directors' provision assumptions, we considered the Group's historical forecasting accuracy in this area and we examined correspondence during the year between the Group and the FCA, and other regulatory pronouncements. We compared the Directors' assumptions to our own expectations based on the Group's historical experience, current trends and our industry knowledge.	We communicated to the Audit Committee that provisions for PPI redress and other conduct related matters held by the Group were reasonably estimated. We noted that the Group's disclosures describe the uncertainties and risks associated with determining the provisions, and the sensitivity of the provisions to changes in key assumptions. The Directors' best estimate for future PPI claims and associated costs involved probability weighting a number of possible outcomes. We reported to the Audit Committee that the estimation of provisions for PPI claims is inherently uncertain and requires significant judgements to be made by the Directors. We observed that, based on past experience, there continues to remain the potential for future costs relating to PPI claims to be materially higher than the Directors' estimate at 30 September 2018.

Key audit matters	Our response to the risk	Key observations communicated to the Board's Audit Committee
SME lending impairment provisions The Group has recorded £136m in relation to impairment provisions held on non-retail credit exposures. Please refer to pages 204 to 206 (Impairment provisions on credit exposures note). The majority of the Group's non-retail lending portfolio relates to small and medium sized enterprises ('SMEs') which can be vulnerable to both domestic and foreign market volatility. Estimating the Group's collective and specific provisioning is subjective, requires the Directors to exercise significant judgement, and incorporates the use of assumptions the most significant of which are the probability of default and loss given default assumptions used in the Group's collective modelling process, and the identification and judgements made in respect of loan files subject to specific assessment. Due to the materiality of the provisions and level of judgement involved, this was considered to be a key audit matter.	We tested controls over impairment calculations and the generation of portfolio data for use in these calculations. These controls included those covering the identification and assessment of potentially impaired loans, the transfer of data from source systems to impairment models, and the calculation of specific impairment provisions. We determined that we could rely on these controls for the purposes of our audit. We performed loan file testing on a sample of impaired loans to determine whether the specific provisions held by the Group were, in our judgement, sufficient and appropriate. Our approach included the use of our own valuation specialists to independently test key assumptions underpinning a sample of collateral values used in provision calculations. We tested the collective impairment provision model by using our modelling specialists to examine the logic of the model calculations, the accuracy of data inputs, and assessing the appropriateness of key assumptions and loan ratings used within the model. Using our experience of impairment provisioning in the sector, we assessed the appropriateness of overlays to the collective impairment models applied by the Directors and tested the accuracy of calculations in the overlays. We evaluated the completeness of SME loans assessed for impairment by the Directors and examined key loans where no impairment provisions were held.	We communicated to the Audit Committee that the impairment models, calculations and assumptions employed by the Group were reasonable as at 30 September 2018 and that these resulted in impairment provisions that were appropriately estimated. We also concluded that the disclosures presented were in compliance with IFRSs. Our communication to the Audit Committee presented an independent range for the level of incurred but not reported losses existing in the Group's loan portfolio, and we compared this range to the Directors' own post model adjustments. We found no material differences in this comparison. We assessed and challenged the calculations and related judgements for a sample of specific impairment provisions and communicated to the Audit Committee that these procedures did not identify any material differences to the provisions determined by the Directors.

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Independent auditor's report to the members of CYBG PLC

Key audit matters	Our response to the risk	Key observations communicated to the Board's Audit Committee
Revenue recognition – effective interest method As set out on page 203 in note 3.5, the Group has recorded £25m of net deferred income in relation to fee income and expenses deferred under the Group's effective interest method of accounting. Please also refer to page 193 (net interest income accounting policy). For certain product fees, the Group operates a model to recognise fee income (included within interest income) under the effective interest method. The effective interest method spreads the recognition of product fee income over the life of a financial instrument, as these are in substance an integral part of the overall yield. Effective interest models are sensitive to judgements about the expected lives of the product portfolios to which they relate. Due to the complexity of calculations, the degree of judgement exercised by the Directors in respect of the expected lives of the product portfolios and the different products for which fees are recognised, this is considered a key audit matter.	We gained an understanding of key controls and assessed the appropriateness of key assumptions used within the Group's effective interest model, primarily the average loan life assumption, which we corroborated against underlying loan data, our knowledge of market conditions and observed practice in the UK banking sector. We performed data integrity testing on the key sources of information feeding the effective interest calculation. This involved sample testing data from business systems to the loan data used in the model and vice versa. We examined the journals recording the deferral and amortisation of fee income to verify that the revenue deferred and amortised over the life of the underlying loans was appropriate and aligned with the effective interest model output.	We communicated to the Audit Committee that the effective interest adjustments recognised in interest income had been appropriately derived. We also communicated that the assumptions made by the Directors were reasonable in the context of the Group's lending portfolios and current observable customer behaviours.

In the prior year our conduct provisions key audit matter covered PPI and other conduct related provisioning. As programmes relating to other conduct provisions have substantially been completed during the year, our key audit matter for the current year relates solely to PPI provisions.

Our application of materiality

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

Materiality

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

We determined materiality for the Group and Parent to be £15m (2017: £17m), which represents 4.5% of underlying profit on ordinary activities before tax (consistent with the prior year approach, this is defined as the Group's profit before tax adjusted to exclude one-off expenditure incurred during the year and those related to conduct provisions and restructuring). A reconciliation between statutory profit and the adjusted profit before tax is shown below:

Starting point
- Statutory loss on ordinary activities before tax
- £164m loss

Adjustments

Deduct:
- Restructuring and related expenditure £38m
- Virgin Money acquisition costs: £37m
- RBS alternative remedies spend: £16m
- Separation cost: £8m
- Legacy conduct costs: £396m

Materiality
- Total £331m (Underlying profit before tax)
- Materiality of £15m (4.5% of Underlying profit before tax)

Performance materiality
Performance materiality is the application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality was 75% (2017: 75%) of our planning materiality, namely £11.25m (2017: £12.75m). We have set performance materiality at this percentage due to our previous experience as auditors of the Group, from which we concluded that there is a lower expectation of material financial statement inaccuracies due to the effective control environment and only minor audit differences resulting from our prior and current year work. Our approach is consistent with prior year.

Reporting threshold
This is the amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.75m (2017: £0.85m), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

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

Other information
The other information comprises the information included in the Annual Report set out on pages 1 to 170, including the Strategic Report set out on pages 1 to 33, the Financial Results set out on pages 34 to 43, Governance set out on pages 47 to 119, the Risk Report set out on pages 121 to 170, and Additional Information set out on pages 245 to 257 other than the financial statements and our auditor's report thereon. The Directors are responsible for the other information.

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

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

We have nothing to report in this regard.

In this context, we also have nothing to report in regard to our responsibility to specifically address the following items in the other information and to report as uncorrected material misstatements of the other information where we conclude that those items meet the following conditions:

– **Fair, balanced and understandable** set out on page 119 – the statement given by the Directors that they consider the Annual Report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or

– **Audit Committee reporting** set out on pages 72 to 78 – the section describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee is materially inconsistent with our knowledge obtained in the audit; or

– **Directors' statement of compliance with the UK Corporate Governance Code** set out on page 60 – the parts of the Directors' statement required under the Listing Rules relating to the Company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R(2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code.

Opinions on other matters prescribed by the Companies Act 2006
In our opinion, the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.

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

– the information given in the Strategic Report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and

– the Strategic Report and the Directors' report have been prepared in accordance with applicable legal requirements.

Financial statements

Independent auditor's report to the members of CYBG PLC

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the Group and the Parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the Strategic Report or the Directors' report.

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

- adequate accounting records have not been kept by the Parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Responsibilities of Directors

As explained more fully in the Directors' responsibilities statement set out on page 119, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

Auditor's responsibilities for the audit of the financial statements

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

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

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

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Group and determined that the most significant were the regulations, licence conditions and supervisory requirements of the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA).
- We understood how the Group complies with these legal and regulatory frameworks by making enquiries of management, internal audit, and those responsible for legal and compliance matters. We also: reviewed correspondence between the Group and UK regulatory bodies; reviewed minutes of the Board and Executive Risk Committee; and gained an understanding of the Group's approach to governance, demonstrated by the Board's approval of the Group's governance framework and the Board's review of the Group's risk management framework (RMF) and internal control processes.
- We assessed the susceptibility of the Group's financial statements to material misstatement, including how fraud might occur, by considering the controls that the Group has established to address risks identified by the entity, or that otherwise seek to prevent, deter or detect fraud. We also considered performance and incentive plan targets and their potential to influence management to manage earnings or influence the perceptions of investors.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations identified in the paragraphs above. Our procedures involved inquiries of legal counsel, executive management, internal audit, and focused testing, as referred to in the Key Audit Matters section above.
- The Group operates in the banking industry which is a highly regulated environment. As such the Senior Statutory Auditor considered the experience and expertise of the engagement team to ensure that the team had the appropriate competence and capabilities, which included the use of specialists where appropriate.

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

Other matters we are required to address

- We were appointed as CYBG PLC's External Auditor and signed an engagement letter on 14 January 2016, prior to CYBG PLC becoming the holding company of the Group on its Demerger and IPO in February 2016. The period of total uninterrupted engagement as auditors of CYBG PLC including previous renewals and reappointments, is three years, covering the years ending 30 September 2016 to 30 September 2018
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Company and we remain independent of the Group and the Company in conducting the audit.
- The audit opinion is consistent with the additional report to the Audit Committee.

Use of our report

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

Ernst & Young LLP

Steven Robb (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP,
Statutory Auditor
Leeds

26 November 2018

Notes

1. The maintenance and integrity of the CYBG PLC website is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Financial statements

Consolidated income statement

for the year ended 30 September	Note	2018 £m	2017 £m
Interest income and similar income		**1,113**	1,075
Interest expense and similar charges		**(262)**	(231)
Net interest income	2.2	**851**	844
Gains less losses on financial instruments at fair value		**(3)**	6
Other operating income		**159**	186
Non interest income	2.3	**156**	192
Total operating income		**1,007**	1,036
Total operating and administrative expenses before impairment losses	2.4	**(1,130)**	(720)
Operating (loss)/profit before impairment losses		**(123)**	316
Impairment losses on credit exposures	3.6	**(41)**	(48)
(Loss)/profit on ordinary activities before tax		**(164)**	268
Tax credit/(expense)	2.5	**19**	(86)
(Loss)/profit for the year		**(145)**	182
(Loss)/profit attributable to ordinary shareholders		**(181)**	146
Profit attributable to other equity holders		**36**	36
(Loss)/profit for the year attributable to equity holders		**(145)**	182
Basic (loss)/earnings per share (pence)	2.6	**(19.7)**	17.3
Diluted (loss)/earnings per share (pence)	2.6	**(19.7)**	17.2

All material items dealt with in arriving at the (loss)/profit before tax for the above years relate to continuing activities.

The notes on pages 185 to 235 form an integral part of these financial statements.

Consolidated statement of comprehensive income

for the year ended 30 September	Note	2018 £m	2017 £m
(Loss)/profit for the year		**(145)**	182
Items that may be reclassified to the income statement			
Change in cash flow hedge reserve			
Losses during the year		**(58)**	(84)
Transfers from/(to) the income statement		**9**	(4)
Taxation thereon		**11**	21
		(38)	(67)
Change in available for sale reserve			
Losses during the year		**–**	(7)
Transfers to the income statement		**–**	(20)
Taxation thereon		**–**	7
		–	(20)
Total items that may be reclassified to the income statement		**(38)**	(87)
Items that will not be reclassified to the income statement			
Change in asset revaluation reserve			
Taxation thereon		**1**	–
Remeasurement of defined benefit pension plans	3.16	**(9)**	154
Taxation thereon		**3**	(35)
		(6)	119
Total items that will not be reclassified to the income statement		**(5)**	119
Other comprehensive (losses)/income, net of tax		**(43)**	32
Total comprehensive (losses)/income for the year, net of tax		**(188)**	214
Total comprehensive (losses)/income attributable to ordinary shareholders		**(224)**	178
Total comprehensive income attributable to other equity holders		**36**	36
Total comprehensive (losses)/income attributable to equity holders		**(188)**	214

The notes on pages 185 to 235 form an integral part of these financial statements.

Financial statements

Consolidated balance sheet

as at 30 September	Note	2018 £m	2017 £m
Assets			
Cash and balances with central banks	3.1	**6,573**	6,937
Due from other banks		**836**	1,174
Financial assets available for sale	3.2	**1,562**	2,076
Other financial assets at fair value	3.3	**362**	477
Derivative financial instruments	3.4	**262**	282
Loans and advances to customers	3.5	**32,744**	31,293
Due from customers on acceptances		**4**	4
Property, plant and equipment	3.8	**88**	86
Investment properties	3.9	**7**	14
Intangible assets	3.10	**412**	339
Deferred tax assets	3.11	**206**	154
Defined benefit pension assets	3.16	**212**	207
Other assets		**188**	188
Total assets		**43,456**	43,231
Liabilities			
Due to other banks	3.12	**3,122**	3,817
Other financial liabilities at fair value	3.3	**15**	26
Derivative financial instruments	3.4	**361**	376
Due to customers	3.13	**28,904**	27,718
Liabilities on acceptances		**4**	4
Provisions for liabilities and charges	3.14	**331**	554
Debt securities in issue	3.15	**4,973**	4,785
Retirement benefit obligations	3.16	**3**	3
Deferred tax liabilities	3.11	**77**	75
Other liabilities	3.17	**2,480**	2,471
Total liabilities		**40,270**	39,829
Equity			
Share capital	4.1	**89**	88
Other equity instruments	4.1	**450**	450
Capital reorganisation reserve	4.1	**(839)**	(839)
Merger reserve	4.1	**633**	633
Other reserves	4.1	**(20)**	15
Retained earnings		**2,873**	3,055
Total equity		**3,186**	3,402
Total liabilities and equity		**43,456**	43,231

The notes on pages 185 to 235 form an integral part of these financial statements.

These financial statements were approved by the Board of Directors on 26 November 2018 and were signed on its behalf by:

David Duffy
Chief Executive Officer

Ian Smith
Group Chief Financial Officer

CYBG PLC, Registered number: 09595911

Consolidated statement of changes in equity

	Note	Share capital £m	Capital reorganisation reserve £m	Merger reserve £m	Other equity instruments £m	Other reserves: Equity based compensation reserve £m	Other reserves: Asset revaluation reserve £m	Other reserves: Available for sale reserve £m	Other reserves: Cash flow hedge reserve £m	Retained earnings £m	Total equity £m
As at 1 October 2016		88	(839)	633	450	6	1	27	66	2,779	3,211
Profit for the year		–	–	–	–	–	–	–	–	182	182
Other comprehensive (losses)/income, net of tax		–	–	–	–	–	–	(20)	(67)	119	32
Total comprehensive (losses)/income for the year		–	–	–	–	–	–	(20)	(67)	301	214
AT1 distribution paid (net of tax)		–	–	–	–	–	–	–	–	(29)	(29)
Transfer from equity based compensation reserve		–	–	–	–	(4)	–	–	–	4	–
Equity based compensation expensed		–	–	–	–	6	–	–	–	–	6
As at 30 September 2017	4.1	88	(839)	633	450	8	1	7	(1)	3,055	3,402
Loss for the year		–	–	–	–	–	–	–	–	(145)	(145)
Other comprehensive (losses)/income, net of tax		–	–	–	–	–	1	–	(38)	(6)	(43)
Total comprehensive (losses)/income for the year		–	–	–	–	–	1	–	(38)	(151)	(188)
Dividends paid to ordinary shareholders		–	–	–	–	–	–	–	–	(9)	(9)
AT1 distribution paid (net of tax)		–	–	–	–	–	–	–	–	(29)	(29)
Transfer from equity based compensation reserve		–	–	–	–	(7)	–	–	–	7	–
Ordinary shares issued		1	–	–	–	–	–	–	–	–	1
Equity based compensation expensed		–	–	–	–	9	–	–	–	–	9
As at 30 September 2018	4.1	**89**	**(839)**	**633**	**450**	**10**	**2**	**7**	**(39)**	**2,873**	**3,186**

The notes on pages 185 to 235 form an integral part of these financial statements.

Strategic report
Financial results
Governance
Risk report
Financial statements
Additional information

Financial statements

Consolidated statement of cash flows

for the year ended 30 September	Note	2018 £m	2017 £m
Operating activities			
(Loss)/profit on ordinary activities before tax		**(164)**	268
Adjustments for:			
Non-cash or non-operating items included in profit before tax	5.2	**(715)**	(728)
Changes in operating assets	5.2	**(1,059)**	(1,857)
Changes in operating liabilities	5.2	**(122)**	919
Interest received		**1,108**	1,123
Interest paid		**(173)**	(258)
Tax received – Group relief		**–**	1
Net cash used in operating activities		**(1,125)**	(532)
Cash flows from investing activities			
Interest received		**12**	11
Proceeds from maturity of available for sale investments		**245**	20
Proceeds from sale of available for sale investments		**822**	60
Purchase of available for sale investments		**(593)**	(492)
Proceeds from sale of tangible fixed assets(1)		**9**	19
Purchase of tangible fixed assets(1)		**(22)**	(21)
Purchase and development of intangible assets		**(144)**	(148)
Net cash provided by/(used in) investing activities		**329**	(551)
Cash flows from financing activities			
Interest received		**1**	3
Interest paid		**(94)**	(90)
Redemption and principal repayment on RMBS and covered bonds	3.7	**(1,372)**	(740)
Issuance of RMBS and covered bonds	3.7	**1,049**	750
Issuance of medium-term notes/subordinated debt	3.15	**497**	298
Amounts drawn down under the TFS		**1,250**	1,900
Amounts repaid under the TFS		**(900)**	–
Ordinary dividends paid		**(9)**	–
AT1 distributions		**(36)**	(36)
Net cash provided by financing activities		**386**	2,085
Net (decrease)/increase in cash and cash equivalents		**(410)**	1,002
Cash and cash equivalents at the beginning of the year		**6,952**	5,950
Cash and cash equivalents at the end of the year(2)	5.2	**6,542**	6,952

(1) Tangible fixed assets include property, plant and equipment, investment properties and property inventory.
(2) Cash and cash equivalents is cash and balances with central banks less mandatory deposits plus cash equivalents within other assets, less due to other banks, and other liabilities.

Reconciliation of movements to liabilities from cash flows arising from financing activities

	Term funding scheme £m	Debt securities in issue £m	Total £m
At 1 October 2017	1,901	4,785	6,686
Cash flows:			
Issuances	–	1,546	1,546
Redemptions	–	(1,372)	(1,372)
Drawdowns	1,250	–	1,250
Repayment	(900)	–	(900)
Non-cash flows:			
Movement in accrued interest	3	2	5
Unrealised foreign exchange movements	–	30	30
Unamortised costs	–	(18)	(18)
At 30 September 2018	**2,254**	**4,973**	**7,227**

The notes on pages 185 to 235 form an integral part of these financial statements.

Notes to the consolidated financial statements

Section 1: Basis of preparation

Overview
This section sets out the Group's accounting policies that relate to the consolidated financial statements as a whole. Where an accounting policy is specific to one note, the policy is described in the note to which it relates. This section also shows new accounting standards, amendments and interpretations, relevant to the Group, and whether they are effective in 2018 or later years. We explain how these changes are expected to impact the financial position and performance of the Group.

1.1 General information
The Company is a public company limited by shares, incorporated in the United Kingdom under the Companies Act and registered in England and Wales.

The consolidated financial statements comprise those of the Company and its controlled entities, together the 'Group'.

1.2 Basis of accounting
The consolidated financial statements have been prepared in accordance with IFRS as adopted by the EU and in accordance with the provisions of the Companies Act 2006.

The financial information has been prepared under the historical cost convention, as modified by the revaluation of land and buildings, investment properties, financial assets available for sale and certain other financial assets and liabilities at fair value through profit or loss. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

1.3 Presentation of risk, offsetting and maturity disclosures
Certain disclosures required under IFRS 7 'Financial instruments: disclosures' and IAS 1 'Presentation of financial statements' have been included within the audited sections of the Risk report. Where information is marked as audited, it is incorporated into these financial statements by this cross reference and it is covered by the Independent auditor's report.

1.4 Going concern
The Group's business activities, together with the factors likely to affect its future development, performance and position, are set out in the Strategic report. In addition, the Risk report includes the Group's risk management objectives and the Group's objectives, policies and processes for managing its capital.

In assessing the Group's going concern position as at 30 September 2018, the Directors have considered a number of factors, including the current balance sheet position, the principal and emerging risks which could impact the performance of the Group, the Group's strategic and financial plan and the impact of the acquisition of Virgin Money. The assessment concluded that, for the foreseeable future, the Group has sufficient capital to support its operations; has a funding and liquidity base which is strong, robust and well managed with future capacity; and has expectations that performance will continue to improve as the Group's strategy is executed.

As a result of the assessment, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future and therefore believe that the Group is well placed to manage its risks successfully in line with its business model and strategic aims. Accordingly, they continue to adopt the going concern basis in preparing the consolidated financial statements.

1.5 Basis of consolidation
Controlled entities are all entities (including structured entities) to which the Company is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. An assessment of control is performed on an ongoing basis.

Controlled entities are consolidated from the date on which control is established by the Group until the date that control ceases. The acquisition method of accounting is used to account for business combinations other than those under common control. A non-controlling interest is recognised by the Group in respect of any portion of the total assets less total liabilities of an acquired entity or entities that is not owned by the Group. Post-acquisition, income received and expenses incurred by the entity or entities acquired are included in the consolidated income statement on a line by line basis in accordance with the accounting policies set out herein. Balances and transactions between entities within the Group and any unrealised gains and losses arising from those transactions are eliminated in full upon consolidation.

The consolidated financial statements have been prepared using uniform accounting policies.

Financial statements

Notes to the consolidated financial statements

Section 1: Basis of preparation continued

1.6 Foreign currency

Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The consolidated financial statements are presented in pounds sterling (GBP), which is also the Group's presentation currency, rounded to the nearest million pounds sterling (£m) unless otherwise stated.

Transactions and balances

The Group records an asset, liability, expense or revenue arising from a transaction using the closing exchange rate between the functional and foreign currency on the transaction date. At each subsequent reporting date, the Group translates foreign currency monetary items at the closing rate. Foreign exchange differences arising on translation or settlement of monetary items are recognised in the income statement during the year in which the gains or losses arise.

Foreign currency non-monetary items measured at historical cost are translated at the date of the transaction, with those measured at fair value translated at the date when the fair value is determined. Foreign exchange differences are recognised directly in equity for non-monetary items where any component of associated gains or losses is recognised directly in equity. Foreign exchange differences arising from non-monetary items, whereby the associated gains or losses are recognised in the income statement, are also recognised in the income statement.

1.7 Financial assets and liabilities

Recognition and derecognition

A financial asset or a financial liability is recognised on the balance sheet when the Group becomes party to the contractual provisions of the instrument. Purchases and sales of financial assets classified within fair value through profit or loss are recognised on trade date.

The Group derecognises a financial asset when the contractual cash flows from the asset expire or it transfers the right to receive contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership are transferred. Financial liabilities are derecognised when the Group has discharged its obligation to the contract, or the contract is cancelled or expires.

Offsetting

This can only occur, and the net amount be presented on the balance sheet, when the Group currently has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

1.8 Critical accounting estimates and judgements

The preparation of financial statements requires the use of certain critical accounting estimates and judgements that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosed amount of contingent liabilities. Assumptions made at each balance sheet date are based on best estimates at that date. Although the Group has internal control systems in place to ensure that estimates can be reliably measured, actual amounts may differ from those estimates. The Group considers the most significant use of accounting estimates and judgements relate to the following areas:

- financial assets and liabilities at fair value through profit or loss (note 3.3);
- impairment provisions on credit exposures (note 3.6);
- deferred tax (note 3.11);
- PPI redress provision and other conduct related matters (note 3.14); and
- retirement benefit obligations (note 3.16).

1.9 New accounting standards and interpretations

The Group has adopted the following International Accounting Standards Board (IASB) pronouncements in the current financial year. Except where otherwise stated, these did not have a material impact on the Group's consolidated financial statements:

- amendments to IAS 12: 'Recognition of Deferred Tax Assets for Unrealised Losses' issued in January 2016 and effective for financial years beginning on or after 1 January 2017. The amendments clarify the requirements on the recognition of deferred tax assets for unrealised losses;
- amendments to IAS 7: 'Disclosure initiative' issued in January 2016 and effective for financial years beginning on or after 1 January 2017. The amendments to IAS 7: 'Statement of Cash Flows' require disclosures that enable users of the financial statements to evaluate changes in liabilities arising from an entity's financing activities; and
- 'Annual Improvements to IFRS Standards 2014-2016 Cycle', issued December 2016 and effective for financial years beginning on or after 1 January 2017. The amendment relates to IFRS 12: 'Disclosure of Interests in Other Entities' and clarifies the scope of the standard.

New accounting standards and interpretations not yet adopted

IFRS 9 'Financial Instruments' (issued July 2014) and IFRS 15 'Revenue from Contracts with Customers' (issued September 2015) are both effective for financial years beginning on or after 1 January 2018. IFRS 16 'Leases' was issued in January 2016 and is effective for financial years beginning on or after 1 January 2019. Separate updates on the Group's implementation of these new standards can be found at the end of this section.

There are a number of other standards, interpretations and amendments that have not been applied by the Group in preparing these financial statements as they are either not available for adoption in the EU or are not mandatory for the Group as at 30 September 2018. The pronouncements, while relevant to the Group, are not anticipated to have a material impact and include:

- amendments to IFRS 2: 'Classification and Measurement of Share-based Payment Transactions' issued in June 2016 and effective for financial years beginning on or after 1 January 2018. The amendments provide guidance on the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments; classification of share-based payments with a net settlement feature for withholding tax obligations; and accounting for modifications to a share-based payment that change the classification from cash-settled to equity-settled;
- 'Annual Improvements to IFRS Standards 2014-2016 Cycle', issued December 2016 and effective for financial years beginning on or after 1 January 2018. The amendment relates to IAS 28: 'Investments in Associates and Joint Ventures' and the measurement of an associate or joint venture at fair value;
- IFRIC interpretation 22: 'Foreign Currency Transactions and Advance Consideration', issued December 2016 and effective for financial years beginning on or after 1 January 2018. The new interpretation provides requirements on which exchange rate to use in reporting foreign currency transactions (such as revenue transactions) when payment is made or received in advance;
- amendments to IFRS 9: 'Prepayment Features with Negative Compensation' issued in October 2017 and effective for financial years beginning on or after 1 January 2019. The amendments allow companies to measure particular prepayable financial assets with so-called negative compensation at amortised cost or fair value through other comprehensive income if a specified condition is met, instead of these being measured at fair value through profit or loss. The Group expects to early adopt this amendment with effect from 1 October 2018 in line with the adoption of IFRS 9;
- IFRIC interpretation 23: 'Uncertainty over Income Tax Treatments', issued June 2017 and effective for financial years beginning on or after 1 January 2019. The new interpretation applies to any situation in which there is uncertainty as to whether an income tax treatment is acceptable under tax law and is not limited to actual ongoing disputes;
- 'Annual Improvements to IFRS Standards 2015-2017 Cycle'[(1)], issued December 2017 and effective for financial years beginning on or after 1 January 2019. The IASB has made amendments to the following standards: IFRS 3 'Business Combinations'; IFRS 11 'Joint arrangements'; IAS 12 'Income Taxes'; and IAS 32 'Borrowing Costs';
- amendment to IAS 19: 'Plan amendment, curtailment or settlement'[(1)] issued in February 2018 and effective prospectively for financial years beginning on or after 1 January 2019. The amendments clarify that after a plan event companies should use these updated assumptions to measure current service cost and net interest for the remainder of the reporting period; and
- amendments to references to the 'Conceptual Framework in IFRS Standards'[(1)], issued in March 2018 and effective for financial years beginning on or after 1 January 2020. The amendments were issued following the IASB's publication of a revised version of its Conceptual Framework for Financial Reporting and updates the references in IFRS standards to previous versions of the Conceptual Framework.

(1) Not yet endorsed by the EU.

Financial statements

Notes to the consolidated financial statements

Section 1: Basis of preparation continued

1.9 New accounting standards and interpretations continued

Updates on the implementation of IFRS 9: 'Financial Instruments', IFRS 15: 'Revenue from Contracts with Customers' and IFRS 16: 'Leases'

IFRS 9

IFRS 9 'Financial Instruments' was issued by the IASB in July 2014 and endorsed for use in the EU in November 2016. It is effective for accounting periods beginning on or after 1 January 2018 and replaces IAS 39 'Financial Instruments: Recognition and Measurement' for the Group with effect from 1 October 2018.

In addition, the IASB also issued 'Prepayment Features with Negative Compensation (Amendment to IFRS 9)' in October 2017. This is a narrow scope amendment that enables the use of the amortised cost classification for some financial assets with a prepayable option that could result in the option's holder receiving compensation (referred to as 'negative compensation') for early termination. It is effective for accounting periods beginning on or after 1 January 2019 (with early adoption permitted) and was endorsed for use in the EU in March 2018. The Group will early adopt the amendment to IFRS 9 with effect from 1 October 2018, with no significant impact expected.

Classification and measurement

The existing IAS 39 financial asset classification categories are replaced under IFRS 9 as follows:

Financial assets categories	IAS 39	IFRS 9
Loans and receivables at amortised cost	•	•
Held to maturity (HTM)	•	
Available for sale (AFS)	•	
Fair value through profit or loss (FVTPL)	•	•
Fair value through other comprehensive income (FVOCI)		•

IFRS 9 introduces a two-stage process for the classification of financial assets:

1. The business model assessment

Financial assets with a 'hold to collect' contractual cash flows business model should be classified at amortised cost. Where the business model is 'hold to collect and sell', the financial asset should be classified at fair value through other comprehensive income (FVOCI). To be considered under the FVOCI category, the selling of financial instruments must be integral to the underlying business model.

Final classification is dependent on the financial asset passing the cash flow characteristics assessment. If the financial asset is held in a business model that is neither 'hold to collect' nor 'hold to collect and sell', it must be held at fair value through profit or loss (FVTPL). The option to classify a financial asset at FVTPL under certain circumstances that exists under IAS 39 is also retained in IFRS 9.

2. The cash flow characteristic assessment

The second stage in classification is to assess whether the contractual terms of the financial asset give rise to cash flows which are consistent with that of 'solely payments of principal and interest' (SPPI). IFRS 9 considers financial assets that meet the SPPI criteria as being consistent with a 'basic lending arrangement'.

Any financial asset which fails the SPPI test must be held at FVTPL.

The Group has assessed the financial assets that come under the scope of IFRS 9 and determined that they will transition to IFRS 9 on 1 October 2018 as follows:

	IAS 39			IFRS 9		
Financial assets	Loans and receivables	FVTPL	AFS	Amortised cost	FVTPL	FVOCI
Cash and balances with central banks	●			●		
Due from other banks	●			●		
Listed securities			●			●
Unlisted securities			●		●	
Other financial assets			●		●	
Other financial assets at fair value		●			●	
Derivative financial instruments		●			●	
Loans and advance to customers	●			●		
Due from customers on acceptances	●			●		

The only significant change in classification will be for the Group's Treasury financial assets, which will move from the IAS 39 AFS category to the new FVOCI category under IFRS 9[(1)].

Impairment

The most significant impact of IFRS 9 is the change in credit loss methodology, which moves from the 'incurred loss' basis under IAS 39 to an 'expected loss' basis under IFRS 9.

The single impairment loss methodology (for all financial assets held at either amortised cost or FVOCI) requires the calculation of either a 12-month expected credit loss (ECL) allowance where the financial asset has not experienced a significant increase in credit risk since origination or a lifetime ECL calculation where this significant increase has been observed. Loan commitments and financial guarantees not measured at fair value through profit or loss are also in scope for impairment. IFRS 9 does not define what is meant by a significant increase in credit risk since origination, with the Group exercising judgement in determining how this should be interpreted. The Group has developed a suite of both quantitative and qualitative factors that will determine whether there has been a significant increase in credit risk since origination. Portfolio specific factors are used within the Group's Retail and SME portfolios, with the treatment of customers in receipt of the Group's forbearance programmes being a common trigger in both portfolios that would indicate there has been a significant increase in credit risk since origination. The Group will also utilise the 30 DPD backstop in moving to a lifetime ECL calculation, but expects other triggers to have moved a customer to a lifetime ECL calculation before this point.

The concepts of 12-month and lifetime ECL calculations are not a feature of IAS 39, which requires objective evidence of impairment on a financial asset or group of financial assets due to the identification of a loss event after initial recognition but before the balance sheet date for an impairment loss to be calculated. The move to an expected loss basis will therefore have an initial impact and is generally expected to require an increase in the level of impairment provision held.

IFRS 9 also requires that the ECL calculation reflects an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes; the time value of money; and reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

In meeting this requirement, the Group has incorporated a number of relevant economic parameters within the credit loss models such as base, inflation and unemployment rates. These are included for the full forecast period and will vary between the three economic scenarios the Group will utilise for IFRS 9 purposes (base case, upside and downside). The economic parameters used and the relative weightings of the scenarios are validated internally by an economic scenarios panel which comprises representation from a number of internal stakeholder functions[(2)].

Hedging

While IFRS 9 introduces revised hedge accounting requirements, the IASB is still considering the approach to accounting for dynamic risk management. Consequently, IFRS 9 includes an accounting policy option to continue hedge accounting under the requirements of IAS 39 until such time as the IASB's overall hedge accounting strategy is complete. The Group will exercise the accounting policy option to continue hedge accounting under IAS 39 but will look to provide the new hedge accounting disclosures, where applicable, in the 2019 annual financial statements.

(1) As with the AFS category, fair value movements in the FVOCI category will pass through a reserve account which can be recycled through profit or loss.
(2) This is supplemented by a third-party supplier of economic data.

Financial statements

Notes to the consolidated financial statements

Section 1: Basis of preparation continued

1.9 New accounting standards and interpretations continued

IFRS 9 implementation strategy and transitional impact

During 2018, the Group has continued the development and refinement of IFRS 9 compliant credit loss models. These models adhere to the Group's internal model standards and policies and have been subject to review, challenge and approval from the Group's internal model governance pathway. The IFRS 9 Project team has provided updates to the Board's Audit Committee on a regular basis throughout the year on the outputs from the parallel run process and the improvements in the reporting of the outputs over the same period.

The Group will continue to review and evaluate the credit loss model methodology and overall ECL calculation mechanics and related controls in advance of further IFRS 9 disclosure requirements in 2019. While the Group has calculated the impairment impact of IFRS 9 based on the current view of forward-looking economic conditions and parameters, these are inherently difficult to predict with any great certainty and require an element of management judgement. This is particularly relevant in relation to the eventual outcome of the UK Government's Brexit negotiations, which will not be finalised until March 2019. Consequently, the Group's estimation of expected credit losses under IFRS 9 and the impact this has on results and other related disclosures remain subject to change until finalisation of the Group's results for the year ending 30 September 2019.

The change to the basis of impairment loss provisioning is currently expected to result in a transitional impact of £21m (net of tax) due to the increased level of credit impairments required under IFRS 9 compared with IAS 39. As IFRS 9 does not require the restatement of comparative information, the transitional impact will result in a net decrease in the Group's total equity at 1 October 2018.

The transitional impact of IFRS 9 on the Group's reported CET1 ratio at 1 October 2018 will be a reduction of 14bps(1) on a fully loaded basis. As a result of the transitional capital rules option, which the Group has already confirmed it will exercise(2), the effect on the transitional CET1 ratio is negligible(1).

Transitional disclosures, required by IFRS 7, will be included within the Group's interim financial statements for the six months to 31 March 2019.

IFRS 15

IFRS 15 was issued in May 2014 and is endorsed for use in the EU. It is effective for financial years beginning on or after 1 January 2018 and will be adopted by the Group with effect from 1 October 2018. The core principle of IFRS 15 is that revenue reflects the transfer of goods or services to customers in an amount that reflects the consideration to which an entity expects to be entitled. The standard provides a principles based five-step model for recognition.

The majority of the Group's revenue is in the form of interest income from financial instruments, which is not in scope for IFRS 15. Interest income from lease contracts is also not in scope. Fees and commissions together with certain elements of non-interest income do fall within the scope of the standard. In nearly all cases the Group's current accounting policy is consistent with the requirements of IFRS 15, accordingly there is no material impact in relation to the timing of when the Group recognises revenues.

IFRS 16

IFRS 16 was issued in January 2016 and is endorsed for use in the EU. It is effective for financial years beginning on or after 1 January 2019 and will be adopted by the Group with effect from 1 October 2019. For lessees, operating leases will be brought onto the Group's balance sheet with an asset recognised for the contractual 'right of use' and a financial liability recognised for the contractual payments. This change will mainly impact the properties that the Group currently accounts for as operating leases. There are no substantial changes to the accounting for leases by lessors, nor for finance leases. An implementation plan is in place and the Group continues to assess the impact of the standard.

(1) Unaudited.
(2) This has the effect on phasing the Day 1 impact of the transition to IFRS 9 over five years for capital purposes, with 95% of the impact added back in the first year.

Section 2: Results for the year

2.1 Segment information

The Group's operating segments are operating units engaged in providing different products or services and whose operating results and overall performance are regularly reviewed by the Group's Chief Operating Decision Maker, the Executive Leadership Team.

The Group's business is organised into two principal operating segments: SME banking and Retail banking. In addition, Central Functions consist of the Group's back office support functions.

SME banking

The Group's established regional SME franchise offers a full range of banking products and services to meet business customers' banking needs across its small business, commercial, corporate and structured finance segments.

The Group's SME franchise comprises small businesses (which the Group defines as businesses with lending of up to £0.5m but less than £2.0m in turnover) and medium businesses (which the Group defines as businesses with lending of more than £0.5m and greater than £2.0m in turnover).

Through its SME franchise, the Group offers a full range of lending products and services across a portfolio consisting of term lending, overdrafts and working capital solutions:

- term lending: the Group offers a wide variety of term loans, both secured and unsecured, and offers customers a range of repayment and interest rate options. The majority of the Group's business term lending is London Interbank Offered Rate (LIBOR) based;
- overdrafts: business overdrafts are the primary type of revolving variable rate credit facility offered by the Group to business customers;
- invoice finance: the Group advances funds against the customer's trade receivables;
- asset finance: these products provide a method of financing capital equipment purchases;
- international trade services: these products facilitate transactions between a buyer and seller located in different countries. The Group offers import loans, export loans, documentary collections and currency guarantees, together with letters of credit for securing trade; and
- business current accounts: the Group provides business customers day to day banking, current account facilities (including debit cards, cheque books, regular statements, direct debits and standing orders), and online banking.

Retail banking

The Group has a comprehensive regional and national retail banking product proposition comprising:

- PCA: the Group offers a full range of PCAs, including, for example, B, a digital proposition, together with a packaged bank account and a basic bank account;
- savings accounts: the Group offers a variety of savings accounts that pay a variable rate of interest. It also offers cash ISAs that provide depositors tax free returns;
- term deposits: offer a fixed interest rate for a fixed term;
- mortgages: the Group provides mortgage loans on a capital repayment basis, where the loan is required to be repaid during its life, and on an interest-only basis, where the customer pays interest during the term of the mortgage loan with the principal balance required to be repaid in full at maturity. The Group offers both owner occupied mortgage loans and BTL loans;
- personal loans: the Group provides unsecured personal loans through its branch network and through its digital and telephone distribution channels;
- credit cards: the Group currently offers four credit card products: Private Mastercard, Business Mastercard, Gold Mastercard and B Mastercard;
- overdrafts: the Group provides overdraft lending across a variety of PCA products, subject to the account holder's status; and
- introductions to insurance and investment products through its branch network.

Financial statements

Notes to the consolidated financial statements

Section 2: Results for the year continued

2.1 Segment information continued

Geographical areas

The Group has no operations outside the UK and therefore no secondary geographical area information is presented.

Operating segments 2018	SME banking £m	Retail banking £m	Central functions £m	Other[1] £m	Total £m
Net interest income	**261**	**641**	**(51)**	**–**	**851**
Non-interest income	**76**	**99**	**(19)**	**–**	**156**
Total operating income	**337**	**740**	**(70)**	**–**	**1,007**
Operating and administrative expenses	**(63)**	**(94)**	**(478)**	**(495)**	**(1,130)**
Impairment losses on credit exposures[2]	**(15)**	**(26)**	**–**	**–**	**(41)**
Segment operating profit/(loss) before tax	**259**	**620**	**(548)**	**(495)**	**(164)**
Average interest earning assets	**7,391**	**25,198**	**6,828**	**–**	**39,417**

Operating segments 2017	SME banking £m	Retail banking £m	Central functions £m	Other[1] £m	Total £m
Net interest income	251	644	(51)	–	844
Non-interest income	83	100	(11)	20	192
Total operating income	334	744	(62)	20	1,036
Operating and administrative expenses	(61)	(97)	(517)	(45)	(720)
Impairment losses on credit exposures[2]	(33)	(15)	–	–	(48)
Segment operating profit/(loss) before tax	240	632	(579)	(25)	268
Average interest earning assets	7,209[3]	23,522[3]	6,966	–	37,697

(1) 'Other' reflects underlying adjustments to the statutory view of performance and is therefore not recharged to the Group's two principal operating segments, such as conduct related provisions and restructuring costs. For a breakdown of the items included in this category, refer to 'Measuring financial performance – glossary'.

(2) The impairment losses on credit exposures of £26m (2017: £15m) for Retail banking includes losses on certain retail products attributable to SME (private banking) customers.

(3) Comparative disclosures have been amended to conform with the current period's presentation.

Liabilities are managed on a centralised basis and therefore are not disclosed by segment.

2.2 Net interest income

Accounting policy

Interest income is reflected in the income statement using the effective interest method which discounts the estimated future cash payments or receipts over the expected life of the financial instrument, to the net carrying amount of the financial asset or liability.

When calculating the effective interest rate, cash flows are estimated considering all contractual terms of the financial instrument (e.g. prepayment, call and similar options) excluding future credit losses. The calculation includes all amounts paid or received that are an integral part of the effective interest rate such as transaction costs and all other premiums or discounts. Where it is not possible to reliably estimate the cash flows or the expected life of a financial instrument (or group of financial instruments), the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments) are used.

Loan origination and commitment fees are recognised within the effective interest rate calculation. Non-utilisation of a commitment fee is recognised as revenue upon expiry of the agreed commitment period. Loan related administration and service fees are recognised as revenue over the period of service.

Interest income and interest expense on hedged assets and liabilities and financial assets and liabilities designated as fair value through profit or loss are also recognised as part of net interest income.

Where a trading derivative is economically hedging an interest-bearing financial asset or liability designated at fair value through profit or loss, the interest income and expense attributable to the derivative is recognised within net interest income (in a manner consistent with hedging derivatives) and not as part of the fair value movement of the trading derivative.

	2018 £m	2017 £m
Interest income and similar income		
Loans and advances to other banks	**26**	11
Financial assets available for sale	**12**	11
Loans and advances to customers	**1,057**	1,030
Financial assets at fair value through profit or loss	**15**	18
Other interest income	**3**	5
Total interest income and similar income	**1,113**	1,075
Less: interest expense and similar charges		
Due to other banks	**18**	15
Due to customers	**148**	126
Debt securities in issue	**94**	90
Other interest expense	**2**	–
Total interest expense and similar charges	**262**	231
Net interest income	**851**	844

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Notes to the consolidated financial statements

Section 2: Results for the year continued

2.3 Non-interest income

Accounting policy

Gains less losses on financial instruments at fair value

This includes fair value gains and losses from three distinct activities:

- derivatives classified as held for trading – the full change in fair value of trading derivatives is recognised inclusive of interest income and expense arising on those derivatives except when economically hedging other assets and liabilities at fair value as outlined in note 2.2;
- other financial assets and liabilities designated at fair value through profit or loss – these relate to the Group's fixed interest rate loan portfolio and related term deposits (note 3.3), which were designated at inception as fair value through profit or loss. The fair value of these loans is derived from the future loan cash flows using appropriate discount rates and includes adjustments for credit risk and credit losses. The valuation technique used is reflective of current market practice; and
- hedged assets, liabilities and derivatives designated in hedge relationships – fair value movements are recognised on both the hedged item and hedging derivative in a fair value hedge relationship (the net of which represents hedge ineffectiveness), and hedge ineffectiveness on cash flow hedge relationships (note 3.4).

Fees and commissions

Where not integral to the effective interest rate, these are recognised on an accruals basis as the services are provided or on completion of the underlying transaction.

	2018 £m	2017 £m
Gains less losses on financial instruments at fair value		
Interest rate derivatives	**16**	45
Other assets and liabilities at fair value(1)	**(13)**	(35)
Ineffectiveness arising from fair value hedges (note 3.4)	**–**	(4)
Ineffectiveness arising from cash flow hedges (note 3.4)	**(6)**	–
	(3)	6
Other operating income		
Fees and commissions	**141**	146
Margin on foreign exchange derivative brokerage	**18**	18
Gains on disposal of available for sale financial assets	**–**	20
Net fair value movement on investment properties	**–**	(1)
Other income	**–**	3
	159	186
Total non-interest income	**156**	192

(1) A credit risk gain on other assets and liabilities at fair value of £3m, offset by a fair value loss of £16m, has been recognised in the current year (2017: £6m gain and £41m loss, respectively).

On 28 April 2017, Mastercard completed its acquisition of 94.2% of VocaLink, resulting in a gain of £20m, which was included within 'Gains on disposal of available for sale financial assets' in the year ended 30 September 2017.

2.4 Operating and administrative expenses

Accounting policy

Personnel expenses primarily consist of wages and salaries, accrued bonus and social security costs arising from services rendered by employees during the financial year.

The Group recognises bonus costs where it has a present obligation that can be reliably measured. Bonus costs are recognised over the relevant service period required to entitle the employee to the reward.

The Group's accounting policies on pension expenses and equity based compensation are included in notes 3.16 and 4.2 respectively.

	2018 £m	2017 £m
Personnel expenses	**223**	166
Restructuring and related expense (note 3.14)	**38**	67
Virgin Money acquisition costs	**37**	–
RBS alternative remedies package spend	**16**	–
Depreciation and amortisation expense (notes 3.8, 3.10)	**89**	87
Other operating and administration expenses	**727**	400
Total operating and administrative expenses	**1,130**	720

Personnel expenses comprise the following items:

	2018 £m	2017 £m
Salaries, wages and non-cash benefits and social security costs	**139**	171
Defined contribution pension expense	**33**	19
Defined benefit pension expense/(income) (note 3.16)	**2**	(54)
Equity based compensation (note 4.2)	**9**	6
Other personnel expenses	**40**	24
Personnel expenses	**223**	166

In the year to September 2017, the Group recognised gains in relation to its defined benefit pension scheme. A past service credit of £88m was included in personnel expenses as a result of the closure of the Scheme to future accrual for the majority of members. In addition, a curtailment gain of £13m was recognised in respect of redundancies which did not attract an enhancement entitlement and was offset against the related restructuring costs.

The average number of FTE employees of the Group during the year was made up as follows:

	2018 Number	2017 Number
Managers	**2,161**	2,234
Clerical staff	**3,608**	3,806
	5,769	6,040

The average monthly number of employees was 6,461 (2017: 6,818).

All staff are contracted employees of the Group and its subsidiary undertakings. The average figures above do not include contractors.

Other items of significance to the Group which are included within other operating and administrative expenses are:

	2018 £m	2017 £m
Operating lease charges	**26**	29
PPI redress expense (note 3.14)	**352**	48
Other conduct expenses (note 3.14)	**44**	10
Separation costs	**8**	8
Auditor's remuneration	**3**	2

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Notes to the consolidated financial statements

Section 2: Results for the year continued

2.4 Operating and administrative expenses continued

Auditor's remuneration included within other operating and administrative expenses:

	2018 £'000	2017 £'000
Fees payable to the Company's auditor for the audit of the Company's financial statements	**21**	20
Fees payable to the Company's auditor for the audit of the Company's subsidiaries	**1,593**	1,251
Total audit fees	**1,614**	1,271
Audit related assurance services	**120**	124
Other assurance services	**700**	308
Total non-audit fees	**820**	432
Fees payable to the Company's auditor in respect of associated pension schemes	**84**	63
Total fees payable to the Company's auditor	**2,518**	1,766

Non-audit services of £820k (2017: £432k) performed by the auditor during the year included the review of the Interim Financial Report; agreed upon procedures under the Conduct Indemnity arrangement with NAB; preparation of a comfort letter for the global medium-term note programme issuance; and a TFS assurance review. The increase in the year is principally due to reporting accountant procedures in relation to the Virgin Money transaction.

In addition to the above, out of pocket expenses of £49k (2017: £48k) were borne by the Group, principally related to reimbursement of travel expenses incurred by staff when performing the above services.

2.5 Taxation

Accounting policy

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it is related to items recognised directly in equity, in which case the tax is also recognised in equity.

Current tax is the expected tax payable or receivable on the taxable profit or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years. Deferred tax assets and liabilities are recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax is determined using tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

	2018 £m	2017 £m
Current tax		
UK corporation tax		
Current year	**8**	17
Adjustment in respect of prior years	**8**	–
	16	17
Deferred tax (note 3.11)		
Current year	**(1)**	64
Adjustment in respect of prior years	**(34)**	5
	(35)	69
Tax (credit)/expense for the year	**(19)**	86

The tax assessed for the year differs from that arising from applying the standard rate of corporation tax in the UK of 19%. A reconciliation from the expense implied by the standard rate to the actual tax expense is as follows:

	2018 £m	2017 £m
(Loss)/profit on ordinary activities before tax	**(164)**	268
Tax (credit)/expense based on the standard rate of corporation tax in the UK of 19% (2017: 19.5%)	**(31)**	52
Effects of:		
Disallowable expenses	**42**	9
Conduct indemnity adjustment	**(5)**	7
Deferred tax assets recognised	**(8)**	(21)
Impact of rate changes	**9**	34
Adjustments in respect of prior years	**(26)**	5
Tax (credit)/expense for the year	**(19)**	86

The total amount of tax, current and deferred, recognised directly in equity during the year was a credit of £23m (2017: £1m). Disallowable expenses represent, in the main, the Group's share of incremental conduct charges that are not deductible in computing taxable profits, and non-deductible transaction costs predominantly in relation to the acquisition of Virgin Money.

The prior year adjustment comprises movements in the deferred tax asset recognised for losses following the enactment of the Corporate Loss Restriction in Finance Act (No.2) 2017 in November 2017. These rules allowed, for the first time, certain losses to be relieved against the profits of group entities other than the one in which they arose, and also changed the order of precedence for relief of existing losses. The consequence of this change was that historic losses which were previously derecognised are now brought onto the balance sheet in accordance with the Group's established methodology. The remainder of the prior year adjustment relates to the revaluation of the conduct indemnity adjustment, and incorporates a fully offsetting movement between current and deferred tax.

The rate change charge arises on the revaluation of assets as a consequence of the UK mainstream rate of tax trending towards the enacted rate of 17%, and where deferred tax assets have been utilised at rates lower than initially forecast.

2.6 Earnings per share (EPS)

Accounting policy

Basic earnings per share

Basic earnings per share is calculated by taking the profit attributable to ordinary shareholders of the parent company and dividing this by the weighted-average number of ordinary shares outstanding during the period.

Diluted earnings per share

This requires the weighted average number of ordinary shares in issue to be adjusted to assume conversion of all dilutive potential ordinary shares. These arise from awards made under equity based compensation schemes. Share awards with performance conditions attaching to them are not considered to be dilutive unless these conditions have been met at the reporting date.

The Group presents basic and diluted (loss)/earnings per share data in relation to the ordinary shares of CYBG PLC.

	2018 £m	2017 £m
(Loss)/profit attributable to ordinary shareholders	**(181)**	146
Tax relief on AT1 distribution attributable to ordinary equity holders	**7**	7
(Loss)/profit attributable to ordinary equity holders for the purposes of basic and diluted EPS	**(174)**	153

	2018 Number of shares (million)	2017 Number of shares (million)
Weighted-average number of ordinary shares in issue		
– Basic	**885**	883
– Diluted	**885**	884
Basic (loss)/earnings per share (pence)	**(19.7)**	17.3
Diluted (loss)/earnings per share (pence)	**(19.7)**	17.2

The calculation of the diluted earnings per share for the current year end excludes conditional awards of over 1m ordinary shares made under equity based compensation schemes. These are considered anti-dilutive due to the Group making a loss in the year.

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Section 3: Assets and liabilities

3.1 Cash and balances with central banks

	2018 £m	2017 £m
Cash assets	**1,656**	1,507
Balances with central banks (including EU payment systems)	**4,917**	5,430
	6,573	6,937
Less mandatory deposits with central banks[1]	**(75)**	(44)
Included in cash and cash equivalents (note 5.2)	**6,498**	6,893

(1) Mandatory deposits are not available for use in the Group's day to day business and are non-interest bearing.

3.2 Financial assets available for sale

Accounting policy

Available for sale financial assets are recognised on trade date and comprise listed and unlisted non-derivative financial assets not classified into any other financial asset category. They are initially recognised at fair value including direct and incremental transaction costs, and subsequently measured at fair value. Gains and losses arising from changes in fair value are included as a separate component of equity until sale or impairment, at which point the cumulative gain or loss is transferred to the income statement.

All available for sale financial assets are continually monitored for evidence of any impairment, which would typically be deemed to have arisen where there is evidence of a significant or prolonged reduction in the fair value of the security below its cost. Where such evidence of impairment exists, the cumulative net loss previously recognised directly in equity is transferred to the income statement.

In situations where evidence suggests a subsequent increase in value, reversals of impairment of previously impaired equity instruments are recognised directly in equity while reversals of impairment of debt instruments are recognised in the income statement.

Interest income, determined using the effective interest method, is recognised in the income statement. Impairment losses and translation differences on monetary items are recognised in the income statement within the year in which they arise.

	2018 £m	2017 £m
Listed securities	**1,551**	2,066
Unlisted securities	**5**	4
Other financial assets	**6**	6
	1,562	2,076

Refer to note 3.18 for further information on the valuation methodology applied to available for sale assets and their classification within the fair value hierarchy.

Credit quality of investments

	2018 £m	2017 £m
Available for sale		
Senior investment grade	**1,551**	2,066
Other	**11**	10
	1,562	2,076

Senior investment grade securities

These include £595m (2017: £1,221m) of UK Government Gilts. The remainder relates to highly liquid, AAA-rated corporate bonds.

3.3 Financial assets and liabilities at fair value through profit or loss

Accounting policy

Financial assets and liabilities are designated at fair value through profit or loss, with gains and losses recognised in the income statement as they arise (note 2.3), when this reduces an accounting mismatch or where the performance is evaluated on a fair value basis. In such cases, transaction costs are recognised immediately in the income statement upon initial recognition of the financial asset and liability.

The derivatives related to the assets and liabilities at fair value through profit or loss do not meet the requirements for hedge accounting and are accounted for as held for trading derivative financial instruments (note 3.4).

Critical accounting estimates and judgements

Where the fair values of financial assets and financial liabilities recorded on the balance sheet cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where such data is not available, judgement is required to establish fair values. The judgements include considerations of liquidity and credit risk.

The most significant judgement is in relation to the Group's fair value loan portfolio. The most significant unobservable input impacting the carrying value of the loans other than interest rates is the future expectation of credit losses. If the lifetime expected losses were 20% greater than predicted, the carrying value of the loans would decrease by £2m and vice versa.

	2018 £m	2017 £m
Financial assets at fair value through profit or loss		
Loans and advances	**362**	477
Financial liabilities at fair value through profit or loss		
Due to customers – term deposits	**15**	26

Loans and advances

Included in financial assets at fair value through profit or loss is a historical portfolio of loans (sales ceased in 2012). Interest rate risk associated with these loans is managed using interest rate derivative contracts and the loans are recorded at fair value to avoid an accounting mismatch. The maximum credit exposure of the loans is £362m (2017: £477m) including accrued interest receivable of £2m (2017: £2m). The cumulative loss in the fair value of the loans attributable to changes in credit risk amounts to £8m (2017: £11m) and the change for the current year is a decrease of £3m (2017: decrease of £13m), of which £3m (2017: £6m) has been recognised in the income statement.

Due to customers – term deposits

Included in other financial liabilities at fair value through profit or loss are fixed rate deposits, the interest rate risk on which is hedged using interest rate derivative contracts. The deposits are recorded at fair value to avoid an accounting mismatch.

The change in fair value attributable to changes in the Group's credit risk is £Nil (2017: £Nil). The Group is contractually obligated to pay £0.3m (2017: £1m) less than the carrying amount at maturity to the deposit holder.

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.4 Derivative financial instruments

Accounting policy

All derivative instruments manage exposures to interest rates and foreign currency and are recognised on the balance sheet at fair value on trade date. The carrying value of a derivative is measured at fair value throughout the life of the contract. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative. The notional amount of a derivative contract is not recorded on the balance sheet but is disclosed as part of this note.

The method of recognising the fair value gain or loss on a derivative depends on whether it is designated as a hedging instrument and the nature of the item being hedged. Certain derivatives are designated as either hedges of highly probable future cash flows attributable to a recognised asset or liability, or a highly probable forecast transaction (a cash flow hedge); or hedges of the fair value of recognised assets or liabilities or firm commitments (a fair value hedge).

Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in equity. Specifically, the separate component of equity (note 4.1) is adjusted to the lesser of the cumulative gain or loss on the hedging instrument, and the cumulative change in fair value of the expected future cash flows on the hedged item from the inception of the hedge. Any remaining gain or loss on the hedging instrument is recognised in the income statement. The carrying value of the hedged item is not adjusted. Amounts accumulated in equity are transferred to the income statement in the period in which the hedged item affects profit or loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

Fair value hedge

The carrying value of the hedged item on initial designation is adjusted for the fair value attributable to the hedged risk. Subsequently, changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The movement in the fair value of the hedged item attributable to the hedged risk is made as an adjustment to the carrying value of the hedged asset or liability.

Where the hedged item is derecognised from the balance sheet, the adjustment to the carrying amount of the asset or liability is immediately transferred to the income statement. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item is amortised to the income statement on an effective interest basis over the remaining life of the asset or liability.

Hedge effectiveness

The Group documents, at the inception of a transaction, the relationship between hedging instruments and the hedged items, and the Group's risk management objective and strategy for undertaking these hedge transactions. The documentation covers how effectiveness will be measured throughout the life of the hedge relationship and its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. A hedge is expected to be highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated are expected to offset in a range of 80% to 125%.

Derivatives held for trading

The Group uses derivatives for risk management purposes and does not have a trading book. However, derivatives that do not meet the hedging criteria within IAS 39, or for which hedge accounting is not applied, are classified as held for trading. Changes in value of held for trading derivatives are immediately recognised in the income statement (note 2.3).

The tables below analyse derivatives between those designated as hedging instruments and those classified as held for trading:

	2018 £m	2017 £m
Fair value of derivative financial assets		
Designated as hedging instruments	**203**	202
Designated as held for trading	**59**	80
	262	282
Fair value of derivative financial liabilities		
Designated as hedging instruments	**259**	229
Designated as held for trading	**102**	147
	361	376

Cash collateral on derivatives placed with banks totalled £306m (2017: £338m). Cash collateral received on derivatives totalled £37m (2017: £31m). These amounts are included within due from and due to other banks respectively.

The derivative financial instruments held by the Group are further analysed below. The notional contract amount is the amount from which the cash flows are derived, and does not represent the principal amounts at risk relating to these contracts.

Total derivative contracts

	Notional contract amount 2018 £m	Fair value of assets 2018 £m	Fair value of liabilities 2018 £m	Notional contract amount 2017 £m	Fair value of assets 2017 £m	Fair value of liabilities 2017 £m
Derivatives designated as hedging instruments						
Cash flow hedges						
Interest rate swaps	**24,570**	**88**	**111**	17,952	56	104
Cross currency swaps	**690**	**70**	**–**	527	89	–
Forward foreign exchange	**–**	**–**	**–**	6	–	–
	25,260	**158**	**111**	18,485	145	104
Fair value hedges						
Interest rate swaps	**2,180**	**45**	**148**	1,452	57	125
Derivatives designated as held for trading						
Foreign exchange rate related contracts						
Spot and forward foreign exchange	**1,788**	**26**	**23**	2,689	45	47
Cross currency swaps	**455**	**10**	**10**	150	9	9
Options	**11**	**–**	**–**	103	2	2
	2,254	**36**	**33**	2,942	56	58
Interest rate related contracts						
Swaps	**811**	**15**	**59**	983	18	82
Swaptions	**33**	**–**	**–**	33	–	–
Options	**501**	**1**	**3**	477	2	3
	1,345	**16**	**62**	1,493	20	85
Commodity related contracts	**53**	**7**	**7**	93	4	4
Total derivative contracts	**31,092**	**262**	**361**	24,465	282	376

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.4 Derivative financial instruments continued

Derivatives traded to manage the Group's interest rate exposure on a net portfolio basis are accounted for as cash flow hedges. Derivatives traded to manage interest rate risk on certain fixed rate assets, such as UK Government Gilts, are accounted for as fair value hedges.

The Group hedging positions also include those designated as foreign currency and interest rate hedges of debt issued from the Group's securitisation and covered bond programmes respectively. As such, certain derivative financial assets and liabilities have been booked in structured entities and consolidated within these financial statements.

Cash flow hedged derivatives include vanilla interest rate swaps within macro hedges and cross currency swaps within a structured entity. The Group has notional commitments in the following periods:

Nominal values per time period	2018 £m	2017 £m
Within 0 to 3 months	**2,582**	92
Between 3 and 12 months	**7,325**	2,986
1 to 5 years	**14,882**	14,817
Greater than 5 years	**471**	590
	25,260	18,485

The Group has hedged forecast future cash flows, which vary primarily with interest or foreign exchange rates. These cash flows are expected to impact the income statement in the following periods:

	Forecast receivable cash flows 2018 £m	Forecast payable cash flows 2018 £m	Forecast receivable cash flows 2017 £m	Forecast payable cash flows 2017 £m
Within 1 year	**109**	**283**	52	399
Between 1 and 2 years	**130**	**366**	70	86
Between 2 and 3 years	**108**	**160**	70	86
Between 3 and 4 years	**63**	**5**	44	122
Between 4 and 5 years	**37**	**3**	19	6
Greater than 5 years	**60**	**10**	26	18
	507	**827**	281	717

	2018 £m	2017 £m
Gain/(loss) arising from fair value hedges (note 2.3)		
Hedging instrument	**14**	1
Hedged item attributable to the hedged risk	**(14)**	(5)
	–	(4)

	2018 £m	2017 £m
Loss from cash flow hedges due to hedge ineffectiveness (note 2.3)	**(6)**	–

3.5 Loans and advances to customers

Accounting policy

Loans and advances to customers arise when the Group provides money directly to a customer and include mortgages, term lending, overdrafts, credit card lending, lease finance and invoice financing.

Loans and advances to customers are initially recognised at fair value including direct and incremental transaction costs. They are subsequently measured at amortised cost, using the effective interest method, adjusted for impairment losses. They are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership.

Leases entered into by the Group as lessor, where the Group transfers substantially all the risks and rewards of ownership to the lessee, are classified as finance leases. The leased asset is not held on the Group balance sheet; instead, a finance lease is recognised representing the minimum lease payments receivable under the terms of the lease, discounted at the rate of interest implicit in the lease. Interest income is recognised in interest receivable, allocated to accounting periods to reflect a constant periodic rate of return.

	2018 £m	2017 £m
Mortgages	**24,540**	23,480
Term lending – SME	**5,009**	4,762
Term lending – Retail	**767**	709
Overdrafts	**1,525**	1,524
Lease finance	**660**	594
Credit cards	**381**	396
Trade finance	**35**	23
Gross loans and advances to customers	**32,917**	31,488
Accrued interest receivable	**79**	75
Unearned income	**(32)**	(28)
Deferred and unamortised fee income	**(25)**	(32)
Impairment provisions on credit exposures (note 3.6)	**(195)**	(210)
	32,744	31,293

The Group has transferred a proportion of mortgages to the securitisation and covered bond programmes (note 3.7).

The Group has a portfolio of fair valued business loans of £362m (2017: £477m) which are held separately as Other financial assets at fair value on the balance sheet (note 3.3). Combined with the above this is equivalent to total loans and advances of £33,106m (2017: £31,770m).

Lease finance

The Group leases a variety of assets to third parties under finance lease arrangements, including vehicles and general plant and machinery. The cost of assets acquired by the Group during the year for the purpose of letting under finance leases and hire purchase contracts amounted to £20m (2017: £13m) and £399m (2017: £408m) respectively. The total receivables from finance leases and hire purchase contracts were £32m (2017: £17m) and £596m (2017: £550m) respectively.

Finance lease and hire purchase receivables

	2018 £m	2017 £m
Gross investment in finance lease and hire purchase receivables		
Due within 1 year	**269**	241
Due within 1 to 5 years	**376**	346
Due after more than 5 years	**15**	7
	660	594
Unearned income	**(32)**	(27)
Net investment in finance lease and hire purchase receivables	**628**	567

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.6 Impairment provisions on credit exposures

Accounting policy

Assets carried at amortised cost

At each reporting date the Group assesses if there is objective evidence of impairment of a financial asset or group of financial assets due to one or more loss events that occurred after initial recognition but prior to the balance sheet date. Examples of loss events are (i) where there has been an actual breach of contract by the borrower such as a default or delinquency in payment of interest or principal; or (ii) the granting of a concession to the borrower that the Group would not otherwise consider.

The Group first assesses whether objective evidence of impairment exists either individually for assets that are separately significant, or collectively for assets that are not separately significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and collectively assessed for impairment ('collective provisions').

Collective provisions

Collective provisions are generally established for homogeneous portfolios such as the Retail portfolios and the small business portfolio within the SME franchise.

Within the Group's Retail environment, past loss experience is a key factor in determining an appropriate collective provision level and takes into account a number of different elements including:

– the number of days past due;
– the realisable value of any security held; and
– the timing of any such security sale.

These and other factors will influence the probability that the customer defaults on the loan (the PD). In the event of a default occurrence, the Retail collective provision calculator provides the amount the Group expects to be irrecoverable from that customer (the LGD). The level and impact of LGD varies significantly between the Group's secured and unsecured lending portfolios.

Collective provisioning for the Group's SME portfolio is also based on the use of PD and LGD. The assets are included in a group of financial assets with similar risk characteristics and collectively assessed for impairment. The modelled collective assessment considers factors such as:

– credit quality;
– levels of arrears;
– credit utilisation;
– loan to collateral ratios; and
– other factors including the Group's internal customer rating system (eCRS).

These characteristics are relevant to the estimation of future cash flows for groups of such assets as they are indicative of the borrower's ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Reliance is placed on the eCRS rating when assessing PD as these are directly mapped within the model. Manual interventions to the eCRS rating, such as the placement on a watch list, will directly lead to an increase in PD and consequently the level of collective provision required. LGD assumptions are driven by the level of security assigned to the customer within the collective provisioning model. These are regularly monitored to ensure comparability with recent actual loss experience.

In addition, for both the Group's Retail and SME portfolios, experienced judgement is used to estimate the amount of an impairment loss. This reflects a limited number of refinements that have been assessed as necessary to reflect specific and evolving circumstances that, by their nature, cannot be adequately captured in the models. The use of judgements and supportable estimates is considered by management to be an essential part of the credit impairment process. The methodology and assumptions used for estimating future cash flows are reviewed regularly to identify and reduce any significant differences between loss estimates and actual loss experience.

Specific provision
If there is objective evidence that an impairment loss has been incurred on a loan, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (including the estimated realisable value of any security) discounted at the asset's original effective interest rate (a 'specific provision').

Specific provision allowances are primarily established against the Group's commercial business within the SME franchise. Assets are reviewed on a regular basis and those showing potential or actual vulnerability are placed onto a watch list where enhanced monitoring is undertaken.

Impairment
When first recognised, the impairment allowance, which is a combination of both the collective and specific provision, is recognised in the income statement.

Following impairment, interest income is recognised using the original effective rate of interest which was used to discount the future cash flows for the purpose of measuring the impairment loss. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. The amount of the reversal is recognised in the income statement.

When a loan is deemed uncollectable, and all necessary internal procedures have been completed, it is written off against the related impairment loss. Subsequent recoveries of amounts previously written off reduce the expense in the income statement.

The Group's impairment policy for available for sale financial assets is included in note 3.2.

Critical accounting estimates and judgements
In determining the required level of collective impairment provisions, the Group uses the output from various statistical models, with management judgement required to assess the modelled outputs and, where necessary, make appropriate adjustments.

The key assumptions within the Group's collective provisioning models which give rise to significant estimation uncertainty are the PD and the LGD. Both measures are predicated on expectations of customer behaviour and performance, which requires management to form a judgement based on a wide range of historic and current evidence. The actual amount of the future cash flows and their timing may differ significantly from the assumptions made for the purposes of determining the impairment allowances and consequently these allowances can be subject to variation as time progresses and the circumstances of the customer become clearer.

From an SME perspective, changes made to eCRS will have a direct impact as these are mapped to PDs. Assumption changes on retail customer behaviour will also have an impact on the PDs used.

Within the Retail portfolio, the Group's collective provision is reflective of the fact that the majority of lending is concentrated on customer mortgages, where the available security is generally sufficient to cover the exposure. This differs from the SME portfolio where the availability and strength of the security will have less of an impact on overall recoveries, leading to a potentially higher collective provision charge relative to the overall exposure.

Sensitivities within the collective provision
There are interactions between the various assumptions within the provisioning models which mean that no single factor is likely to move independent of others; however, the sensitivities disclosed below assume all other assumptions remain unchanged.

If the PDs were to move by +/- 5% from those presently used within the Group's provisioning models, the impairment provision would increase/decrease accordingly by £5m.

An important element to the PD is the loss emergence period (LEP) which represents the Group's assessment of the period from when a loss event occurs to eventual default. The impact of the LEP differs between the Group's Retail and SME portfolios.

A two-month increase in the LEP would result in a further £2m impairment provision within the SME portfolio, and a further £3m being added to the Retail impairment provision.

To the extent that recovery rates improve from those presently used within each of the Group's provisioning models by 5%, the impairment provision on loans and advances would decrease by £14m. Alternatively, if recovery rates deteriorate by 5%, the impairment provision on loans and advances would increase by £24m.

Provision in the SME portfolio is sensitive not only to default rates and severity of losses, but also to the assessment of risk and security. If 10% of the SME portfolio were to fall by one notch, the impairment provision would increase by £2m.

In addition to modelled outputs, the impairment provision is further impacted by management judgements. These include judgements that reflect elements which are not sufficiently sensitive to the current economic conditions, model risk reserves that are held to cover against a range of potential model limitations, and judgements made in respect of potential recoveries for specific provisions which also involve customer and economic specific conditions. These management judgements do not allow for any meaningful sensitivity comparison.

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.6 Impairment provisions on credit exposures continued

	2018 £m	2017 £m
Opening balance	**210**	215
Charge for the year	**41**	48
Amounts written off	**(68)**	(75)
Recoveries of amounts written off in previous years	**13**	18
Other(1)	**(1)**	4
Closing balance	**195**	210
Specific	**43**	56
Collective	**152**	154
	195	210

(1) Other includes the unwind of net present value elements of specific provisions and other minor movements.

3.7 Securitisation and covered bond programmes

Accounting policy

The Group sponsors the formation of structured entities, primarily for the purpose of facilitation of asset securitisation and covered bond transactions to accomplish certain narrow and well-defined objectives. Although the Group has no shareholding in these entities, where it is exposed, or has rights, to variable returns from its involvement with the entities and it has the ability to affect those returns through its power over the entity, they are regarded as controlled entities as described in note 1.5 and are consolidated in the Group's financial statements.

Securitisation

The Group has securitised a portion of its retail mortgage loan portfolio under the Group's master trust securitisation programmes. The securitised mortgage loans have been assigned at principal value to bankruptcy remote structured entities. These structured entities have been funded through the issue of RMBS to third-party institutional debt investors. The Group is entitled to any residual income from the vehicles after the debt obligations and senior expenses of the programmes have been met. The securitised debt holders have no recourse to the Group other than the principal and interest (including fees) generated from the securitised mortgage loan portfolio. The Group continues servicing these mortgage loans in return for an administration fee.

The mortgage loans do not qualify for derecognition because the Group remains exposed to the majority of the risks and rewards of the mortgage loan portfolio, principally the associated credit risk. The securitisation structured entities are consolidated and the securitised mortgage loans retained on the Group's balance sheet. A liability is recognised for the proceeds of the funding transaction. The externally held securitised notes in issue are included within debt securities in issue (note 3.15). There are a number of notes held internally by the Group, not recognised on the balance sheet, which are used as collateral for repurchases and similar transactions or for credit enhancement purposes.

Covered bond

A subset of the Group's retail mortgage loan portfolio has been ring fenced and assigned to a bankruptcy remote limited liability partnership, Clydesdale Covered Bond 2 LLP, associated with the covered bond programme, to provide a guarantee for the obligations payable on the covered bonds issued by the Group. Similar to the securitisation programmes, the Group is entitled to any residual income after all payment obligations due under the terms of the covered bonds and senior programme expenses have been met.

The Group continues servicing these mortgage loans in return for an administration fee.

The mortgage loans do not qualify for derecognition because the Group retains all of the risks and rewards of the mortgage loan portfolio. The covered bond partnership is consolidated with the mortgage loans retained on the consolidated balance sheet and the covered bonds issued included within debt securities in issue. The covered bond holders have dual recourse: firstly, to Clydesdale Bank PLC on an unsecured basis; and secondly, to the LLP under the Covered Bond Guarantee secured against the mortgage loans.

Significant restrictions

Where the Group uses its financial assets to raise finance through securitisations and the sale of securities subject to repurchase agreements, this leads to the assets becoming encumbered. Once encumbered, the assets are not available for transfer around the Group.

The assets and liabilities in relation to securitisation and covered bonds in issue at 30 September are as follows:

2018	Securitisation £m	Covered bonds £m	Total £m
Liabilities			
At 1 October 2017	**3,242**	**748**	**3,990**
Issuance of debt	**1,049**	**–**	**1,049**
Repayments	**(1,372)**	**–**	**(1,372)**
Other movements	**30**	**(16)**	**14**
At 30 September 2018	**2,949**	**732**	**3,681**
Assets			
Securitised mortgage loans	**6,412**	**1,389**	**7,801**

2017	Securitisation £m	Covered bonds £m	Total £m
Liabilities			
At 1 October 2016	3,208	797	4,005
Issuance of debt	750	–	750
Repayments	(740)	–	(740)
Other movements	24	(49)	(25)
At 30 September 2017	3,242	748	3,990
Assets			
Securitised mortgage loans	6,182	1,344	7,526

Other movements consist of exchange rate movements on currency denominated bonds and fair value hedge accounting adjustments.

The following table sets out the net position of the fair value of financial assets relating to the securitisation programmes where the counterparty to the associated liabilities has recourse only to the financial assets:

	2018 £m	2017 £m
Fair value of transferred assets	**6,248**	6,074
Fair value of associated liabilities	**(2,948)**	(3,262)
	3,300	2,812

There were no events during the year that resulted in any Group transferred financial assets being derecognised.

The Group has contractual and non-contractual arrangements which may require it to provide financial support as follows:

Securitisation programmes
The Group provides credit support to the structured entities via reserve funds, which are partly funded through subordinated debt arrangements and by holding junior notes. Exposures totalled £23m in subordinated debt (2017: £47m) and £971m in junior notes held (2017: £856m). The Group has a beneficial interest in the securitised mortgage portfolio held by the structured entities of £1,074m (2017: £711m).

Furthermore, the Group has an obligation to repurchase mortgage exposures if certain mortgage loans no longer meet the programme criteria.

Looking forward through future reporting periods there are a number of date based options on the notes issued by the structured entities which could be actioned by them as issuer. These could require the Group, as sponsor, to provide additional liquidity support.

Covered bond programme
The nominal level of over-collateralisation was £860m (2017: £681m) of the outstanding covered bonds. From time to time the obligations of the Group to provide over-collateralisation may increase due to the formal requirements of the programme.

Furthermore, the Group has an obligation to repurchase mortgage exposures if certain mortgage loans no longer meet the programme criteria.

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Section 3: Assets and liabilities continued

3.8 Property, plant and equipment

Accounting policy

The Group's freehold and long-term leasehold land and buildings are carried at their fair value as determined by the Directors, taking account of advice received from independent valuers. Fair values are determined in accordance with guidance published by the Royal Institution of Chartered Surveyors, including adjustments to observable market inputs reflecting any specific characteristics of the land and buildings. Directors' valuations are performed annually in July, with the independent valuations carried out on a three-year cycle on an open market basis. The valuations are classified in Level 3 of the fair value hierarchy as defined in note 3.18.

All other items of property, plant and equipment are carried at cost, less accumulated depreciation and impairment losses. Cost includes expenditure that is directly attributable to acquisition of the asset. Impairment is assessed whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

With the exception of freehold and long-term leasehold land, all items of property, plant and equipment are depreciated or amortised using the straight line method, at rates appropriate to their estimated useful life to the Group. The annual rates of depreciation or amortisation are:

Buildings	50 years
Leases (leasehold improvements)	the lower of the expected lease term or the asset's remaining useful life
Fixtures and equipment	3–10 years

Residual values and useful lives of assets are reviewed at each reporting date. Depreciation is recognised within depreciation expense in the income statement.

	Freehold land and buildings £m	Long-term leasehold land and buildings £m	Building improvements £m	Fixtures and equipment £m	Total £m
Cost or valuation					
At 1 October 2016	6	3	154	100	263
Additions	–	–	14	7	21
Disposals	(1)	–	(25)	(5)	(31)
At 30 September 2017	5	3	143	102	253
Additions	–	–	9	13	22
Disposals	(2)	–	(3)	(1)	(6)
At 30 September 2018	**3**	**3**	**149**	**114**	**269**
Accumulated depreciation					
At 1 October 2016	1	–	90	73	164
Charge for the year	–	–	14	8	22
Disposals	–	–	(16)	(3)	(19)
At 30 September 2017	1	–	88	78	167
Charge for the year (note 2.4)	–	–	10	8	18
Disposals	–	–	(3)	(1)	(4)
At 30 September 2018	**1**	**–**	**95**	**85**	**181**
Net book value					
At 30 September 2018	**2**	**3**	**54**	**29**	**88**
At 30 September 2017	4	3	55	24	86

Valuations

A comparison of the carrying value between the revaluation basis and the historical cost basis, for freehold and long-term leasehold land and buildings, is shown below:

	2018 £m	2017 £m
Carrying value as included under the revaluation basis	**5**	7
Carrying value if the historical cost basis had been used	**5**	6

3.9 Investment properties

Accounting policy

Investment properties are measured at fair value and are revalued annually by the Directors. The valuations are based upon advice received from independent valuers and performed on an open market basis. Adjustments are made to observable market data for comparable properties for specific characteristics such as the nature, location or condition of the asset. Fair value movements are recognised in the income statement in the period in which they arise.

Investment properties are classified in Level 3 of the fair value hierarchy as defined in note 3.18.

	2018 £m	2017 £m
At 1 October	**14**	22
Disposals	**(7)**	(7)
Revaluation	**–**	(1)
At 30 September	**7**	14

During the year 90% (2017: 86%) of the investment properties generated total rental income of £1m (2017: £1m) and incurred operating and administrative expenses of £1m (2017: £1m). The operating and administrative expenses of the investment properties that did not generate rental income were £Nil (2017: £Nil).

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.10 Intangible assets

Accounting policy

Capitalised software costs are stated at cost, less amortisation and any provision for impairment.

Identifiable and directly associated external and internal costs of acquiring and developing software are capitalised where the software is controlled by the Group, and where it is probable that future economic benefits that exceed its cost will flow from its use over more than one year. Costs associated with maintaining software are recognised as an expense as incurred. Capitalised computer software costs are amortised on a straight line basis over their expected useful lives, usually between three and 10 years. Impairment losses are recognised in the income statement as incurred.

Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable, which typically arises when the benefits associated with the software were substantially reduced from what had originally been anticipated or the asset has been superseded by a subsequent investment. In such situations, an impairment loss is recognised for the amount by which the carrying amount of an asset exceeds its recoverable amount. The recoverable amount of an asset is the higher of its fair value less costs of disposal or its value in use.

Intangible assets which are fully amortised are reviewed annually to consider whether the assets remain in use.

Capitalised software costs

	2018 £m	2017 £m
Cost		
At 1 October	**589**	463
Additions	**144**	148
Write-off	**–**	(22)
At 30 September	**733**	589
Accumulated amortisation		
At 1 October	**250**	207
Charge for the year (note 2.4)	**71**	65
Write-off	**–**	(22)
At 30 September	**321**	250
Net book value at 30 September	**412**	339

£1m (2017: £3m) of the £144m (2017: £148m) software additions do not form part of internally generated software projects.

3.11 Deferred tax

Accounting policy

Deferred tax assets and liabilities are recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. A deferred tax asset is recognised for unused tax losses and unused tax credits only if it is probable that future taxable amounts will arise against which those temporary differences and losses may be utilised.

Critical accounting estimates and judgements

The Group has deferred tax assets of £206m (2017: £154m); the increase from the previous balance sheet date is mainly due to increased loss recognition due to the implementation of the Corporate Loss Restriction, losses incurred in the year and additionally previously written off historic losses re-recognised in accordance with IAS 12. The Group has assessed the recoverability of these deferred tax assets at 30 September 2018 and considers it probable that sufficient future taxable profits will be available against which the underlying deductible temporary differences can be utilised over the corporate planning horizon.

At 30 September 2018, the Group had an unrecognised deferred tax asset of £157m (2017: £180m) representing trading losses with a gross value of £926m (2017: £1,058m). Although there is no prescribed period after which losses expire, a deferred tax asset has not been recognised in respect of these losses as the Directors have insufficient certainty over their recoverability in the foreseeable future.

Movement in net deferred tax asset

	2018 £m	2017 £m
At 1 October	**79**	156
Recognised in the income statement (note 2.5)	**35**	(69)
Recognised directly in equity	**15**	(8)
At 30 September	**129**	79

The Group has recognised deferred tax in relation to the following items:

	2018 £m	2017 £m
Deferred tax assets		
Tax losses carried forward	**99**	28
Capital allowances	**88**	120
Cash flow hedge reserve	**12**	1
Transitional adjustment – available for sale reserve	**1**	3
Employee equity based compensation	**3**	2
Other	**3**	–
	206	154
Deferred tax liabilities		
Defined benefit pension scheme surplus	**(74)**	(72)
Gains on unlisted available for sale investments	**(3)**	(3)
	(77)	(75)
Net deferred tax asset	**129**	79

Since 1 April 2017, the statutory rate of UK corporation tax has been 19% and will fall to 17% from 1 April 2020. In accordance with the appropriate accounting standard, these enacted rates are used to measure the value at which assets are expected to be realised and liabilities settled.

A prior year adjustment to claim capital allowances provisionally disclaimed at 30 September 2017 has resulted in an increase to the residual loss deferred tax asset of £14m and a decrease in the corresponding capital allowance deferred tax asset of £19m. The difference between the two amounts, which arises because the two types of deferred tax assets are recognised at different rates, is taken to the income statement as part of the prior year credit set out in note 2.5.

The acquisition of Virgin Money on 15 October 2018 is not expected to have a material impact on the deferred tax asset recognition.

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.12 Due to other banks

Accounting policy

Repurchase agreements

Securities sold subject to sale and repurchase agreements ('repos') are retained in their respective balance sheet categories. The associated liabilities are included in amounts due to other banks based upon the counterparties to the transactions.

The difference between the sale and repurchase price of repos is treated as interest and accrued over the life of the agreements using the effective interest method.

	2018 £m	2017 £m
Securities sold under agreements to repurchase (1)	**802**	1,864
Transaction balances with other banks	**29**	21
Deposits from other banks	**37**	31
Secured loans	**2,254**	1,901
	3,122	3,817

(1) The underlying securities sold under agreements to repurchase have a carrying value of £1,172m (2017: £2,660m).

Secured loans comprise amounts drawn under the TFS (including accrued interest).

3.13 Due to customers

	2018 £m	2017 £m
Interest bearing demand deposits	**19,895**	19,130
Term deposits	**6,192**	5,957
Non-interest bearing demand deposits	**2,756**	2,548
Other wholesale deposits	**1**	18
	28,844	27,653
Accrued interest payable	**60**	65
	28,904	27,718

3.14 Provision for liabilities and charges

Accounting policy

Provisions for liabilities and charges are recognised when a legal or constructive obligation exists as a result of past events, it is probable that an outflow of economic benefits will be necessary to settle the obligation, and the obligation can be reliably estimated. Provisions for liabilities and charges are not discounted to the present value of their expected net future cash flows except where the time value of money is considered material.

Critical accounting estimates and judgements

PPI redress provision and other conduct related matters

Management has exercised significant judgement around the key assumptions that underpin the estimates and used estimation techniques to quantify them. Ongoing regulatory review and input, as well as rulings from the Financial Ombudsman Service over time, and the Group's internal reviews and assessments of customer complaints, will continue to impact upon the nature and extent of conduct related customer redress and associated costs for which the Group may ultimately become liable in future periods.

Significant judgement is required in determining the key assumptions used to estimate the quantum of the provision, including the level of future complaint volumes, uphold rates (how many claims are, or may be, upheld in the customer's favour), and redress costs (the average payment made to customers). The provision is therefore subject to inherent uncertainties as a result of the subjective nature of the assumptions used in quantifying the overall estimated position at 30 September 2018, consequently, the provision calculated may be subject to change in future years if outcomes differ to those currently assumed. Sensitivity analysis indicating the impact of reasonably possible changes in key assumptions on the PPI provision is presented within this note.

There are similar uncertainties and judgements for other conduct risk related matters, however the level of liability is materially lower.

	2018 £m	2017 £m
PPI redress provision		
Opening balance	**422**	725
Charge to the income statement (note 2.4)	**352**	48
Charge reimbursed/reimbursable under Conduct Indemnity	**148**	446
Utilised	**(647)**	(797)
Closing balance	**275**	422
Customer redress and other provisions		
Opening balance	**109**	101
Charge to the income statement (note 2.4)	**44**	10
Charge reimbursed/reimbursable under Conduct Indemnity	**–**	88
Utilised	**(112)**	(90)
Closing balance	**41**	109
Restructuring provision[1]		
Opening balance	**23**	26
Charge to the income statement	**15**	58
Utilised	**(23)**	(61)
Closing balance	**15**	23
Total provisions for liabilities and charges	**331**	554

(1) Restructuring provision includes surplus lease space provision.

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Section 3: Assets and liabilities continued

3.14 Provision for liabilities and charges continued

PPI redress

In common with the wider UK retail banking sector, the Group continues to deal with complaints and redress issues arising out of historic sales of PPI. During the year, the Group reassessed the level of provision that was considered appropriate to meet current and future expectations in relation to the mis-selling of PPI policies and concluded that a further charge of £500m was required incorporating the Group's estimate of the impact of heightened media coverage, the FCA advertising campaign and increased activity by claims management companies ahead of the August 2019 industry deadline. It also incorporated a reassessment of the costs of processing cases and the impact of experience adjustments. The impact on the Group's income statement (£352m) has been reduced by the remaining balance of the Capped Indemnity. The total provision raised to date in respect of PPI is £2,640m (2017: £2,140m), with £275m of this remaining (2017: £293m)[1] for customer initiated complaints including costs of administration.

The Group implemented a comprehensive new PPI complaint handling process from August 2014 which involved making a number of significant changes to the PPI operations and resulted in an increase in operational and administrative costs. As reported previously, this involved the Group reopening complaints and reviewing the original decision reached in light of the new PPI complaint handling processes. This process has been concluded during the year at an additional cost of £88m.

To 30 September 2018, the Group has received 483,000[2] complaints (2017: 361,000) and has allowed for 83,000 further walk in complaints (2017: 73,000). This reflects an expectation that incoming complaints will reduce from current levels in aggregate reflecting the recently observed decline following the implementation of the fee cap.

The increase in provision has taken into account the above factors as well as a revision in the Group's expectation of new customer initiated complaints in light of current experience. The overall provision is based on a number of assumptions derived from a combination of past experience, estimated future experience, industry comparison and the exercise of judgement in the key areas identified. There remain risks and uncertainties in relation to these assumptions and consequently in relation to the ultimate costs of redress and related costs, including: (i) the number of PPI claims (and the extent to which this is influenced by the activity of claims management companies, the application of a time bar, Plevin, and FCA advertising); (ii) the number of those claims that ultimately will be upheld; (iii) the amount that will be paid in respect of those claims; and (iv) the costs of administration.

As such, the factors discussed above mean there is a risk that existing provisions for PPI customer redress may not cover all potential costs. In light of this, the eventual costs of PPI redress and complaint handling may therefore differ materially from that estimated and further provision could be required.

The table below sets out the key assumptions and the effect on the provision at 30 September 2018 of future, potential, changes in key assumptions:

Assumptions

	Change in assumption	Sensitivity[3]
Number of expected future customer initiated complaints (83,000 new complaints)	+/-10%	£24m
Uphold rate	+/-1%	£3m
Average redress costs[4]	+/-1%	£1m

(1) Comparatives refer to the remaining provision for customer initiated complaints only, the balance being for the completion of the remediation exercise.
(2) Of these cases, c.12,000 were work in progress as at 30 September 2018 (2017: c.11,000).
(3) There are inter-dependencies between several of the key assumptions which add to the complexity of the judgements the Group has to make. This means that no single factor is likely to move independently of others, however, the sensitivities disclosed above assume all other assumptions remain unchanged.
(4) Sensitivity to a change in average redress across customer initiated complaints.

Customer redress and other provisions

Other provisions include amounts in respect of a number of non-PPI conduct related matters, legal proceedings, and claims arising in the ordinary course of the Group's business. Over the course of the year, the Group has raised further provisions of £44m for these matters, none of which was covered by the Capped Indemnity. The ultimate cost to the Group of other customer redress matters is driven by a number of factors relating to offers of redress, compensation, offers of alternative products, consequential loss claims and administrative costs. The matters are at varying stages of their life cycle and in certain circumstances, usually early in the life of a potential issue, elements of the potential exposure are contingent. These factors could result in the total cost of review and redress varying materially from the Group's estimate. The final amount required to settle the Group's potential liabilities in these matters is therefore uncertain and further provision could be required.

Conduct Indemnity Deed

The Group's economic exposure to the impact of historic conduct related liabilities was mitigated by a Capped Indemnity of £1.7bn from NAB. The full amount of the remaining Capped Indemnity was drawn down in the current year. The Company and NAB had an agreement under which NAB provided the Company with a Capped Indemnity to meet the costs of dealing with conduct matters related to products sold in the period prior to the date of the Group's Demerger (the Conduct Indemnity Deed). The legacy conduct matters covered by the Capped Indemnity are referred to as Relevant Conduct Matters. The Capped Indemnity provided the Group with economic protection against certain costs and liabilities (including financial penalties imposed by a regulator) resulting from conduct issues relating to:

a) PPI, standalone interest rate hedging products, voluntary scope tailored business loans and fixed rate tailored business loans; and

b) other conduct matters, subject to certain limitations and minimum financial thresholds.

Amounts payable under the Capped Indemnity included, subject to certain limitations, payments to customers to satisfy, settle or discharge a Relevant Conduct Matter and the direct costs and expenses of satisfying, settling, discharging or administering such Relevant Conduct Matter.

It was agreed that NAB would meet 90.3% of Qualifying Conduct Costs claimed by the Company, up to the amount of the Capped Indemnity.

Claims under the Capped Indemnity have been recognised in the consolidated income statement simultaneously with the charge for Relevant Conduct Matters. The conduct expense and associated reimbursement income have been presented net within Other operating and administrative expenses. The provision expense and reimbursement income are disclosed above.

Now that the Qualifying Conduct Costs have exceeded the Capped Indemnity, any costs in excess of the amounts currently provided will be borne by the Group.

To the extent that tax relief is expected in relation to provisions for which reimbursement income is applicable, amounts may become repayable to NAB. In the consolidated financial statements, deferred tax assets are only recognised in respect of the loss share proportion (9.7%) of unused tax losses on Relevant Conduct Matters, on the basis that the Group does not obtain the economic benefit of the future tax relief which is repayable to NAB.

The utilisation of the Capped Indemnity is set out below:

	Conduct protection £m
Conduct protection provided by NAB	1,700
Capital injected into CYB Investments Limited (CYBI) prior to Demerger(1)	(120)
Drawn in the period to 30 September 2017(2)	(1,432)
Undrawn Conduct Indemnity as at 30 September 2017	148
Drawn in the year to 30 September 2018	(148)
Undrawn balance as at 30 September 2018	–

(1) £120m of the £670m of capital injected in CYBI on 24 September 2015 related to the Conduct Indemnity Deed.
(2) £465m of the £1,432m represented the pre-covered provision amount.

Restructuring provision

Restructuring of the business is currently ongoing and a provision is held to cover redundancy payments, property vacation costs and associated enablement costs. During the year £38m (2017: £67m) was charged to the income statement, of which £23m (2017: £9m) was charged directly to the income statement and £15m (2017: £58m) was provided for in accordance with the requirements of IAS 37. £23m (2017: £61m) of the total provision was utilised in the year.

Included within the restructuring provision is an amount for committed rental expense on surplus lease space consistent with the expected exposure on individual leases where the property is unoccupied. This element of the provision will be utilised over the remaining life of the leases or until the leases are assigned, and is measured at present values by discounting anticipated future cash flows.

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Section 3: Assets and liabilities continued

3.15 Debt securities in issue

Accounting policy

Debt securities comprise short and long-term debt issued by the Group including commercial paper, medium-term notes, term loans, covered bonds and RMBS notes.

Debt securities are initially recognised at fair value, being the issue proceeds, net of transaction costs incurred. These instruments are subsequently measured at amortised cost using the effective interest method resulting in premiums, discounts and associated issue costs being recognised in the income statement over the life of the instrument.

The breakdown of debt securities in issue is shown below:

2018	Medium-term notes £m	Subordinated debt £m	Securitisation £m	Covered bonds £m	Total £m
Amortised cost	**794**	**476**	**2,949**	**698**	**4,917**
Fair value hedge adjustments	**(1)**	**–**	**–**	**34**	**33**
Total debt securities	**793**	**476**	**2,949**	**732**	**4,950**
Accrued interest payable	**3**	**3**	**7**	**10**	**23**
	796	**479**	**2,956**	**742**	**4,973**

2017	Medium-term notes £m	Subordinated debt £m	Securitisation £m	Covered bonds £m	Total £m
Amortised cost	297	476	3,242	698	4,713
Fair value hedge adjustments	–	–	–	50	50
Total debt securities	297	476	3,242	748	4,763
Accrued interest payable	3	3	6	10	22
	300	479	3,248	758	4,785

The Group issued the following debt securities during the year:

Issue date	Debt security	Initial proceeds	Programme
1 February 2018	Lanark 2018-1 1A	$300m	Securitisation
1 February 2018	Lanark 2018-1 2A	£285m	Securitisation
5 July 2018	Lanark 2018-2 1A	$400m	Securitisation
5 July 2018	Lanark 2018-2 2A	£250m	Securitisation
25 September 2018	Medium-term notes 2018	£500m	Medium-term notes

The following redemptions occurred during the year with the final redemption value in line with the scheduled programme terms:

Redemption date	Debt security	Initial proceeds	Programme
20 November 2017	Lannraig 2011-1 1A	£335m	Securitisation
22 November 2017	Lanark 2012-2 2A	£525m	Securitisation
22 August 2018	Lanark 2014-2 1A	€550m	Securitisation
22 August 2018	Lanark 2015-1 1A	£300m	Securitisation

Further reduction in the carrying value is as a result of scheduled principal repayments on outstanding securitisation notes.

Details of the terms and conditions of the notes issued under the medium-term notes and subordinated debt programmes as at 30 September 2018 were as follows:

Medium-term notes	**Carrying value[1] £m**
CYBG 3.125% fixed to floating rate callable senior notes due 2025	**298**
CYBG 4% fixed rate reset callable senior notes due 2026	**495**
Total medium-term notes	**793**

Subordinated debt	**Carrying value[1] £m**
CYBG 5% fixed rate reset callable subordinated notes due 2026	**476**

Details of the terms and conditions of the notes issued under the securitisation and covered bond programmes as at 30 September 2018 were as follows:

Issue date	Currency	**Carrying value[1] £m**	Coupon rate	Call date
Class A Lanark RMBS notes				
19 March 2014	GBP	**218**	3M GBP LIBOR + 0.50%	22 November 2018
11 December 2014	GBP	**274**	3M GBP LIBOR + 0.60%	22 February 2020
6 August 2015	EUR	**249**	3M EURIBOR + 0.45%	22 May 2021
4 August 2016	GBP	**419**	3M GBP LIBOR + 1.00%	22 February 2019
5 July 2017	GBP	**349**	3M GBP LIBOR + 0.42%	22 November 2020
5 July 2017	GBP	**399**	3M GBP LIBOR + 0.55%	22 August 2022
1 February 2018	USD	**202**	3M USD LIBOR + 0.42%	22 August 2020
1 February 2018	GBP	**284**	3M GBP LIBOR + 0.42%	22 February 2023
5 July 2018	USD	**306**	3M USD LIBOR + 0.42%	22 February 2021
5 July 2018	GBP	**249**	3M GBP LIBOR + 0.52%	22 August 2023
		2,949		
Covered bonds				
8 June 2012	GBP	**732**	4.625%	8 June 2026
Total securitised notes and covered bonds (note 3.7)		**3,681**		

(1) Excludes accrued interest.

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.16 Retirement benefit obligations

Accounting policy

The Group makes contributions to both defined benefit and defined contribution pension schemes which entitle employees to benefits on retirement or disability.

Defined contribution pension scheme

The Group recognises the obligation for contributions to the scheme as an expense in the income statement as incurred. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payment is available.

Defined benefit pension scheme

A liability or asset in respect of the defined benefit scheme is recognised on the balance sheet and is measured as the present value of the defined benefit obligation less the fair value of the defined benefit scheme assets at the reporting date. The present value of the defined benefit obligation for the scheme is discounted by high quality corporate bond rates that have maturity dates approximating to the terms of the Group's defined benefit obligation. Surpluses are only recognised to the extent that they are recoverable through reduced contributions in the future or through refunds from the scheme. In assessing whether a surplus is recoverable, the Group considers its current right to obtain a refund or a reduction in future contributions and does not anticipate any future acts by other parties that could change the amount of the surplus that may be ultimately recovered.

Pension expense attributable to the Group's defined benefit scheme comprises current service cost, net interest on the net defined benefit obligation/asset, past service cost resulting from a scheme amendment or curtailment, gains or losses on settlement and administrative costs incurred. Where actuarial remeasurements arise, the Group recognises such amounts directly in equity through the statement of comprehensive income in the period in which they occur. Actuarial remeasurements arise from experience adjustments (the effects of differences between previous actuarial assumptions and what has actually occurred) and changes in actuarial assumptions.

The Group operates both defined benefit and defined contribution arrangements. The Group's principal trading subsidiary, Clydesdale Bank PLC, is the sponsoring employer in one funded defined benefit pension scheme, the Yorkshire and Clydesdale Bank Pension Scheme ('the Scheme'). The Scheme was established under trust on 30 September 2009 as a result of the merger of the Clydesdale Bank Pension Scheme and the Yorkshire Bank Pension Fund. The assets of the Scheme are held in a trustee administered fund, with the Trustee responsible for the operation and governance of the Scheme, including making decisions regarding the Scheme's funding and investment strategy.

The Scheme is subject to the funding legislation outlined in the Pensions Act 2004 which came into force on 30 December 2005. This, together with documents issued by the Pensions Regulator, sets out the framework for funding defined benefit occupational pension plans in the UK.

The Group also provides post-retirement health care under a defined benefit scheme for pensioners and their dependent relatives for which provision has been made on a basis consistent with the methodology applied to the defined benefit pension scheme. This is a closed scheme and the provision will be utilised over the life of the remaining scheme members.

The following table provides a summary of the present value of the defined benefit obligation and fair value of plan assets for the Scheme:

	2018 £m	2017 £m
Active members' defined benefit obligation	**(24)**	(807)
Deferred members' defined benefit obligation(1)	**(2,131)**	(1,549)
Pensioner and dependant members' defined benefit obligation	**(1,591)**	(1,618)
Total defined benefit obligation	**(3,746)**	(3,974)
Fair value of Scheme assets	**3,958**	4,181
Net defined benefit pension asset	**212**	207
Post-retirement medical benefits obligations	**(3)**	(3)

(1) Deferred members' defined benefit obligation includes employees who became deferred members on 1 August 2017 as part of the Scheme closure exercise.

The Group has implemented a number of reforms to the Scheme to manage the liability. It closed the Scheme to new members in 2004 and since April 2006 has determined benefits accruing on a career average revalued earnings basis. On 1 August 2017, the Scheme was closed to future benefit accrual for the majority of current employees, with affected employees' future pension benefits being provided through the existing defined contribution scheme, 'Total Pension'. The Total Pension income statement charge for the year is shown in note 2.4.

The last scheme funding valuation was at 30 September 2016 with a calculated deficit of £290m. In the latest recovery plan dated 31 January 2018, the Group agreed to eliminate the deficit through the following scheduled contributions: a single contribution of £25m on 15 October 2018; thereafter, equal monthly contributions totalling £50m per annum until 31 March 2022; and £55m in the year to 31 March 2023.

On 26 October 2018 the High Court ruled on a landmark pensions case relating to the defined benefits pension schemes operated by Lloyds Banking Group. Refer to note 5.5 for further information on post balance sheet events.

Reconciliation of the net defined benefit pension asset/(liability)

	2018 £m	2017 £m
Opening net defined benefit pension scheme asset/(liability)	**207**	(75)
Service (cost)/credit	**(3)**	54
Interest on net defined benefit asset/(liability)	**5**	(1)
Remeasurement effects recognised in SOCI	**(9)**	154
Employer contributions	**18**	69
Administrative expenses	**(6)**	(7)
Curtailments and settlements	**–**	13
Closing fair value of net defined benefit pension scheme asset	**212**	207

Reconciliation of the defined benefit pension scheme assets

	2018 £m	2017 £m
Opening fair value of defined benefit pension scheme assets	**4,181**	4,462
Interest income on Scheme assets at discount rate	**109**	104
Return on Scheme assets greater/(less) than discount rate	**27**	(195)
Employer contributions (note 5.3)	**18**	69
Benefits paid	**(93)**	(102)
Transfer payments	**(278)**	(150)
Administrative costs paid	**(6)**	(7)
Closing fair value of defined benefit pension scheme assets	**3,958**	4,181

Reconciliation of the defined benefit pension scheme obligations

	2018 £m	2017 £m
Opening defined benefit pension scheme obligations	**(3,974)**	(4,537)
Current service cost	**(1)**	(26)
Past service (cost)/credit	**(2)**	80
Interest expense on the defined benefit obligation	**(104)**	(105)
Actuarial (loss)/gain – experience adjustments	**(35)**	76
Actuarial gain – demographic assumptions	**19**	88
Actuarial (loss)/gain – financial assumptions	**(20)**	185
Benefits paid from Scheme assets	**93**	102
Transfer payments	**278**	150
Curtailments and settlements	**–**	13
Closing defined benefit pension scheme obligations	**(3,746)**	(3,974)

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.16 Retirement benefit obligations continued

The major categories of plan assets for the Scheme, stated at fair value, are as follows:

	2018 £m	2017 £m
Quoted		
Equities	**650**	804
Government bonds	**2,017**	1,495
Global sovereign bonds	**24**	33
Corporate bonds	**706**	829
Alternative credit	**260**	97
Infrastructure	**255**	272
Secure income alternatives	**336**	209
Derivatives(1)	**172**	169
Other	**4**	4
Repurchase agreements	**(836)**	–
Cash	**238**	124
Unquoted		
Property	**132**	145
Fair value of defined benefit pension scheme assets	**3,958**	4,181

(1) Derivative financial instruments are used to modify the profile of the assets of the Scheme to better match the Scheme's liabilities. Derivative holdings may lead to increased or decreased exposures to the physical asset categories disclosed above.

The Scheme is not invested in any of the Group's own financial instruments.

Through its defined benefit pension plan and post-employment medical plan, the Group is exposed to a number of risks. The main risk to the Group is that additional contributions are required if the Scheme's assets are not sufficient to pay for the benefits (which will be influenced mainly by inflation and the longevity of members). The level of asset returns will be a key factor in the overall investment return. The investment portfolio is subject also to a range of risks typical of the assets held, in particular equity risk, credit risk on bonds and exposure to the property market.

The Trustee has implemented an investment structure (including physical assets and derivatives) that seeks to reduce the Scheme's exposure to inflation and interest rate risks. As at 30 September 2018, both the interest rate and inflation rate hedge ratios were around 60% of liabilities when measured on a self-sufficiency basis. The estimated hedge ratios will be updated pending changes to the Trustee's strategic asset allocation but it is expected these have both increased. This strategy reflects the Scheme's liability profile and the Trustee's and the Group's attitude to risk. The Trustee monitors the investment objectives and asset allocation policy on a regular basis.

Amounts recognised in the income statement

	2018 £m	2017 £m
Current service cost	**1**	26
Past service cost	**2**	8
Past service credit on closure of Scheme	**–**	(88)
Curtailment and settlement gains	**–**	(13)
Net interest on net defined benefit (asset)/liability	**(5)**	1
Defined benefit pension income for the year	**(2)**	(66)
Administrative costs incurred	**6**	7
Cost/(credit) recognised in the income statement (note 2.4)	**4**	(59)

The Group incurred a past service cost of £2m (2017: £8m) in relation to enhanced early retirement entitlements on redundancy; in both years these were fully offset in the income statement by a corresponding release from the restructuring provision. In the prior year, the income statement benefited from a curtailment gain of £13m due to a higher than normal level of redundancies with no enhancement entitlement; this gain was offset against the related restructuring costs.

Amounts recognised in the statement of comprehensive income

	2018 £m	2017 £m
Opening cumulative actuarial losses	**(695)**	(849)
Actuarial (loss)/gain due to liability experience adjustments	**(35)**	76
Actuarial (loss)/gain due to liability assumption changes	**(20)**	185
Actuarial gain due to demographic assumption changes	**19**	88
Return on Scheme assets greater/(less) than discount rate	**27**	(195)
Cumulative actuarial losses recognised in the statement of comprehensive income	**(704)**	(695)

Actuarial assumptions

	2018 % p.a.	2017 % p.a.
Financial assumptions		
Discount rate	**2.75**	2.74
Inflation (RPI)	**3.30**	3.24
Inflation (CPI)	**2.30**	2.24
Career average revalued earnings (CARE) revaluations:		
Pre 31 March 2012 benefits (RPI)	**3.30**	3.24
Post 31 March 2012 benefits (CPI capped at 5% per annum)	**2.30**	2.24
Pension increases (capped at 2.5% per annum)	**2.13**	2.12
Pension increases (capped at 5% per annum)	**3.15**	3.10
Rate of increase for pensions in deferment	**2.30**	2.24

Demographic assumptions Post-retirement mortality:	2018 years	2017 years
Current pensioners at 60 – male	**28.2**	28.2
Current pensioners at 60 – female	**29.8**	29.7
Future pensioners at 60 – male	**29.3**	29.3
Future pensioners at 60 – female	**31.0**	30.9

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.16 Retirement benefit obligations continued

Critical accounting estimates and judgements

The value of the Group's defined benefit pension scheme requires management to make several assumptions. The key areas of estimation uncertainty are:

– *The discount rate applied.* The discount rate is required to be set with reference to market yields at the end of the reporting period on high quality corporate bonds in the currency and with a term consistent with the Scheme's obligations. The average duration of the Scheme's obligations is approximately 19 years. The market for bonds with a similar duration is illiquid and, as a result, significant management judgement is required to determine an appropriate yield curve on which to base the discount rate.

– *Inflation assumptions.* Inflation is set with reference to market expectations of the RPI measure of inflation for a term consistent with the Scheme's obligations, based on data published by the BoE. Other measures of inflation (such as CPI, or inflation measures subject to an annual cap) are derived from this assumption.

– *Mortality assumptions.* The cost of the benefits payable by the Scheme will also depend upon the life expectancy of the members. The assumptions for mortality rates are based on standard mortality tables which allow for future improvements in life expectancies.

The table below sets out the sensitivity of the defined benefit obligation and pension cost to realistic changes in the key actuarial assumptions:

Assumption change		Impact on defined benefit obligation £m	Impact on pension cost £m
Discount rate	+0.25%	(169)	(6)
	-0.25%	182	5
Inflation	+0.25%	115	3
	-0.25%	(113)	(3)
Life expectancy	+1 year	126	4
	-1 year	(120)	(3)

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, changes in some of the assumptions may be correlated.

The discounted mean term of the defined benefit obligation at 30 September 2018 is 19 years (2017: 20 years). The expected contributions for the year ending 30 September 2019 are £77m (2018: £33m) and expected benefit payments for the year ending 30 September 2019 are £98m (2018: £100m).

The Group and Trustee have entered into a contingent security arrangement (the 'Security Arrangement') (note 5.3).

3.17 Other liabilities

	2018 £m	2017 £m
Notes in circulation	**2,254**	2,197
Accruals and deferred income	**125**	163
Other	**101**	111
	2,480	2,471

3.18 Fair value of financial instruments

Accounting policy

Fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants at the valuation date.

When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. Where no such active market exists for the particular asset or liability, the Group uses a valuation technique to arrive at the fair value, including the use of transaction prices obtained in recent arm's length transactions where possible, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. In doing so, fair value is estimated using a valuation technique that makes maximum possible use of market inputs and that places minimal possible reliance upon entity-specific inputs.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, which represents the fair value of the consideration paid or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Group recognises profits or losses on the transaction date.

In certain limited circumstances the Group applies the fair value measurement option to financial assets including loans and advances where the inherent market risks (principally interest rate and option risk) are individually hedged using appropriate interest rate derivatives. The loan is designated as being carried at fair value through profit or loss to offset the movements in the fair value of the derivative within the income statement and therefore avoid an accounting mismatch. When a loan is held at fair value, a statistical based calculation is used to estimate expected losses attributable to adverse movements in credit risk on the assets held. This adjustment to the credit quality of the asset is then applied to the carrying amount of the loan to arrive at fair value and recognised in the income statement.

Analysis of the fair value disclosures uses a hierarchy that reflects the significance of inputs used in measuring fair value. The level in the fair value hierarchy within which a fair value measurement is categorised is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. The fair value hierarchy is as follows:

- Level 1 fair value measurements – quoted prices (unadjusted) in active markets for an identical financial asset or liability;
- Level 2 fair value measurements – inputs other than quoted prices within Level 1 that are observable for the financial asset or liability, either directly (as prices) or indirectly (derived from prices); and
- Level 3 fair value measurements – inputs for the financial asset or liability that are not based on observable market data (unobservable inputs).

For the purpose of reporting movements between levels of the fair value hierarchy, transfers are recognised at the beginning of the reporting period in which they occur.

(a) Fair value of financial instruments recognised on the balance sheet at amortised cost

The tables overleaf show a comparison of the carrying amounts of financial assets and liabilities measured at amortised cost, as reported on the balance sheet, and their fair values where these are not approximately equal.

There are various limitations inherent in this fair value disclosure particularly where prices are derived from unobservable inputs due to some financial instruments not being traded in an active market. The methodologies and assumptions used in the fair value estimates are therefore described in the notes to the tables. The difference between carrying value and fair value is relevant in a trading environment, but is not relevant to assets such as loans and advances.

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.18 Fair value of financial instruments continued

	30 September 2018					30 September 2017				
			Fair value measurement using:					Fair value measurement using:		
	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets										
Loans and advance to customers	**32,744**	**32,307**	**–**	**1,110**	**31,197**	31,293	31,088	–	1,009	30,079
Financial liabilities										
Due to other banks	**3,122**	**3,057**	**–**	**3,057**	**–**	3,817	3,817	–	3,817	–
Due to customers	**28,904**	**28,968**	**–**	**28,968**	**–**	27,718	27,833	–	27,833	–
Debt securities in issue	**4,973**	**5,052**	**1,279**	**3,773**	**–**	4,785	4,910	795	4,115	–

The Group's fair values disclosed for financial instruments at amortised cost are based on the following methodologies and assumptions:

(a) *Loans and advances to customers* – The fair values of loans and advances are determined by firstly segregating them into portfolios of similar characteristics. Contractual cash flows are then adjusted for expected credit losses and expectations of customer behaviour based on observed historic data. The cash flows are then discounted using current market rates for instruments of similar terms and maturity to arrive at an estimate of their fair value. Certain variable rate loan portfolios are discounted using market rates on similar loans offered by the Group at the valuation date.

(b) *Due to other banks* – The fair value is determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity.

(c) *Due to customers* – The fair value of deposits is determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity.

(d) *Debt securities in issue* – The fair value is taken directly from quoted market prices where available or determined from a discounted cash flow model using current market rates for instruments of similar terms and maturity.

(b) Fair value of financial instruments recognised on the balance sheet at fair value

The following tables provide an analysis of financial instruments that are measured subsequent to initial recognition at fair value, using the fair value hierarchy described above.

	Fair value measurement as at 30 September 2018				Fair value measurement as at 30 September 2017			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets								
Derivative financial assets	**–**	**262**	**–**	**262**	–	282	–	282
AFS investments – listed	**1,551**	**–**	**–**	**1,551**	2,066	–	–	2,066
AFS investments – unlisted	**–**	**–**	**5**	**5**	–	–	4	4
AFS – other	**–**	**–**	**6**	**6**	–	–	6	6
Other financial assets at fair value	**–**	**362**	**–**	**362**	–	–	477	477
Total financial assets at fair value	**1,551**	**624**	**11**	**2,186**	2,066	282	487	2,835
Financial liabilities								
Derivative financial liabilities	**–**	**361**	**–**	**361**	–	376	–	376
Other financial liabilities at fair value	**–**	**15**	**–**	**15**	–	–	26	26
Total financial liabilities at fair value	**–**	**376**	**–**	**376**	–	376	26	402

There were no transfers between Level 1 and 2.

The Group's valuations for financial instruments that are measured subsequent to initial recognition at fair value are based on the following methodologies and assumptions:

(a) *Derivative financial assets and liabilities* – The fair values of derivatives, including foreign exchange contracts, interest rate swaps, interest rate and currency option contracts, and currency swaps, are obtained from discounted cash flow models or option pricing models as appropriate.

(b) *Available for sale investments*

– *Listed (Level 1)* – The fair values of listed investments are based on quoted closing market prices.

– *Unlisted (Level 3)* – Includes £4m of Visa Inc. preferred stock received as partial consideration for the sale of the Group's share in Visa Europe (note 2.3). The preferred stock is convertible into Visa Inc. common stock or its equivalent at a future date, subject to potential reduction for certain litigation losses that may be incurred by Visa Europe. The fair value of the preference shares has been calculated by taking the period end New York Stock Exchange share price for Visa Inc. and discounting for illiquidity and clawback related to contingent litigation. For other unlisted equity and debt investments, the Group's share of the net asset value or the transaction price respectively are considered the best representation of the exit price and are the Group's best estimates of fair value.

– *Available for sale – other (Level 3)* – The other available for sale financial asset represents deferred consideration receivable and consists of the rights to future commission. The valuation is determined from a discounted cash flow model incorporating estimated attrition rates and investment growth rates appropriate to the underlying funds under management.

(c) *Financial assets and liabilities at fair value through profit or loss* – fair values are derived from data or valuation techniques based upon observable market data and non-observable inputs as appropriate to the nature and type of the underlying instrument.

Level 3 movement analysis:

	2018			2017		
	Financial assets available for sale £m	**Other financial assets at fair value £m**	**Other financial liabilities at fair value £m**	Financial assets available for sale £m	Other financial assets at fair value £m	Other financial liabilities at fair value £m
Balance at the beginning of the year	**10**	**477**	**(26)**	36	750	(48)
Transfer to Level 2[1]	**–**	**(477)**	**26**	–	–	–
Fair value (losses)/gains recognised[2]						
In profit or loss – (unrealised)	**1**	**–**	**–**	–	(39)	2
In profit or loss – (realised)	**(1)**	**–**	**–**	1	2	–
In available for sale – (unrealised)	**1**	**–**	**–**	1	–	–
Purchases	**–**	**–**	**–**	–	–	–
Sales[3]	**–**	**–**	**–**	(26)	–	–
Settlements	**–**	**–**	**–**	(2)	(236)	20
Balance at the end of the year	**11**	**–**	**–**	10	477	(26)

(1) The financial assets at fair value comprise a portfolio of loans which are no longer on sale. The continued run-off of these loans has resulted in the unobservable credit risk inputs no longer being significant to their fair value. As such the loans (and associated liabilities) have been reclassified to Level 2 in the fair value hierarchy. In accordance with the Group's accounting policy, the transfer is deemed to have occurred at the beginning of the reporting period. There were no transfers into or out of Level 3 in the year ended 30 September 2017.

(2) Net gains or losses were recorded in non-interest income or within the available for sale reserve as appropriate.

(3) The sale principally relates to the disposal of the VocaLink investment during the prior year (note 2.3).

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Notes to the consolidated financial statements

Section 3: Assets and liabilities continued

3.18 Fair value of financial instruments continued

Quantitative information about significant unobservable inputs in Level 3 valuations

The table below lists key unobservable inputs to Level 3 financial instruments, and provides the range of those inputs as at 30 September 2018.

	Fair value £m	Valuation technique	Unobservable inputs	Low range	High range
Financial assets					
AFS investments – unlisted	**5**	Discounted cash flow	Contingent litigation risk	0%	100%
AFS – other	**6**	Discounted cash flow	Funds under management attrition rate	10%	20%

Sensitivity of Level 3 fair value measurements to reasonably possible alternative assumptions

Where valuation techniques use non-observable inputs that are significant to a fair value measurement in its entirety, changing these inputs will change the resultant fair value measurement.

The most significant input impacting the carrying value of the available for sale – other asset is the Funds Under Management Attrition rate. The Group currently assumes an annual 15% attrition rate. If this rate was 20% the fair value would reduce by £1m; if it was 10% the fair value would increase by £2m.

Other than these significant Level 3 measurements, the Group has a limited remaining exposure to Level 3 fair value measurements, and changing one or more of the inputs for fair value measurements in Level 3 to reasonable alternative assumptions would not change the fair value significantly with respect to profit or loss, total assets, total liabilities or equity on these remaining Level 3 measurements.

Section 4: Capital

4.1 Equity

Accounting policy

Equity

The financial instruments issued by the Company are treated as equity (i.e. forming part of shareholders' funds) only to the extent that they meet the following two conditions:

(a) they include no contractual obligations upon the Company to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the Group; and

(b) where the instrument will or may be settled in the Company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the Company's own equity instruments or is a derivative that will be settled by the Company exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability.

Dividends

Incremental costs directly attributable to the issue of new shares or options or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds.

Final dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the Company's shareholders. Interim dividends are deducted from equity when they are no longer at the discretion of the Company.

Proposed final dividends for the year are disclosed as an event after the balance sheet date.

4.1.1 Share capital

	2018 Number of shares	2017 Number of shares	**2018 £m**	2017 £m
Ordinary shares of £0.10 each – allotted, called up and fully paid				
Opening ordinary share capital	**883,606,066**	881,531,852	**88**	88
Issued under employee share schemes	**2,473,893**	2,074,214	**1**	–
Closing ordinary share capital	**886,079,959**	883,606,066	**89**	88

The holders of ordinary shares are entitled to dividends as declared from time to time and are entitled to one vote per share at meetings of the shareholders of the Company. All shares in issue at 30 September 2018 rank equally with regard to the Company's residual assets.

During the year 2,473,893 (2017: 2,074,214) ordinary shares were issued under employee share schemes with a nominal value of £0.2m (2017: £0.2m).

A final dividend in respect of the year ended 30 September 2017 of 1p (2016: £Nil) per ordinary share amounting to £9m (2016: £Nil), was paid in February 2018. These dividends were deducted from retained profits in the current year. The Directors have recommended a final dividend in respect of the year ended 30 September 2018 of 3.1p per ordinary share in the Company to be paid on 15 February 2019. The payment of the final dividend is subject to approval of the shareholders at the 2019 Annual General Meeting. These financial statements do not reflect the recommended dividend.

A description of the other equity categories included within the Consolidated statement of changes in equity, and significant movements during the year, is provided below:

4.1.2 Other equity instruments

Other equity instruments consist of Perpetual Contingent Convertible Notes (fixed 8%) which were issued on 8 February 2016 with a principal amount of £450m and an optional redemption on 8 December 2022. AT1 distributions of £36m were paid in the year, £29m net of tax (2017: £36m paid, £29m net of tax).

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Notes to the consolidated financial statements

Section 4: Capital continued

4.1.3 Capital reorganisation reserve
The capital reorganisation reserve of £839m was recognised on the issuance of CYBG PLC ordinary shares in February 2016 in exchange for the acquisition of the entire share capital of the Group's previous parent company, CYBI. The reserve reflects the difference between the consideration for the issuance of CYBG PLC shares and CYBI's share capital and share premium.

4.1.4 Merger reserve
A merger reserve of £633m was recognised on the issuance of CYBG PLC ordinary shares in February 2016 in exchange for the acquisition of the entire share capital of CYBI. The merger reserve reflects the difference between the consideration for the issuance of CYBG PLC shares and the nominal value of the shares issued.

4.1.5 Other reserves
4.1.5.1 Asset revaluation reserve

The asset revaluation reserve includes the gross revaluation increments and decrements arising from the revaluation of land and buildings.

4.1.5.2 Available for sale reserve

The available for sale reserve records the gains and losses arising from changes in the fair value of available for sale financial assets.

4.1.5.3 Cash flow hedge reserve

The cash flow hedge reserve represents the cumulative post-tax gains and losses on derivatives designated as cash flow hedging instruments that will be recycled to the income statement when the hedged items affect profit or loss.

As at 30 September 2018, the cash flow hedge reserve reflected a cumulative loss of £39m (2017: £1m cumulative loss), all of which is in relation to ongoing hedges. The fair value of derivatives in cash flow hedges decreased by £58m in the year (2017: £84m decrease), and a £3m loss (2017: £4m gain) was recycled to interest income in line with hedged items affecting profit or loss. A £6m loss (2017: £0.3m loss) was transferred to non-interest income due to ineffectiveness arising from cash flow hedges. These movements were offset by a deferred tax credit of £11m (2017: credit of £21m).

4.1.5.4 Equity-based compensation reserve

The Group's equity based compensation reserve records the value of equity settled share based payment benefits provided to the Group's employees as part of their remuneration that has been charged through the income statement and adjusted for deferred tax.

4.2 Equity based compensation

Accounting policy

The Group operates a number of equity settled share based compensation plans in respect of services received from certain of its employees. The fair value of the services received is recognised as an expense. The total amount to be expensed is measured by reference to the fair value of the Company's shares, performance options or performance rights granted, including, where relevant, any market performance conditions and any non-vesting conditions. The impacts of any service and non-market performance vesting conditions are not included in the fair value and instead are included in estimating the number of awards or options that are expected to vest.

The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. A corresponding credit is recognised in the equity based compensation reserve, adjusted for deferred tax. In some circumstances employees may provide services in advance of the grant date and therefore the grant date fair value is estimated for the purposes of recognising the expense during the period between the start of the service period and the grant date.

At the end of each reporting period, the Group revises its estimates of the number of shares, performance options and performance rights that are expected to vest based on the non-market and service vesting conditions. The impact of the revision to original estimates, if any, is recognised in the income statement, with a corresponding adjustment to the equity based compensation reserve.

The equity settled share based payment charge for the year is £9m (2017: £6m).

CYBG awards

The Group made a number of awards under its share plans:

Plan	Eligible employees	Nature of award	Vesting conditions[1]	Grant dates[2]
DEP[3]	Selected employees	Conditional rights to shares	Continuing employment or leaving in certain limited circumstances	2016, 2017 and 2018
LTIP	Selected senior employees	Conditional rights to shares	Continuing employment or leaving in certain limited circumstances and achievement of delivery of the Group's strategic goals and growth in shareholder value	2017 and 2018
SIP	All employees	Non-conditional share award	Continuing employment	2016 and 2017

(1) All awards are subject to vesting conditions and therefore may or may not vest.
(2) The year in which grants have been made under the relevant plan.
(3) Grants made under the DEP are made the year following the financial year to which they relate.

Further detail on each plan is provided below:

DEP

Under the plan employees were awarded conditional rights to CYBG PLC shares. The shares are subject to forfeiture conditions including forfeiture as a result of resignation, termination by the Group or failure to meet compliance requirements. Awards include:

– The upfront and deferred elements of bonus awards where required to comply with the PRA Remuneration Code or the Group's deferral policy.

– Buyout of equity from previous employment for senior new hires.

– Demerger awards which are also subject to the achievement of performance conditions over a three-year period. Details of the performance conditions are set out in the Directors' remuneration report.

LTIP

Under the plan employees were awarded conditional rights to CYBG PLC shares. The shares are subject to forfeiture conditions including forfeiture as a result of resignation, termination by the Group or failure to meet compliance requirements.

The performance conditions of the plan must be met over a three year period. The measures reflect a balanced approach between financial and non-financial performance and are aligned to the organisation's strategic goals. Measures, relative weightings and the quantum for assessing performance are outlined in the Directors' remuneration report section.

SIP

Eligible employees at the date of the award, were awarded Group shares, which are held in the Share Incentive Plan Trust (SIP Trust). Awards are not subject to performance conditions and participants are the beneficial owners of the shares granted to them, but not the registered owners. Voting rights over the shares are normally exercised by the registered owner at the direction of the participants. For the 2015 Demerger award, leavers (with the exception of gross misconduct) retain their awards but they must withdraw their shares from the SIP Trust.

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Notes to the consolidated financial statements

Section 4: Capital continued

4.2 Equity based compensation continued

Awards/rights made during the year

Plan	Number outstanding at 1 October 2017	Number awarded	Number forfeited	Number released	**Number outstanding at 30 September 2018**	Average fair value of awards at grant pence
DEP						
2015 Demerger	2,038,052	–	–	–	**2,038,052**	196.96
2015 Bonus	135,595	–	–	(80,642)	**54,953**	195.17
2015 Commencement	65,068	–	–	(39,383)	**25,685**	194.67
2016 Bonus	543,195	–	(1,276)	(520,516)	**21,403**	266.03
2016 Commencement	131,996	–	–	(74,725)	**57,271**	266.03
2017 Bonus	–	1,319,049	(4,263)	(721,979)	**592,807**	313.20
2017 Commencement	–	98,499	–	(30,332)	**68,167**	313.20
2018 Commencement	–	7,796	–	(7,796)	**–**	313.20
LTIP						
2016 LTIP	2,243,387	–	(10,996)	–	**2,232,391**	266.03
2017 LTIP	–	2,332,462	(17,975)	–	**2,314,487**	313.20
SIP						
2015 Demerger	1,483,008	–	(1,536)[1]	(184,320)[2]	**1,297,152**	194.67
2017 Free Share	–	998,520	(636)	(91,743)	**906,141**	313.20

(1) Forfeited shares remain in the SIP Trust.
(2) Shares withdrawn from SIP Trust on leaving the Group.

Determination of grant date fair values

Participants of the DEP and LTIP plans are not entitled to dividends until the awards vest, but the number of shares which vest may be increased to reflect the value of dividends that would have been paid up to the end of the holding period for the awards, subject to the extent permitted under the relevant remuneration regulation. Accordingly, the grant date fair value of the awards with only service conditions and/or non-market performance conditions has been taken as the market value of the Company's ordinary shares at the grant date. Where awards are subject to non-market performance conditions, an estimate is made of the number of awards expected to vest in order to determine the overall share-based payment charge to be recognised over the vesting period.

The Group has not issued awards under any CYBG plan with market performance conditions.

Section 5: Other notes

5.1 Contingent liabilities and commitments

Accounting policy

Financial guarantees

The Group provides guarantees in the normal course of business on behalf of its customers. Guarantees written are conditional commitments issued by the Group to guarantee the performance of a customer to a third party and are primarily issued to support direct financial obligations such as commercial bills or other debt instruments issued by a counterparty. The rating of the Group as a guarantee provider enhances the marketability of the paper issued by the counterparty in these circumstances. Financial guarantee contracts are initially recorded at fair value which is equal to the premium received, unless there is evidence to the contrary.

Operating lease commitments

The leases entered into by the Group are primarily operating leases; with operating lease rentals charged to the income statement on a straight line basis over the period of the lease. The Group discloses its obligations for future minimum payments under non-cancellable leases.

Contingent liabilities

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefit is uncertain or cannot be reliably measured. Contingent liabilities are not recognised on the balance sheet but are disclosed unless they are remote.

The table below sets out the amounts of financial guarantees and commitments which are not recorded on the balance sheet. Financial guarantees and commitments are credit-related instruments which include acceptances, letters of credit, guarantees and commitments to extend credit. The amounts do not represent the amounts at risk at the balance sheet date but the amounts that would be at risk should the contracts be fully drawn upon and the customer defaults. Since a significant portion of guarantees and commitments is expected to expire without being drawn upon, the total of the contract amounts is not representative of future liquidity requirements.

Financial guarantees

	2018 £m	2017 £m
Guarantees and assets pledged as collateral security:		
Due in less than 3 months	**26**	19
Due between 3 months and 1 year	**36**	40
Due between 1 year and 3 years	**10**	7
Due between 3 years and 5 years	**2**	3
Due after 5 years	**45**	42
	119	111
Other credit commitments		
Undrawn formal standby facilities, credit lines and other commitments to lend at call	**7,016**	8,408

Capital commitments

The Group had future capital expenditure which had been contracted for but not provided for at 30 September 2018 of £1m (2017: £1m).

Financial statements

Notes to the consolidated financial statements

Section 5: Other notes continued

5.1 Contingent liabilities and commitments continued

Operating lease commitments

	2018 £m	2017 £m
Leases as lessor		
Future minimum lease payments under non-cancellable operating leases are:		
Within 1 year	**1**	1
Between 1 year and 5 years	**4**	4
Over 5 years	**1**	–
	6	5
Leases as lessee		
Future minimum lease payments under non-cancellable operating leases are:		
Within 1 year	**29**	30
Between 1 year and 5 years	**96**	100
Over 5 years	**124**	137
	249	267

Other contingent liabilities

Conduct risk related matters

There continues to be significant uncertainty and thus judgement is required in determining the quantum of conduct risk related liabilities, with note 3.14 reflecting the Group's current position in relation to redress provisions including those for PPI. The final amount required to settle the Group's potential liabilities for these, and other conduct related matters, is materially uncertain. Contingent liabilities include those matters where redress is likely to be paid and costs incurred but the amounts cannot currently be estimated.

The Group will continue to reassess the adequacy of provisions for these matters and the assumptions underlying the calculations at each reporting date based upon experience and other relevant factors at that time.

Legal claims

The Group is named in and is defending a number of legal claims arising in the ordinary course of business. No material adverse impact on the financial position of the Group is expected to arise from the ultimate resolution of these legal actions.

5.2 Notes to the statement of cash flows

	2018 £m	2017 £m
Adjustments included in the profit before tax		
Interest receivable	**(1,113)**	(1,075)
Interest payable	**262**	231
Depreciation and amortisation (note 2.4)	**89**	87
Derivative financial instruments fair value movements	**(3)**	(6)
Impairment losses on credit exposures (note 3.6)	**41**	48
Fair value movement on investment properties	**–**	1
Equity based compensation	**9**	6
Gain on disposal of VocaLink	**–**	(20)
	(715)	(728)
Changes in operating assets		
Net (increase)/decrease in:		
Balances with supervisory central banks	**(31)**	(1)
Due from other banks	**339**	(221)
Derivative financial instruments	**18**	280
Financial assets at fair value through profit or loss	**117**	237
Loans and advances to customers	**(1,488)**	(2,140)
Other assets	**(14)**	(12)
	(1,059)	(1,857)
Changes in operating liabilities		
Net increase/(decrease) in:		
Due to other banks	**(1,053)**	608
Derivative financial instruments	**(16)**	(221)
Financial liabilities at fair value through profit or loss	**(11)**	(21)
Due to customers	**1,186**	699
Provisions for liabilities and charges	**(223)**	(298)
Defined benefit pension obligations	**(14)**	(128)
Other liabilities	**9**	280
	(122)	919

For the purposes of the statement of cash flows, cash and cash equivalents comprise the following balances with less than three months maturity from the date of acquisition. This includes cash and liquid assets and amounts due to other banks (to the extent less than 90 days).

	2018 £m	2017 £m
Cash and balances with central banks (note 3.1)	**6,498**	6,893
Other assets	**86**	99
Due to other banks	**(12)**	(12)
Other liabilities	**(30)**	(28)
	6,542	6,952

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Notes to the consolidated financial statements

Section 5: Other notes continued

5.3 Related party transactions

Compensation of key management personnel (KMP)

KMP comprises Directors of the Company and members of the Executive Leadership Team.

	2018 £m	2017 £m
Salaries and short-term benefits	9	8
Other long-term employee benefits	–	–
Termination benefits	–	–
Equity based compensation(1)	1	1
	10	9

(1) Basis of the expense recognised in the year in accordance with IFRS 2 'Equity based compensations', including associated employers' NIC.

The following information regarding Directors' remuneration is presented in accordance with the Companies Act 2006.

	2018 £m	2017 £m
Aggregate remuneration	5	5

In addition to the above, £0.4m (2017: £0.2m) was expensed relating to LTIP. None of the Directors were members of the Group's defined contribution pension scheme during 2018 (2017: none). None of the Directors were members of the Group's defined benefit pension scheme during 2018 (2017: one). None of the Directors hold share options and none were exercised during the year (2017: none).

Transactions with KMP

KMP, their close family members and any entities controlled or significantly influenced by the KMP have undertaken the following transactions with the Group in the normal course of business. The transactions were made on the same terms and conditions as applicable to other Group employees, or on normal commercial terms.

	2018 £m	2017 £m
Loans and advances	2	2
Deposits	3	4

No provisions have been recognised in respect of loans provided to the KMP (2017: £Nil). There were no debts written off or forgiven during the year to 30 September 2018 (2017: £Nil). Included in the above are six (2017: three) loans totalling £2m (2017: £1m) made to Directors. In addition to the above, there are guarantees of £Nil (2017: £Nil) made to Directors and their related parties.

Other related party transactions

The Group and the Trustee to the pension scheme have entered into a contingent Security Arrangement which provides additional support to the Scheme by underpinning recovery plan contributions and some additional investment risk. The security is in the form of a pre-agreed maximum level of assets that are set aside for the benefit of the Pension Scheme in certain trigger events. These assets are held by Red Grey Square Funding LLP, an insolvency remote consolidated structured entity.

The Group incurred costs in relation to pension scheme administration. These costs, which amounted to £0.3m in the year ended 30 September 2018 (2017: £0.3m), were charged to the Group sponsored scheme. The Group has deposits of £36m (2017: £20m) at the year end placed by the Scheme at market rates.

Pension contributions of £18m (2017: £69m) were made during the year to the Yorkshire and Clydesdale Bank Pension Scheme sponsored by the Group (note 3.16).

5.4 Pillar 3 disclosures

Basel III Capital Requirements Directive IV

Pillar 3 disclosure requirements are set out in Part Eight of the CRR. The consolidated disclosures of the Group, for the 2018 financial year, will be issued concurrently with the Annual Report and Accounts and will be found at www.cybg.com/investor-centre/financial-results/.

5.5 Post balance sheet events

IRB accreditation

On 10 October 2018, the Group received IRB accreditation from the PRA for both its mortgage and SME portfolios. The Group continues to progress its Retail unsecured lending IRB application.

Acquisition

On 15 October 2018, the Company acquired all the voting rights in Virgin Money by means of a scheme of arrangement under Part 26 of the UK Companies Act 2006 for a purchase consideration of £1.6bn. This comprised the fair value of approximately 541m new CYBG PLC ordinary shares in exchange for all Virgin Money shares at a ratio of 1.2125 CYBG shares for each Virgin Money share. Following completion, Virgin Money shareholders owned approximately 38% of the Combined Group (on a fully diluted basis).

The fair value of the shares issued was calculated using the market price of 286.4 pence per share, on the London Stock Exchange at its close of business on 12 October 2018.

In seeking to address the underlying trends of scale and adaptability within the banking industry, the combination will bring together the two challenger banks to create a national competitor to the large incumbent banks. The combination will offer retail and SME customers an alternative to the status quo.

Due to the acquisition date of Virgin Money taking place on 15 October 2018, there has been insufficient time to complete the fair value exercise as required by IFRS 3: 'Business combinations'. Accordingly, the fair value of the net assets acquired and any resultant goodwill to be recognised as a result of the acquisition have not yet been determined.

Following completion, CB PLC subsequently acquired all the voting rights in Virgin Money for a consideration of £1.6bn.

Guaranteed minimum payments (GMP) equalisation

On 26 October 2018 the High Court ruled on a landmark pensions case relating to the defined benefits pension schemes operated by Lloyds Banking Group. The case dealt with GMP provided by schemes which were contracted-out of the State Earnings-Related Pension Scheme (SERPS) up until 5 April 1997, with the High Court ruling concluding that the associated benefits were inherently unequal between males and females because of their different state pension retirement ages.

The High Court has confirmed that it is necessary for schemes to equalise benefits, for those pensions accrued between 17 May 1990 and 6 April 1997, to address the inherent inequality of GMP between males and females. There is no single prescribed solution in order to equalise following this judgment, and it is anticipated that significant discussion and guidance will be required as to the permissible equalisation method to be adopted in any particular case.

The Group is currently assessing the impact of this recent ruling on its defined benefit pension scheme, and will work with its key advisors to ensure compliance with the recent findings as appropriate. Due to the early stage of this assessment and the complexity involved in such an exercise, it is not possible to quantify the extent of any additional financial obligation at this time.

Financial statements

Company balance sheet

as at 30 September	Note	2018 £m	2017 £m
Assets			
Due from related entities	6.6	**1,314**	803
Financial assets available for sale		**1**	–
Due from other banks		**–**	364
Current tax assets		**1**	1
Investments in controlled entities	6.2	**2,268**	2,249
Other assets		**30**	–
Total assets		**3,614**	3,417
Liabilities			
Due to other banks		**110**	91
Due to related entities	6.6	**41**	366
Debt securities in issue	6.3	**1,276**	779
Other liabilities		**1**	2
Total liabilities		**1,428**	1,238
Equity			
Share capital		**89**	88
Other equity instruments	6.5	**450**	450
Merger reserve	6.5	**633**	633
Other reserves	6.5	**9**	6
Retained earnings	6.5	**1,005**	1,002
Total equity		**2,186**	2,179
Total liabilities and equity		**3,614**	3,417

The Company made a profit of £34m (2017: profit of £24m) during the year.

The notes on pages 239 to 243 form an integral part of these financial statements.

Company statement of changes in equity

for the year ended 30 September	Note	Share capital £m	Merger reserve £m	Other equity instruments £m	Other reserves: Equity based compensation reserve £m	Other reserves: Cash flow hedge reserve £m	Retained earnings £m	Total equity £m
At 1 October 2016	6.5	88	633	450	6	(3)	1,003	2,177
Profit for the year		–	–	–	–	–	24	24
Other comprehensive income, net of tax		–	–	–	–	1	–	1
Total comprehensive income for the year		–	–	–	–	1	24	25
AT1 distributions paid (net of tax)		–	–	–	–	–	(29)	(29)
Transfer from equity based compensation reserve		–	–	–	(4)	–	4	–
Equity based compensation		–	–	–	6	–	–	6
As at 30 September 2017	6.5	88	633	450	8	(2)	1,002	2,179
Profit for the year		–	–	–	–	–	34	34
Other comprehensive income, net of tax		–	–	–	–	1	–	1
Total comprehensive income for the year		–	–	–	–	1	34	35
Dividends paid to ordinary shareholders		–	–	–	–	–	(9)	(9)
AT1 distributions paid (net of tax)		–	–	–	–	–	(29)	(29)
Transfer from equity based compensation reserve		–	–	–	(7)	–	7	–
Ordinary shares issued		1	–	–	–	–	–	1
Equity based compensation		–	–	–	9	–	–	9
As at 30 September 2018	6.5	**89**	**633**	**450**	**10**	**(1)**	**1,005**	**2,186**

The notes on pages 239 to 243 form an integral part of these financial statements.

Financial statements

Company statement of cash flows

For the year ended 30 September	2018 £m	2017 £m
Operating activities		
Profit on ordinary activities before tax	**40**	29
Adjustments for:		
Changes in operating assets		
Due from other banks	**511**	(357)
Changes in operating liabilities		
Due to other banks	**–**	55
Other liabilities	**(2)**	–
Interest receivable	**(33)**	(25)
Interest payable	**36**	27
Costs recharged from subsidiary	**1**	–
Net (decrease)/increase in amounts due to related entities	**(504)**	359
Tax received – Group relief	**1**	3
Net cash provided by operating activities	**50**	91
Cash flows from investing activities		
Investment in controlled entities	**–**	(49)
Net cash used in investing activities	**–**	(49)
Cash flows from financing activities		
Interest received	**34**	22
Interest paid	**(34)**	(24)
Issuance of medium-term notes/subordinated debt	**497**	298
Net decrease in amounts due from related entities	**(487)**	(296)
Ordinary dividends paid	**(9)**	–
AT1 distributions	**(36)**	(36)
Net cash used in financing activities	**(35)**	(36)
Net increase in cash and cash equivalents	**15**	6
Cash and cash equivalents at the beginning of the year	**21**	15
Cash and cash equivalents at the end of the year	**36**	21

Cash and cash equivalents comprise the following balances with less than three months' maturity from the date of acquisition.

	2018 £m	2017 £m
Due from related parties (note 6.6)	**36**	21

	Debt securities in issue £m	Total £m
At 1 October 2017	779	779
Cash flows:		
Issuances	497	479
At 30 September 2018	**1,276**	**1,276**

The notes on pages 239 to 243 form an integral part of these financial statements.

Notes to the Company financial statements

Section 6: Notes to the Company financial statements

6.1 Company basis of preparation

The Company is incorporated in the UK and registered in England and Wales.

The Company financial statements of CYBG PLC, the Parent Company (the Company), which should be read in conjunction with the Group Directors' Report, have been prepared on a going concern basis in accordance with IFRSs as adopted by the EU and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

No individual income statement or statement of comprehensive income is presented for the Company, as permitted by Section 408 of the Companies Act 2006.

Basis of measurement

The financial information has been prepared under the historical cost convention. The preparation of the financial statements in conformity with IFRS 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 underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

The accounting policies of the Company are the same as those of the Group which are set out in the notes to the consolidated financial statements except that the Company has no policy in respect of consolidation. These accounting policies have been applied consistently to all periods presented in these financial statements.

6.2 Company investments in controlled entities

Accounting policy

The Company's investments in controlled entities are valued at cost or valuation less any provision for impairment. Such investments are reviewed annually for potential evidence of impairment, or more frequently when there are indications that impairment may have occurred. Losses relating to impairment in the value of shares in controlled entities are recognised in the income statement.

	2018 £m	2017 £m
At 30 September	**2,268**	2,249

As disclosed in note 3.14 to the consolidated financial statements, the Company has entered into a Conduct Indemnity Deed with NAB. Claims under the Conduct Indemnity Deed are made by the Company, while the provisions in respect of the qualifying conduct costs are raised and incurred by its principal trading subsidiary, Clydesdale Bank PLC. As a consequence, the recognition and measurement basis of the Capped Indemnity in the Company differs from that of the Group. For the Company, the substance of the indemnity agreement is that of variable consideration in relation to its investment in controlled entities.

When a claim is raised under the Capped Indemnity, the Company recognises a receivable from NAB (presented within amounts due from other banks) with a corresponding decrease in the cost of the Company's investments in controlled entities. The Company does not recognise any income or expense in relation to claims under the Capped Indemnity. It is intended that upon collection of the claim proceeds from NAB the capital impact of providing for Relevant Conduct Matters in Clydesdale Bank PLC is mitigated by the Company using the proceeds to subscribe for share capital. During the year ended 30 September 2018 the Company's investments in controlled entities was reduced by £148m (2017: £536m) in relation to Conduct Indemnity adjustments and the Company subscribed for £511m (2017: £179m) of additional share capital in its controlled entities.

Where provisions for Relevant Conduct Matters are increased in respect of a reporting period, but proceeds from that claim are not received from NAB prior to the reporting date, the Company has put in place an agreement with Clydesdale Bank PLC in order to mitigate the effect of capital losses at the end of the reporting period. Upon raising a provision for a Relevant Conduct Matter, the Company indemnifies Clydesdale Bank PLC for the Qualifying Conduct Costs (excluding the Group's loss share) until it subscribes for an equivalent amount of capital in Clydesdale Bank PLC. The Company recognises a capital contribution within investments in controlled entities and a liability in amounts due to other entities in respect of these amounts. This totalled £Nil at 30 September 2018 (2017: £364m).

Financial statements

Notes to the Company financial statements

Section 6: Notes to the Company financial statements continued

6.2 Company investments in controlled entities continued

The table below represents the wholly owned subsidiary undertakings of the Group and Company as at 30 September 2018:

Wholly owned subsidiary undertakings	Nature of business	Class of share held	Proportion held	Country of incorporation	Registered office
Direct holdings					
Clydesdale Bank PLC	Banking	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
CYB Investments Limited	Holding company	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
Indirect holdings					
CGF No 9 Limited	Leasing	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
Clydesdale Bank Asset Finance Limited	Leasing	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
Clydesdale Bank (Head Office) Nominees Limited	In liquidation	Limited by guarantee	100%	Scotland	Saltire Court, 20 Castle Terrace, Edinburgh, EH1 2DB
CYB Intermediaries Limited	Insurance intermediary	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
St Vincent (Equities) Limited	Investment company	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
Yorkshire Bank Home Loans Limited	Mortgage finance	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
CB Nominees Limited	Dormant	Limited by guarantee	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
CYB SSP Trustee Limited	Dormant	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
YCB DC Trustee Limited	Dormant	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
YCBPS Property Nominee Company Limited	Dormant	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ
Yorkshire and Clydesdale Bank Pension Trustee Limited	Dormant	Ordinary	100%	Scotland	30 St Vincent Place, Glasgow, G1 2HL
Yorkshire Bank PLC	Dormant	Ordinary	100%	England	20 Merrion Way, Leeds, Yorkshire, LS2 8NZ

The Company also has an interest in the Yorkshire and Clydesdale Bank Foundation, a charitable foundation registered in Scotland as a company limited by guarantee. Clydesdale Bank PLC acts as a guarantor for £10 and is the main donor.

All subsidiaries have a 30 September year end.

During the year, Craig Yr Haul Management Company Limited, 11 Tudor Hill Residential Management Company Limited, Linton Springs Residential Management Company Limited, and St Johns Place Residential Management Company Limited were disposed of for no gain or loss.

CYB Intermediaries Holdings Limited and CYB Services Limited were also liquidated during the year.

In addition to the above, the Company also has an interest in a number of structured entities:

Other controlled entities as at 30 September 2018	Nature of business	Country of incorporation	Registered office
Clydesdale Covered Bonds No. 2 LLP	Acquisition of mortgage loans	England	20 Merrion Way, Leeds, LS2 8NZ
Lanark Holdings Limited	Holding company	England	Winchester House, Mail Stop 429, 1 Great Winchester Street, London, EC2N 2DB
Lanark Trustees Limited	Mortgages trustee	England	Winchester House, Mail Stop 429, 1 Great Winchester Street, London, EC2N 2DB
Lanark Funding Limited	Funding company	England	Winchester House, Mail Stop 429, 1 Great Winchester Street, London, EC2N 2DB
Lanark Master Issuer PLC	Issuer of securitised notes	England	Winchester House, Mail Stop 429, 1 Great Winchester Street, London, EC2N 2DB
Lannraig Holdings Limited	Holding company	England	35 Great St. Helen's, London, EC3A 6AP, United Kingdom
Lannraig Trustees Limited	Mortgages trustee	Jersey	44 Esplanade, St Helier, Jersey, JE4 9WG, Channel Islands
Lannraig Funding Limited	Funding company	England	35 Great St. Helen's, London, EC3A 6AP, United Kingdom
Lannraig Master Issuer PLC	Issuer of securitised notes	England	35 Great St. Helen's, London, EC3A 6AP, United Kingdom
Red Grey Square Funding LLP	Security provider	England	35 Great St. Helen's, London, EC3A 6AP, United Kingdom

All of the above structured entities have a financial year end of 30 September.

Details of the Group's interests in consolidated structured entities associated with securitisation and covered bond arrangements are set out in note 3.7.

6.3 Company debt securities in issue

	2018 £m	2017 £m
Subordinated debt	**479**	479
Medium-term notes	**797**	300
	1,276	779

Information on subordinated debt and medium-term notes is provided in note 3.15 to the consolidated financial statements.

The fair value hedge adjustment included in note 3.15 is not applicable at Company level.

Financial statements

Notes to the Company financial statements

Section 6: Notes to the Company financial statements continued

6.4 Company fair value of financial instruments

Fair value of financial instruments carried at amortised cost

The tables below show a comparison of the carrying amounts of financial assets and liabilities measured at amortised cost as reported on the balance sheet and their fair values where these are not approximately equal.

There are various limitations inherent in this fair value disclosure particularly where prices may not represent the underlying value due to dislocation in the market. Not all of the Company's financial instruments can be exchanged in an active trading market.

	30 September 2018					30 September 2017				
			Fair value measurement using:					Fair value measurement using:		
Company	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m	Carrying value £m	Fair value £m	Level 1 £m	Level 2 £m	Level 3 £m
Financial assets										
Due from related entities	**1,315**	**1,325**	**–**	**1,325**	**–**	803	819	–	819	–
Financial liabilities										
Debt securities in issue	**1,276**	**1,279**	**1,279**	**–**	**–**	779	795	795	–	–

Notes

The Company's fair values disclosed for financial instruments at amortised cost are based on the following methodologies and assumptions:

Amounts due from related entities – The fair value of subordinated debt and medium-term notes due from related entities is derived from quoted market prices of the debt security in issue after accounting for differences in credit spread. All other amounts due from related entities are redeemable at call and therefore carrying value approximates fair value.

Debt securities in issue – The fair value of subordinated debt is taken directly from quoted market prices.

The Company also holds £1m of debt investments measured at fair value, which were purchased from Clydesdale Bank PLC at 30 September 2018. These investments are categorised as Level 3, as the valuations incorporate significant unobservable inputs. Valuation is based on the transaction price which the Company believes is the best representation of an exit price. The significant unobservable input is the recoverable amount which could range from 0 to 100%.

6.5 Company reserves

6.5.1 Cash flow hedge reserve

As at 30 September 2018, the cash flow hedge reserve comprised crystallised fair value losses arising from a matured cash flow hedge of £1m (2017: £2m). This hedge relationship was entered into to mitigate the interest rate risk exposure prior to the issuance of the subordinated debt. The hedge matured at the date of issue. The balance on the cash flow hedge reserve within the statement of changes in equity is net of tax.

The crystallised fair value losses will be amortised from the cash flow hedge reserve to the income statement over the life of the subordinated debt. In respect of this, a £0.8m loss (2017: £0.8m loss) was recycled to the income statement during the year.

6.5.2 Other equity instruments and reserves

Information on other equity instruments and other reserves is provided in note 4.1 to the Group's consolidated financial statements. Included within retained earnings is the profit for the year ended 30 September 2018 of £34m (2017: profit of £24m).

6.5.3 Available distributable items

Distributable reserves are determined as required by the Companies Act 2006 by reference to a company's individual financial statements. At 30 September 2018, the Company had accumulated distributable reserves of £1,005m (2017: £1,002m).

6.6 Company related party transactions

During the year there have been transactions between the Company, controlled entities of the Company, and other related parties. The Company receives and provides a range of services from/to its principal subsidiary undertaking, including loans and deposits.

Amounts due from controlled entities of the Company

	2018 £m	2017 £m
Cash and cash equivalents	**36**	21
Other receivables	**1**	–
Subordinated debt	**480**	482
Medium-term notes	**797**	300
Total amounts due from related entities	**1,314**	803

On 25 September 2018, the Company purchased £500m of 4% fixed rate reset callable medium-term notes with a final maturity date of 25 September 2026 from Clydesdale Bank PLC. Medium-term notes comprise dated, unsecured loans and are issued by Clydesdale Bank PLC.

On 22 June 2017, the Company purchased £300m of 3.125% fixed to floating rate callable medium-term notes with a final maturity date of 22 June 2025 from Clydesdale Bank PLC. Medium-term notes comprise dated, unsecured loans and are issued by Clydesdale Bank PLC. These securities will, in the event of the winding-up of the issuer, be subordinated to the claims of depositors and all other creditors of the issuer, other than creditors whose claims rank junior to the claims of the holders of the medium-term note liabilities, including those of subordinated debt holders.

On 8 February 2016, the Company purchased £475m of 5% fixed rate reset callable subordinated debt with a final maturity date of 9 February 2026 from Clydesdale Bank PLC. Subordinated debt comprises dated, unsecured loan capital and is issued by Clydesdale Bank PLC. These securities will, in the event of the winding-up of the issuer, be subordinated to the claims of depositors and all other creditors of the issuer, other than creditors whose claims rank junior to the claims of the holders of subordinated liabilities.

Amounts due to controlled entities of the Company

	2018 £m	2017 £m
Amounts due in relation to conduct indemnity	**–**	364
Other payables	**41**	2
Total amounts due to related entities	**41**	366

Other related party transactions

As discussed in note 4.2 to the consolidated financial statements, the Group provides share based compensation to employees through a number of schemes, all in relation to shares in the Company. The cost of providing these benefits is recharged to the employing company, Clydesdale Bank PLC. Recharges are calculated based on the fair value of awards expensed in the period in accordance with IFRS 2: 'Share based payments'. The key management personnel of the Company are the key management personnel of the Group, with relevant disclosures given in note 5.3 to the consolidated financial statements. The Company has no employees (2017: Nil).

Additional information

Additional information

Measuring financial performance – glossary

Financial performance measures

As highlighted in the Strategic report, the Financial results section and the Risk report, the Group utilises a range of performance measures[1] to assess the Group's performance. These can be grouped under the following headings:

- Profitability;
- Asset quality; and
- Capital optimisation.

The performance measures used are a combination of statutory, regulatory and alternative performance measures; with the type of performance measure used dependent on the component elements and source of what is being measured.

Statutory performance measures (S)
These are used when the basis of the calculation is derived from a measure that is required under generally accepted accounting principles (GAAP). An example of this would be references to earnings per share.

Regulatory performance measures (R)
These are used when the basis of the calculation is required and specified by the Group's regulators. Examples of this would be the leverage ratio and the Tier 1 ratio.

Alternative performance measures (A)
These are used when the basis of the calculation is derived from a non-GAAP measure – also referred to as APMs. Examples of this would be the cost to income ratio and the return on tangible equity.

Where a performance measure refers to an 'underlying' metric, the detail on how this measure is arrived at, along with management's reasoning for excluding the item from the Group's current underlying performance rationale, can be found on page 248, directly following this section. These adjustments to the Group's statutory results made by management are necessary to provide a more meaningful underlying basis.

Descriptions of the performance measures used, including the basis of calculation where appropriate, are set out below:

Profitability:

Term	Type	Definition
Net interest margin **(NIM)**	**A**	Net interest income as a percentage of average interest earning assets for a given period. Net interest income of £851m (2017: £844m) is divided by average interest earning assets for a given period of £39,417m (2017: £37,697m) (which is then adjusted to exclude short-term repos used for liquidity management purposes, amounts received under the Conduct Indemnity and not yet utilised, and any associated income). As a result of the exclusions noted above, average interest earning assets used as the denominator have reduced by £120m (2017: £491m) and the net interest income numerator has reduced by £0.4m (2017: £1.1m).
Underlying RoTE	**A**	Underlying profit after tax attributable to ordinary equity holders as a percentage of average tangible equity (total equity less intangible assets and AT1) for a given period.
Underlying CIR	**A**	Underlying total operating expenses as a percentage of underlying total operating income for a given period.
Underlying return on assets	**A**	Underlying profit after tax as a percentage of average total assets for a given period.
Underlying basic EPS	**A**	Underlying profit after tax attributable to ordinary equity holders divided by the weighted average number of ordinary shares in issue for a given period.
Underlying profit after tax attributable to ordinary equity holders	**A**	Underlying profit before tax of £331m (2017: £293m) less tax charge of £33m (2017: £73m), less AT1 distributions (net of tax relief) of £29m (2017: £29m) and was equal to £269m (2017: £191m). The underlying tax charge is calculated by applying the statutory tax rate for the relevant period to the taxable items adjusted on the underlying basis.
Statutory return on tangible equity **(RoTE)**	**A**	Statutory profit/(loss) after tax attributable to ordinary equity holders as a percentage of average tangible equity (total equity less intangible assets and AT1) for a given period.
Statutory cost to income ratio **(CIR)**	**A**	Statutory total operating expenses as a percentage of total operating income for a given period.

(1) The term 'financial performance measure' covers all metrics, ratios and percentage calculations used to assess the Group's performance and is interchangeable with similar terminology used in the Annual Report and Accounts such as highlights, key metrics, key performance indicators (KPIs) and key credit metrics.

Term	Type	Definition
Statutory return on assets	A	Statutory profit/(loss) after tax as a percentage of average total assets for a given period.
Statutory basic earnings per share **(EPS)**	S	Statutory profit/(loss) attributable to ordinary equity shareholders including tax relief on any distributions made to other equity holders divided by the weighted average number of ordinary shares in issue for a given period.

Asset quality:

Term	Type	Definition
Impairment charge to average customer loans **(cost of risk)**	A	Impairment losses on credit exposures plus credit risk adjustment on fair value loans to average customer loans (defined as loans and advances to customers, other financial assets at fair value and due from customers on acceptances).
90+ days past due **(DPD)** plus impaired assets to customer loans	A	Customer loans that are either impaired or where the repayment is more than 90 days overdue as a percentage of total customer loans at a given date.
Specific provision to gross impaired assets	A	The specific impairment provision on credit exposures as a percentage of gross impaired assets at a given date.
Total provision to customer loans	A	Total impairment provision on credit exposures as a percentage of total customer loans at a given date.
Indexed loan to value **(LTV)** of the mortgage portfolio	A	The mortgage portfolio weighted by balance and indexed using the MIAC Acadametrics indices at a given date.
Net write offs to customer loans	A	Net write offs, including loans at fair value, as a percentage of total customer loans at a given date.

Capital optimisation:

Term	Type	Definition
Common Equity Tier 1 **(CET1)** ratio	R	CET1 capital divided by RWAs at a given date.
Tier 1 ratio	R	Tier 1 capital as a percentage of risk weighted assets.
Total capital ratio	R	Total capital resources divided by risk weighted assets at a given date.
Leverage ratio	R	This is a regulatory standard ratio proposed by the Basel III as a supplementary measure to the risk based capital requirements. It is intended to constrain the build-up of excess leverage in the banking sector and is calculated by dividing Tier 1 capital resources by a defined measure of on and off-balance sheet items plus derivatives.
Modified leverage ratio	R	The Group's leverage ratio on a modified basis, excluding qualifying central bank claims from the exposure measure in accordance with the policy statement issued by the PRA in October 2017.
Tangible net asset value **(TNAV)** per share	A	Tangible equity as at the period end divided by the closing number of ordinary shares.
Loan to deposit ratio **(LDR)**	R	Customer loans as a percentage of customer deposits at a given date.
Liquidity coverage ratio **(LCR)**	R	Measures the surplus (or deficit) of the Group's high quality liquid assets relative to weighted net stressed cash outflows over a 30 day period. It assesses whether the Group has sufficient liquid assets to withstand a short-term liquidity stress based on cash outflow assumptions provided by regulators.
Net stable funding ratio **(NSFR)**	R	The total amount of available stable funding divided by the total amount of required stable funding, expressed as a percentage. The Group monitors the NSFR based on its own interpretations of current guidance available for CRD IV NSFR reporting. Therefore, the reported NSFR may change over time with regulatory developments. Due to possible differences in interpretation of the rules, the Group's ratio may not be directly comparable with those of other financial institutions.

Additional information

Measuring financial performance – glossary

Underlying adjustments to the statutory view of performance

In arriving at an underlying basis, the effects of certain items that do not promote an understanding of historical or future trends of earnings or cash flows are removed; with management believing this presents a set of results that provide a more reflective year-on-year comparison. These items are:

Item	FY2018 £m	FY2017 £m	Description	Reason for exclusion from the Group's current underlying performance
Legacy conduct charges	**(396)**	(58)	These are customer redress and associated costs arising from legacy products and past sales practices.	These costs are historical in nature and are not indicative of the Group's current underlying performance.
Restructuring and related expense	**(38)**	(67)	Restructuring of the business is currently ongoing with costs including redundancy payments, property vacation costs, associated enablement costs and non-recurring costs arising from operational transformation.	These costs are significant and are part of the Group's strategic objective in simplifying and streamlining operations and processes to enhance productivity. Consequently, this expense is not viewed as a normal ongoing operating cost to the Group.
Virgin Money acquisition costs	**(37)**	–	Costs incurred directly relating to the acquisition of Virgin Money.	These costs are significant and not indicative of the Group's underlying performance.
RBS alternative remedies package spend	**(16)**	–	Costs incurred, in relation to the RBS alternative remedies package, to enable strategic and inorganic growth.	These costs are part of delivering the Group's growth strategy. Consequently, this expense is not viewed as a normal ongoing operating cost to the Group.
Separation costs	**(8)**	(8)	Costs incurred directly relating to the Demerger.	Specific costs relating to the Demerger are historic and not indicative of the Group's current underlying performance.
Gain on disposal of VocaLink	**–**	20	A one-off gain recognised on the disposal of the Group's VocaLink share.	Losses or gains from one-off or infrequent transactions are not indicative of the Group's current underlying performance.
Gain on defined benefit pension scheme reforms	**–**	88	A one-off gain on the closure of the defined benefit pension scheme to future accrual for the majority of members.	Losses or gains from one-off or infrequent transactions are not indicative of the Group's current underlying performance.

Glossary

Term	Definition
Additional Tier 1 securities **(AT1)**	Securities that are considered additional Tier 1 capital in the context of CRD IV.
arrears	A customer is in arrears when they fail to adhere to their contractual payment obligations resulting in an outstanding loan that is unpaid or overdue.
average assets	Represents the average of assets over the year adjusted for any disposed operations.
B	The Group's digital application suite, offering Retail customers money management capabilities across Web, Android and Apple platforms.
Bank	Clydesdale Bank PLC.
Basel II	The capital adequacy framework issued by the BCBS in June 2006 defining how firms should calculate their regulatory capital requirements.
Basel III	Reforms issued by the Basel Committee on Banking Supervision (BCBS) in December 2010 to strengthen global capital and liquidity rules with the goal of promoting a more resilient banking sector. In Europe the new requirements were implemented by CRD IV, on a phased basis from 1 January 2014 with full implementation by 1 January 2019.
basis points **(bps)**	One hundredth of a percent (0.01%); meaning that 100 basis points is equal to 1%. This term is commonly used in describing interest rate movements.
Board	Refers to the CYBG PLC Board or the Clydesdale Bank PLC Board as appropriate.
Capped Indemnity	The indemnity from NAB in favour of CYBG in respect of certain qualifying conduct costs incurred by the Group, which is capped at the Capped Indemnity Amount, subject to the Loss Sharing Arrangement, under the terms of the Conduct Indemnity Deed.
Capped Indemnity Amount	An amount equal to £1.58bn less any Pre Covered provision amount.
carrying value (also referred to as carrying amount)	The value of an asset or a liability in the balance sheet based on either amortised cost or fair value principles.
CMA9	The nine largest banks and building societies in Great Britain and Northern Ireland, based on the volume of personal and business current accounts, who are mandated to deliver Open Banking. The nine banks are AIB, Bank of Ireland, Barclays, HSBC, Lloyds, Nationwide, Danske Bank, RBS and Santander.
collateral	The assets of a borrower that are used as security against a loan facility.
collective impairment provision	Impairment assessment on a collective basis for homogeneous groups of loans that are not considered individually significant and to cover losses which have been incurred but have not yet been identified on loans subject to individual assessment.
Combined Group	CYBG and its controlled entities following the acquisition of Virgin Money.
commercial paper	An unsecured promissory note issued to finance short-term credit requirements. These instruments have a specified maturity date and stipulate the face amount to be paid to the investor on that date.
Common Equity Tier 1 capital **(CET1)**	The highest quality form of regulatory capital that comprises total shareholders' equity and related non-controlling interests, less goodwill and intangible assets and certain other regulatory adjustments.
Company/CYBG	CYBG PLC.
Conduct Indemnity Deed	The deed between NAB and CYBG setting out the terms of: – the Capped Indemnity; and – certain arrangements for the treatment and management of Relevant Conduct Matters.
conduct risk	The risk of treating customers unfairly and/or delivering inappropriate outcomes resulting in customer detriment, regulatory fines, compensation, redress costs and reputational damage.
counterparty	The other party that participates in a financial transaction, with every transaction requiring a counterparty in order for the transaction to complete.
covered bonds	A corporate bond with primary recourse to the institution and secondary recourse to a pool of assets that act as security for the bonds on issuer default. Covered bonds remain on the issuer's balance sheet and are a source of term funding for the Group.

Additional information

Glossary

Term	Definition
CRD IV	European legislation to implement Basel III. It replaces earlier European capital requirements directives with a revised package consisting of a new Capital Requirements Directive and a new Capital Requirements Regulation. CRD IV sets out capital and liquidity requirements for European banks and harmonises the European framework for bank supervision. See also 'Basel III'.
credit risk adjustment/credit valuation adjustment	An adjustment to the valuation of financial instruments held at fair value to reflect the creditworthiness of the counterparty.
customer deposits	Money deposited by individuals and corporate entities that are not credit institutions, and can be either interest bearing, non-interest bearing or term deposits.
CYBI	CYB Investments Limited
default	A customer is in default when either they are more than 90 DPD on a credit obligation to the Group, or are considered unlikely to pay their credit obligations in full without recourse to actions such as realisation of security (if held).
delinquency	See 'arrears'.
Demerger	The demerger of the Group from NAB pursuant to which all of the issued share capital of CYBI was transferred to CYBG by NAB in consideration for the issue and transfer of CYBG shares to NAB in part for the benefit of NAB (which NAB subsequently sold pursuant to the IPO) and in part for the benefit of NAB shareholders under a scheme of arrangement under part 5.1 of the Australian Corporations Act.
Demerger date	8 February 2016.
derivative	A financial instrument that is a contract or agreement whose value is related to the value of an underlying instrument, reference rate or index.
earnings at risk **(EaR)**	A measure of the quantity by which net interest income might change in the event of an adverse change in interest rates.
effective interest rate	The carrying value of certain financial instruments which amortises the relevant fees over the expected life of the instrument.
encumbered assets	Assets that have been pledged as security, collateral or legally 'ring fenced' in some other way which prevents those assets being transferred, pledged, sold or otherwise disposed.
exposure	A claim, contingent claim or position which carries a risk of financial loss.
fair value	The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions.
Financial Ombudsman Service **(FOS)**	An independent body set up by the UK Parliament to resolve individual complaints between financial businesses and their customers.
Financial Services Compensation Scheme **(FSCS)**	The UK's compensation fund of last resort for customers of authorised financial services firms and is funded by the financial services industry. The FSCS may pay compensation if a firm is unable, or likely to be unable, to pay claims against it. This is usually because it has stopped trading or has been declared in default.
forbearance	The term generally applied to the facilities provided or changes to facilities provided to assist borrowers, both retail and SME, who are experiencing, or are about to experience, a period of financial stress.
funding risk	A form of liquidity risk arising when the liquidity needed to fund illiquid asset positions cannot be obtained at the expected terms and when required.
Group	CYBG and its controlled entities.
hedge ineffectiveness	Represents the extent to which the income statement is impacted by changes in fair value or cash flows of hedging instruments not being fully offset by changes in fair value or cash flows of hedged items.
iB	The Group's IT digital platform, built on an open architecture framework providing integration and connectivity for our customer systems, applications and technology partners.
IFRS 9	The new financial instrument accounting standard which is applicable for accounting periods beginning on or after 1 January 2018, which the Group will adopt from 1 October 2018.

Term	Definition
impaired loans	Loans in arrears with insufficient security to cover principal and arrears of interest revenue or where there is sufficient doubt about the ultimate collectability of principal and interest.
impairment allowances	A provision held on the balance sheet to recognise that a loan is impaired. This can be calculated at either the individual or collective level.
impairment losses	Where an asset's recoverable amount is less than its carrying value and the difference is recognised in the income statement with the carrying value of the asset reduced by creating an impairment allowance. This can be assessed at either the individual or collective level.
interest rate hedging products **(IRHP)**	This incorporates: (i) standalone hedging products identified in the Financial Services Authority (FSA) 2012 notice; (ii) the voluntary inclusion of certain of the Group's more complex tailored business loan (TBL) products; and (iii) the Group's secondary review of all fixed-rate tailored business loans (FRTBLs) complaints which were not in scope for the FSA notice.
Internal Capital Adequacy Assessment Process **(ICAAP)**	The Group's assessment of the levels of capital that it needs to hold through an examination of its risk profile from regulatory and economic capital viewpoints.
Internal Liquidity Adequacy Assessment Process **(ILAAP)**	The Group's assessment and management of balance sheet risks relating to funding and liquidity.
Internal Ratings-Based approach **(IRB)**	A method of calculating credit risk capital requirements using internal, rather than supervisory, estimates of risk parameters.
investment grade	The highest possible range of credit ratings, from 'AAA' to 'BBB', as measured by external credit rating agencies.
jaws	The net difference between movements in total income and underlying costs for the period expressed as a percentage.
Level 1 fair value measurements	Financial instruments whose fair value is derived from unadjusted quoted prices for identical instruments in active markets.
Level 2 fair value measurements	Financial instruments whose fair value is derived from quoted prices for similar instruments in active markets and financial instruments valued using models where all significant inputs are observable.
Level 3 fair value measurements	Financial instruments whose fair value is derived from valuation techniques where one or more significant inputs are unobservable.
Listing Rules	Regulations applicable to any company listed on a United Kingdom stock exchange, subject to the oversight of the UK Listing Authority (UKLA). The Listing Rules set out mandatory standards for any company wishing to list its shares or securities for sale to the public.
loan to value ratio **(LTV)**	A ratio that expresses the amount of a loan as a percentage of the value of the property on which it is secured.
Loss Share	The percentage of a provision raised or an increase in a provision which CYBG will be responsible for under the Conduct Indemnity Deed. Fixed at 9.7% at the Demerger date.
Loss Sharing Arrangement	The arrangement relating to the Capped Indemnity pursuant to which CYBG will be responsible for the Loss Share.
medium-term notes	Debt instruments issued by corporates, including financial institutions, across a range of maturities.
minimum requirement for own funds and eligible liabilities **(MREL)**	MREL is a minimum requirement for institutions to maintain equity and eligible debt liabilities, to help ensure that when an institution fails the resolution authority can use these financial resources to absorb losses and recapitalise the continuing business. The BoE set out its approach to setting banks' MREL in November 2016.
net interest income	The amount of interest received or receivable on assets, net of interest paid or payable on liabilities.
net promoter score **(NPS)**	This is an externally collated customer loyalty metric that measures loyalty between a provider, who in this context is the Group, and a consumer.
operational risk	The risk of loss resulting from inadequate or failed internal processes, people strategies and systems or from external events.

Additional information

Glossary

Term	Definition
Overall Liquidity Adequacy Rule **(OLAR)**	An FCA and PRA rule that firms must at all times maintain liquidity resources which are adequate both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due. This is included in the Group's risk appetite and subject to approval by the Board as part of the ILAAP.
pension risk	The risk that, at any point in time, the available assets to meet pension liabilities are at a value below current and future scheme obligations.
PPI redress	Includes PPI customer redress and all associated costs excluding fines.
Pre Covered provision amount	The amount of any provision(s) relating to Relevant Conduct Matters raised or increased by the Group between 31 March 2015 and the demerger date in respect of which NAB has provided specific support at any time after 31 March 2015 but before the Demerger date. This was £465m at the Demerger date.
probability of default **(PD)**	The probability that a customer will default (usually within a one-year time horizon); although the time horizon will change on 1 October 2018 in line with IFRS 9 requirements.
regulatory capital	The capital which the Group holds, determined in accordance with rules established by the PRA.
Relevant Conduct Matters	The legacy conduct issues covered by the Capped Indemnity, including certain conduct issues relating to PPI, standalone IRHP, voluntary scope TBLs and FRTBLs and other conduct matters in the period prior to the Demerger date whether or not known at the Demerger date.
residential mortgage-backed securities **(RMBS)**	Securities that represent interests in groups or pools of underlying mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and principal).
retail lending	Lending to individuals rather than institutions. This includes both secured and unsecured lending such as personal loans, residential and BTL mortgages, overdrafts and credit card balances.
Ring-fencing	A new regime of rules which require banks to change the way that they are structured by separating retail banking services from investment and international banking. This is to ensure the economy and taxpayers are protected in the event of any future financial crises.
risk appetite	The level and types of risk the Group is willing to assume within the boundaries of its risk capacity to achieve its strategic objectives.
risk weighted assets **(RWA)**	On and off balance sheet assets of the Group are allocated a risk weighting based on the amount of capital required to support the asset.
sale and repurchase agreement ('repo')	A short-term funding agreement that allows a borrower to create a collateralised loan by selling a financial asset to a lender. As part of the agreement, the borrower commits to repurchase the security at a date in the future repaying the proceeds of the loan. For the counterparty (buying the security and agreeing to sell in the future) it is a reverse repurchase agreement or a reverse repo.
Scheme	The Group's defined benefit pension scheme, the Yorkshire and Clydesdale Bank Pension Scheme.
secured lending	Lending in which the borrower pledges some asset (e.g. property) as collateral for the lending.
securitisation	The practice of pooling similar types of contractual debt and packaging the cash flows from the financial asset into securities that can be sold to institutional investors in debt capital markets. It provides the Group with a source of secured funding than can achieve a reduction in funding costs by offering typically 'AAA' rated securities secured by the underlying financial asset.
SME lending	Lending to non-retail customers, including overdrafts, asset and lease financing, term lending, bill acceptances, foreign currency loans, international and trade finance, securitisation and specialised finance.
specific impairment provision	A specific provision relates to a specific loan, and represents the estimated shortfall between the carrying value of the asset and the estimated future cash flows, including the estimated realisable value of securities after meeting securities realisation costs.

Term	Definition
standardised approach	In relation to credit risk, a method for calculating credit risk capital requirements using External Credit Assessment Institutions (ECAI) ratings and supervisory risk weights. In relation to operational risk, a method of calculating the operational capital requirement by the application of a supervisory defined percentage charge to the gross income of eight specified business lines.
stress testing	The term used to describe techniques where plausible events are considered as vulnerabilities to ascertain how this will impact the own funds or liquidity which a bank holds.
structured entities **(SE)**	An entity created to accomplish a narrow well-defined objective (e.g. securitisation of financial assets). An SE may take the form of a corporation, trust, partnership or unincorporated entity. SEs are often created with legal arrangements that impose strict limits on the activities of the SE. May also be referred to as an SPV.
subordinated debt	Liabilities which rank after the claims of other creditors of the issuer in the event of insolvency or liquidation.
Term Funding Scheme **(TFS)**	Launched in 2016 by the BoE to allow banks and building societies to borrow from the BoE at rates close to base rate. This is designed to increase lending to businesses by lowering interest rates and increasing access to credit.
Tier 1 capital	A measure of a bank's financial strength defined by CRD IV. It captures Common Equity Tier 1 capital plus other Tier 1 securities in issue, subject to deductions.
Tier 2 capital	A component of regulatory capital, including qualifying subordinated debt, eligible collective impairment allowances and other Tier 2 securities as defined by CRD IV.
total net capital absorbed	The amount of capital generated by the business in basis points over a given period, after non underlying items are included.
unaudited/unverified	Financial information that has not been subject to validation by the Group's external auditor.
underlying capital generation	The amount of capital generated by the business in basis points over a given period, before non-underlying items are included.
unsecured lending	Lending in which the borrower pledges no assets as collateral for the lending (such as credit cards and current account overdrafts).
value at risk **(VaR)**	A measure of the loss that could occur on risk positions as a result of adverse movements in market risk factors (e.g. rates, prices, volatilities) over a specified time horizon and to a given level of confidence.
Virgin Money	Virgin Money Holdings (UK) plc

Additional information

Abbreviations

ALCO	Asset and Liability Committee
ASX	Australian Securities Exchange
AT1	Additional Tier 1
BCAs	Business current accounts
BCBS	Basel Committee on Banking Supervision
BoE	Bank of England
bps	Basis points
BTL	Buy-to-let mortgages
CAGR	Compound Annual Growth Rate
CCB	Capital Conservation Buffer
CCyB	Countercyclical Capital Buffer
CET1	Common Equity Tier 1 Capital
CIR	Cost to income ratio
CMA	Competition and Markets Authority
CPI	Consumer Prices Index
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
DEP	Deferred Equity Plan
DPD	Days past due
DTR	Disclosure and Transparency Rules
EaR	Earnings at risk
EBA	European Banking Authority
eCRS	electronic Customer Rating System
EPS	Earnings per share
FCA	Financial Conduct Authority.
FPC	Financial Policy Committee
FRC	Financial Reporting Council
FSCS	Financial Services Compensation Scheme
FTE	Full time equivalent
GHG	Greenhouse Gases
HMRC	Her Majesty's Revenue and Customs
IAS	International Accounting Standard
IASB	International Accounting Standards Board
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standard
ILAAP	Internal Liquidity Adequacy Assessment Process
IPO	Initial Public Offering
IRB	Internal ratings-based
IRHP	Interest rate hedging products
IRRBB	Interest rate risk in the banking book
ISDA	International Swaps and Derivatives Association
LCR	Liquidity coverage ratio
LDR	Loan to deposit ratio
LGD	Loss Given Default
LIBOR	London Interbank Offered Rate
LSE	London Stock Exchange
LTIP	Long-term incentive plan
LTV	Loan to value ratio
MREL	Minimum Requirement for Own Funds and Eligible Liabilities
MRT	Material Risk Takers
NAB	National Australia Bank Limited
NIM	Net interest margin
NPS	Net promoter score
NSFR	Net stable funding ratio
OLAR	Overall liquidity adequacy rule
PBT	Profit before tax
PCA	Personal current accounts
PD	Probability of Default
PILON	Payment in lieu of notice
PPI	Payment protection insurance
PRA	Prudential Regulation Authority
RAS	Risk Appetite Statement
RMBS	Residential mortgage-backed securities
RMF	Risk Management Framework
RoTE	Return on Tangible Equity
RPI	Retail Price Index
RWA	Risk weighted assets
SIP	Share Incentive Plan
SME	Small or medium sized enterprises
SRB	Systemic Risk Buffer
TCC	Transactional Credit Committee
TFS	Term Funding Scheme
TNAV	Tangible net asset value
TSA	Transitional Services Agreement
TSR	Total Shareholder Return
VaR	Value at risk

Country by country reporting

The Capital Requirements (Country-by-Country Reporting) Regulations 2013 came into effect on 1 January 2014 and place certain reporting obligations on financial institutions that are within the scope of the European Union's Capital Requirements Directive (CRD IV). The purpose of the Regulations is to provide clarity on the source of the Group's income and the locations of its operations.

The vast majority of entities that are consolidated within the Group's financial statements are UK registered entities. The activities of the Group are described in the Strategic report.

	2018 UK
Average FTE employees (number)	**5,728**
Total operating income (£m)	**1,007**
Loss before tax (£m)	**(164)**
Corporation tax paid (£m)	**–**
Public subsidies received (£m)	**–**

The only other non-UK registered entity of the Group is a Trustee company that is part of the Group's securitisation vehicles (Lanark and Lannraig). Lannraig Trustees Limited is registered in Jersey. This entity plays a part in the overall securitisation process by having the beneficial interest in certain mortgage assets assigned to it. This entity has no assets or liabilities recognised in its financial statements with the securitisation activity taking place in other UK registered entities of the structures. This entity does not undertake any external economic activity and has no employees. The results of this entity as well as those of the entire Lanark and Lannraig securitisation structures are consolidated in the financial statements of the Group.

Additional information

Shareholder information

Annual general meeting (AGM)

The AGM of the Company will be held at 10.00am (Melbourne time – AEDT) on Wednesday 30 January 2019 at the Melbourne Convention and Exhibition Centre, 1 Convention Centre Place, South Wharf, Melbourne, Victoria, 2006, Australia. The Notice of AGM is published on the CYBG PLC website www.cybg.com

Shareholder enquiries

The Company's share register is maintained by the Company's Registrar, Computershare. Shareholders with queries relating to their shareholding should contact Computershare directly using one of the methods below:

Registrar
Computershare UK
Computershare Investor Services PLC
The Pavilions
Bridgwater Road
Bristol
United Kingdom BS99 6ZZ

Tel within UK – 0370 707 1172
Tel outside UK – +44 370 707 1172
Email: www.investorcentre.co.uk/contactus
Web: www.investorcentre.co.uk

Computershare Australia
Computershare Investor Services Pty Limited
Yarra Falls
452 Johnston Street
Abbotsford VIC 3067
Australia

Tel within Australia – 1800764308
Tel outside Australia – 03 9415 4142
Email: www.investorcentre.com/contact
Web: www.investorcentre.com/au

Duplicate shareholder accounts
If you receive more than one copy of Company mailings this may indicate that more than one account is held in your name on the register. This happens when the registration details of separate transactions differ slightly. If you believe more than one account exists in your name you may contact the Company's Registrar, Computershare, to request that the accounts are combined. There is no charge for this service.

Electronic communications
CYBG PLC uses its website (www.cybg.com) as its primary means of communication with its shareholders provided that the shareholder has agreed or is deemed to have agreed that communications may be sent or supplied in that manner. Electronic communications allow shareholders to access information instantly as well as helping the Company reduce its costs and its impact on the environment. Shareholders who have consented or are deemed to have consented to electronic communications can revoke their consent at any time by contacting the Company's Registrar, Computershare.

Shareholders can sign up for electronic communications online via the following links:

Holders of shares on the London Stock Exchange:
www.investorcentre.co.uk/ecomms

Holders of CDIs on the Australian Securities Exchange:
www.investorcentre.com/au

Corporate website
Information on the Company is available at the CYBG PLC website (www.cybg.com) including:

- financial information – annual and half-yearly reports as well as trading updates;
- share price information – current trading details and historical charts;
- shareholder information – investor presentations and share register profile; and
- news releases – current and historical.

Unsolicited telephone calls and communication
Shareholders are advised to be wary of any unsolicited advice, offers to buy shares at a discount, or offers of free reports about the Company. These are typically from overseas based 'brokers' who target shareholders, offering to sell them what often turns out to be worthless or high risk shares. These operations are commonly known as 'boiler rooms' and the 'brokers' can be very persistent and extremely persuasive.

Shareholders are advised to deal with only financial services firms that are authorised by the FCA. You can check a firm is properly authorised by the FCA before getting involved by visiting www.fca.org.uk/register. If you do deal with an unauthorised firm, you will not be eligible to receive payment under the Financial Services Compensation Scheme if anything goes wrong. For more detailed information on how you can protect yourself from an investment scam, or to report a scam, go to www.fca.org.uk/consumers/report-scam-unauthorised-firm

Shareholder interests as at 30 September 2018

By size of holding

Range	No. of shareholders	%	No. of shares	%
1–1,000	145,951	82.45	48,942,378	5.52
1,001–5000	26,775	15.12	53,165,765	6.00
5,001–10,000	2,621	1.48	18,357,619	2.07
10,001–100,000	1,445	0.82	32,738,107	3.70
100,001–999,999,999	226	0.13	732,876,090	82.71
Totals	177,018	100.00	886,079,959	100.00

Indicative financial calendar for 2019

Q1 Trading update	23 January 2019
Annual General Meeting	30 January 2019
Interim results announcement	May 2019
Q3 Trading update	August 2019
Full year results announcement	November 2019

Forward-looking statements

The information in this document may include forward looking statements, which are based on assumptions, expectations, valuations, targets, estimates, forecasts and projections about future events. These can be identified by the use of words such as 'expects', 'aims', 'targets', 'seeks', 'anticipates', 'plans', 'intends', 'prospects', 'outlooks', 'projects', 'forecasts', 'believes', 'estimates', 'potential', 'possible', and similar words or phrases. These forward looking statements, as well as those included in any other material discussed at any presentation, are subject to risks, uncertainties and assumptions about the Group and its securities, investments and the environment in which it operates, including, among other things, the development of its business and strategy, any acquisitions, combinations, disposals or other corporate activity undertaken by the Group (including but not limited to the acquisition of Virgin Money Holdings (UK) plc), trends in its operating industry, changes to customer behaviours and covenant, macroeconomic and/or geopolitical factors, changes to its board and/or employee composition, exposures to terrorist activity, IT system failures, cyber-crime, fraud and pension scheme liabilities, changes to law and/or the policies and practices of the BoE, the FCA and/or other regulatory and governmental bodies, inflation, deflation, interest rates, exchange rates, changes in the liquidity, capital, funding and/or asset position and/or credit ratings of the Group, future capital expenditures and acquisitions, the repercussions of the UK's referendum vote to leave the European Union (EU), the UK's exit from the EU (including any change to the UK's currency), Eurozone instability, and any referendum on Scottish independence.

In light of these risks, uncertainties and assumptions, the events in the forward looking statements may not occur. Forward looking statements involve inherent risks and uncertainties. Other events not taken into account may occur and may significantly affect the analysis of the forward looking statements. No member of the Group or their respective Directors, officers, employees, agents, advisers or affiliates gives any assurance that any such projections or estimates will be realised or that actual returns or other results will not be materially lower than those set out in this document and/or discussed at any presentation. All forward looking statements should be viewed as hypothetical. No representation or warranty is made that any forward looking statement will come to pass. No member of the Group or their respective Directors, officers, employees, agents, advisers or affiliates undertakes any obligation to update or revise any such forward looking statement following the publication of this document nor accepts any responsibility, liability or duty of care whatsoever for (whether in contract, tort or otherwise) or makes any representation or warranty, express or implied, as to the truth, fullness, fairness, merchantability, accuracy, sufficiency or completeness of, the information in this document.

The information, statements and opinions contained in this document do not constitute or form part of, and should not be construed as, any public offer under any applicable legislation or an offer to sell or solicitation of any offer to buy any securities or financial instruments or any advice or recommendation with respect to such securities or other financial instruments.

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CYBG PLC
Registered number 09595911
(England and Wales)

ARBN 609 948 281
(Australia)

www.cybg.com

Head Office:
30 St. Vincent Place
Glasgow
G1 2HL

London Office:
Floor 15, The Leadenhall Building
122 Leadenhall Street
London
EC3V 4AB

Registered Office:
20 Merrion Way
Leeds, West Yorkshire
LS2 8NZ