Company Number: R0000568

NORTHERN BANK LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED
31 DECEMBER 2017

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NORTHERN BANK LIMITED
Officers and Professional Advisers
For the year ended 31 December 2017

Directors	**Executive:**	Kevin Kingston	Chief Executive Officer
		Stephen Matchett	Chief Financial Officer
		Vicky Davies	Managing Director, Strategy and Corporate Development
	Non-executive:	Lars Stensgaard Mørch~Ω	Chairman
		Michael Black*∞	
		Jim Ditmore~	
		Gerald Gregory*∞Ω	
		Margaret Lesley Jones*∞Ω	
		Paul Rooney∞	

* Member of the Board Audit Committee
~ Member of the Executive Board of the Parent
∞ Member of the Board Risk Committee
Ω Member of the Board Remuneration Committee

Executive Committee	Kevin Kingston	Chief Executive Officer
	Søren Andreasen	Chief Digital Officer (appointed 21 August 2017)
	Paul Black	General Manager of Regulatory Change
	Richard Caldwell	Managing Director, Personal Banking and Small Business
	Liam Curran	Acting Head of Operations (appointed 13 November 2017)
	Vicky Davies	Managing Director, Strategy and Corporate Development
	Stephen Matchett	Chief Financial Officer
	Shaun McAnee	Managing Director, Corporate and Business Banking
	Nigel McMahon	Chief Risk Officer
	Tim Turner	Head of Business Development
	Caroline Van Der Feltz	HR Director
Company Secretary	Fiona Sturgess	(appointed 1 October 2017)
	Lesley Bourke	(resigned 30 September 2017)

Registered Office
Donegall Square West
Belfast BT1 6JS

Bankers
Danske Bank A/S

Auditor
Deloitte (NI) Limited
Chartered Accountants and Statutory Auditor
Bedford Street, Belfast
United Kingdom

The Directors of Northern Bank Limited (the 'Bank') present their Strategic Report for the year ended 31 December 2017.

The Strategic Report is a statutory requirement under the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013 and is intended to be fair and balanced, and to provide information that enables the Directors to be satisfied that they have complied with s172 of the Companies Act 2006 (which sets out the Directors' duty to promote the success of the company). The Bank's 2017 Financial Statements have been prepared under International Financial Reporting Standards (IFRS).

Business review

Principal activities

The Bank is authorised under the Financial Services and Markets Act 2000 and is regulated by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA).

The principal activity of the Bank, operating under the Danske Bank brand, is the provision of a comprehensive range of banking, financial and related services to households and businesses primarily in Northern Ireland.

Review of business

Key performance measures	**2017**	2016
Profit before tax - £m	**147.5**	117.0
Profit before loan impairment credits and tax as per the Income Statement - £m	**118.3**	91.0
Loan to deposit ratio - %	**77%**	75%
Cost/income ratio - %	**49%**	60%
Net interest margin - %	**2.3%**	2.4%

Financial review

The Bank has reported a profit before loan impairment credit of £118.3m (2016: £91.0m). This result was achieved despite the ongoing low interest rate environment. The Bank profit attributable to the shareholders for the year ended 31 December 2017 amounted to £115.2m, an increase of £73.4m on the previous year. The key drivers of this increase were the higher net interest income and impairment credits together with lower costs, and in particular, the negative past service cost arising from the decision to cease defined benefit accrual and a reduced tax charge following the re-recognition, in part, of the deferred tax asset written down in 2016.

Net interest income increased by 1.4% to £162.7m (2016: £160.4m) primarily driven by the positive impact of an increase in lending (6%) and deposit (3%) volumes. Net interest margin fell from 2.4% in 2016 to 2.3% in 2017 and reflects the impact of the lower average Bank of England base rate in 2017 relative to 2016.

The loan-to-deposit ratio increased marginally to 77% (2016: 75%). We remain well positioned to meet any increased demand for credit.

Non interest income increased by £0.2m or 0.3% to £70.2m. Both 2016 and 2017 included exceptional income relating to the sale of the Bank's interest in VISA Europe.(2017: £5.3m 2016: £3.5m). Additionally, 2017 includes a profit on sale of the Bank's wealth business of £4.5m.

Operating expenses decreased by £24.7m or 17.8% to £114.6m. The key driver was a negative past service cost of £40.4m arising from changes to our staff pension arrangements. This was partially offset by investment and restructuring costs relating to branches, digital technology and improved customer solutions, alongside additional PPI and consultancy costs.

The Bank's effective tax rate for the year ended 31 December 2017 was 18.9% (2016: 60.3%). The key driver of the change in effective tax rates relates to the re-recognition in 2017 and the derecognition in 2016 of the deferred tax asset with respect to tax losses. By excluding this, the effective tax rate for the year ended 31 December 2017 would have been 25.8% (2016: 31.4%)

The cost/income ratio fell from 60% to 49%. This was primarily due to the non recurring impact of the negative past service cost arising from the decision to cease defined benefit accrual.

The continued improvement in collateral values and improved trading performance of Business customers were the primary drivers of the impairment credit in 2017 of £29.2m (2016: £25.9m).

The key changes to the Bank's balance sheet have been outlined below.

Customer lending and deposits grew by £328.1m (+6%) and £215.8m (+3%) respectively in 2017. The net increase in lending reflected growth in both personal and business lending. The Bank increased its investment in debt securities by £190.5m. Cash and balances at central bank decreased by £199.8m (-4%) primarily as a result of lending growth exceeding deposit growth and the increased investment in debt securities.

Review of business (continued)

Financial review (continued)

A property revaluation at 30 June 2017 was undertaken by external valuers and this increased the carrying value of properties by 4%. The previous property valuation was at 30 June 2016. During 2017 the Bank disposed of no properties and has one property held for sale at 31 December 2017. (2016: one property).

The funded status of the defined benefit pension scheme was an asset of £154.3m at 31 December 2017 (2016: £39.9m). The scheme surplus increased during the year primarily due to the impact of the decision to cease future benefit accrual from 1 October 2018 (including a one-off employer contribution to the Scheme of £20m); supported by an increase in the value of the pension assets and partly offset by an increase in the value of the pension liabilities as a result of the fall in the discount rate.

The Bank remains well capitalised and this is reflected in its solvency ratio of 18.3% (2016: 19.1%). During the year a dividend of £Nil (2016:£200m) was paid to the Bank's ultimate parent undertaking Danske Bank A/S.

We continue to report a strong liquidity position with a pool of liquid assets in excess of £1.9 billion at 31 December 2017 (2016: £2.1 billion).

General review

In 2017, we continued to focus on achieving our vision to be recognised as the best bank in Northern Ireland for customers, employees, stakeholders and society.

The external environment remained challenging, with slow growth in the economy. While the first Bank of England interest rate increase in ten years was announced in November, the continued low rate environment remains a challenge for all UK banks.

Uncertainty relating to Brexit had an impact on demand for lending in 2017 and economic uncertainty is likely to increase further as the March 2019 departure date approaches.

Personal Banking and Small Business

In Personal Banking, we made notable progress towards our ambition of being the best bank for customers, the result of a sustained focus and investment in this area and a strategy based on combining digital development with personal interaction.

2017 was another strong year for our mortgage business, with new mortgage approvals up 28% year on year and our market share of new business now having more than doubled since 2015.

We invested in developing a new digital online application system for intermediaries, giving mortgage brokers online access to the Bank’s mortgage products and enabling them to get real time decisions in principle. We also expanded our own mortgage consultant team, making this service more readily available.

In response to continuing changes in customer behaviours, we closed two branches in 2017. We also invested through the significant refurbishment of five of our flagship branches, with more planned for development in 2018. Alongside this investment in our physical infrastructure, we have invested in creating a team of 22 Customer Experience Advisors, whose role is to welcome and provide assistance to the wide range of customers who visit our branches.

Following feedback from our small business customers, we relocated Small Business Advisers back into branches, making our people more accessible and closer to customers. These changes have already made a tangible impact, with 37 new small business relationships being established every week.

Corporate and Business Banking

In Corporate and Business Banking, we retained our number one position in customer satisfaction. Corporate lending volumes were up 3% on 2016, and we retained a market leading position in this segment.

Enhancements to our customer proposition have included the introduction of a new invoice finance system.

In 2017, we continued our series of Danske Advantage thought-leadership events across Northern Ireland, bringing together business leaders and experts on a range of topics, from Brexit to cyber security. Over 1,000 customers, prospective customers and stakeholders attended these events.

Digital

Digital innovation continued at pace. We saw further adoption of our digital channels, with more than 4 million digital logons per month and an 19% increase in digital transactions year-on-year. We are leveraging the capabilities and expertise of our parent to develop a wide range of digital offerings for the Northern Ireland market.

New services in 2017 included the introduction of Apple Pay and Fitbit Pay for our customers. We also continued to improve our online sales proposition and launched a new mobile-optimised website focused on enhancing user experience.

Our work to progress the digital agenda in Northern Ireland was further strengthened by the appointment of a Chief Digital Officer, who joined us from within the Danske Bank Group, and the creation of a specialist digital team in the second half of the year.

Review of business (continued)

General review (continued)

Organisational Change

In 2017, organisational change included the disposal of our wealth business, and the creation of a replacement customer offering through partnerships with two external wealth providers. We also leased one of the floors of our head office to professional services firm, Grant Thornton. In addition, we re-assessed our defined benefit pension arrangement, which will now close to future accrual with effect from 1 October 2018. This relates to employees who joined the Bank before 31 December 2003. From October 2018, all staff will avail of a competitive defined contribution pension arrangement.

Responsible business

We remain committed to supporting financial stability by running a profitable business, conducting our business in a responsible manner and making our time and expertise available for the benefit of society. We believe we have a responsibility to help build financial confidence in the next generation and to develop innovative products that are accessible, easy to use and secure.

In 2017, we selected Action Mental Health as our new charity partner. The partnership delivers on four strategic areas - fundraising, volunteering, employee wellbeing and education and awareness. It has been a successful partnership, with staff raising over £70,000 in the first year and delivering over 270 volunteering hours. This partnership will continue in 2018.

We also added two new partners to our Danske "Time to Give" volunteering programme - Young Enterprise and Ulster Wildlife. Through this programme, we have encouraged our staff to volunteer 778 hours in local communities across Northern Ireland, both individually and in teams. Staff have helped educate over 4,600 children and young people through our SMART financial confidence programme, giving an additional 150 hours of their time.

We continue to work hard to reduce our impact on the environment, for example, we have reduced our electricity consumption by 29% since 2015. Danske Bank has achieved Gold in the Arena Network NI environmental benchmarking surveys for the past three years - the highest ranking of any financial services company in Northern Ireland.

Future development

We expect to be operating in an environment of historically low interest rates for a prolonged period.

It remains to be seen how the EU Referendum result will affect confidence levels and economic conditions in 2018. Our planning takes into account a range of possible scenarios and we are committed to supporting our customers on this journey.

Digital transformation will only accelerate further in 2018, driven by both customer expectations, competition and the advent of Open Banking in the UK.

Principal risks and uncertainties

Economic overview

UK GDP grew by 0.4% in the last quarter of 2017, down from 0.5% in the third quarter of the year. In annual terms, the UK economy grew by 1.7% in 2017, lower than the 1.9% observed in 2016. Given the squeeze on consumers, household spending in the UK grew by 1.8% in 2017 – the slowest rate of growth since 2012.

In its Northern Ireland Quarterly Sectoral Forecasts 2017 Q4 report, Danske Bank estimated that annual economic growth in Northern Ireland was 1.1% in 2017.

The CPI inflation rate in the UK fell slightly from 3.1% in November to 3% in December. After starting 2017 at a little under the Bank of England’s target of two per cent, inflation in the UK ended the year one percentage point above the target rate.

The Northern Ireland labour market data for October – December 2017 showed that, over the quarter, the employment rate increased while the unemployment rate and economic inactivity rate both fell. However, over the year, it was a much bleaker picture. The unemployment rate fell but so too the employment rate, and the economic inactivity rate increased sharply to 28.4%.

The annual change in house prices in Northern Ireland was 4.3% in the fourth quarter of 2017, higher than the 3.6% observed in 2017 Q3. The standardised house price in 2017 Q4 was £130,482. In annual average terms, house prices in Northern Ireland increased by 4.0% in 2017.

In 2018, economic growth in the UK and Northern Ireland is expected to remain subdued. Inflation is projected to fall gradually over the year, but it is likely to remain above the Bank of England’s two per cent target throughout 2018. Household spending power is expected to remain under pressure as increases in the rate of nominal wage growth are unlikely to be enough to push real wage growth well into positive territory. With Brexit-related uncertainty also likely to persist, some firms are still expected to postpone capital spending until the UK’s future trading relationship with the EU becomes clearer.

Principal risks and uncertainties (continued)

The UK vote to leave the EU ("Brexit")

The outcome of the EU referendum has created a period of uncertainty for the local Northern Ireland economy and the wider UK economic environment. While the specific plans for the UK to exit the EU remain under development and negotiation between the UK Government and EU representatives continues, the Bank has implemented a number of actions to assess and, where possible, mitigate the emerging risks.

Risk appetite

The Board's setting and review of the Bank's risk appetite is an ongoing process achieved via its approval of key risk frameworks, policies, documents (Internal Capital Adequacy Assessment Process, Individual Liquidity Adequacy Assessment Process etc.) and the ongoing monitoring of the Bank's performance. This provides context for the Board's subsequent review of the Corporate Plan and strategic activities within the Bank and the inherent risks therein. The primary risk areas identified as part of the Bank's ongoing risk assessment framework are:

Business risk (Outlook: Increasing)

Business risk is split into two distinct areas, strategic performance and reputational damage.

- Strategic performance
This is the risk associated with management decisions about the direction and implementation of strategy, including competitors, growth strategies, missed opportunities, planning, change management and re-engineering. This risk is continually measured via both first line monitoring and second line oversight of key agreed metrics. The uncertainty attaching to Brexit contributes to an outlook of increasing business risk.

- Reputational damage
This is the impact of actions/circumstances, via adverse publicity or diminished community standing, having a material impact on the reputation, market confidence and ultimate viability of the Bank. Contagion is the cross-country transmission of shocks or the general cross-country spill over effects. Reputational risk can be a consequence of other events and therefore the impact of reputational risk is considered as part of all the Bank's risk assessment activities and across all risk categories.

A clearly defined Corporate Plan, within the boundaries of the Board approved risk appetite, is prepared annually. This Corporate Plan is based on a balanced growth of lending and deposits with a stable funding profile that is appropriate for the asset mix.

Key performance indicators are clearly defined and are closely and regularly monitored. Overall the outlook is seen as increasing due to the competition in the banking arena from non traditional banks e.g. open banking, together with the significant level of regulatory change e.g. PSD and GDPR.

Operational risk (Outlook: Stable)

This is the risk of losses resulting from inadequate or failed internal processes, people and systems or from external events. The Bank seeks at all times to have optimal control of all types of operational risk but recognises that this is an inherent part of doing business and the Bank's objective generally is not to eliminate the risk, but rather to ensure that the risk is effectively managed at an acceptable level, in a cost effective manner. The key areas of focus in this area include:

- Clients, products and business practice.
  This is the risk of loss from an unintentional or negligent failure to meet a professional obligation to specific clients or from the nature or design of a product. The Bank, in common with the rest of the UK financial services industry, is faced with intense regulatory scrutiny and has implemented specific processes and controls to ensure that the Bank can effectively manage its regulatory obligations.

- Business disruption and/or technology systems failure.
  This is the risk that the Bank's business continuity policy and process is not fit for purpose. The Bank recognises the impact that service interruption or failure would have on its customers and business and therefore continually strives for excellence by monitoring incidents and reviewing and updating its contingency plans to ensure that customer detriment is kept to a minimum.

- Fraud.
  This is the risk of loss due to acts of a type intended to defraud, misappropriate property or circumvent the law by a third party or member of staff. The Bank employs detailed processes and controls to protect its customers and staff from the implications of the various types of fraud that could occur; these include fraud related to cards, cheques, internet banking, robbery, kidnapping, scams and loan fraud.

- Cyber security.
  This is the risk that the Bank and/or its customers become the victim of crimes perpetrated by the use of the internet. In financial services, these crimes include the use of malware designed to bring computer systems down, the use of spyware to gather information and the use of emails designed to trick recipients into revealing details related to personal or business finances to cybercriminals. This risk also includes distributed denial of service type attacks. Robust cyber security forms a significant and key component of the corporate IT strategy and the Bank continues to invest in improvements within the IT security area in order to increase resilience and controls towards cybercrime.

The Bank's strategic focus for operational risk is to see a significant year on year reduction in fraud losses as it continues to make enhancements to channel security controls and to ensure its security infrastructure remains comparable to peers in the UK market. Aside from this, no material additional risk is desired and this includes a clearly defined and conservative risk appetite for conduct risk and an aim to continue to improve IT system stability.

The Bank maintains adequate control and oversight of operational risk via reporting to the Operational Risk and Compliance Committee (ORCC) and the Information Technology Risk Committee (ITRC).

Principal risks and uncertainties (continued)

Regulatory risk (Outlook: Stable)

The Bank is continually scanning the regulatory horizon to ensure that any upcoming changes to the legal and regulatory environment or external events which could have a potential impact on the Bank are identified and appropriately dealt with. The Bank also reviews major developments in the market, local, national and international economies and undertakes forward looking assessment of the potential position and negative impacts on the business.

Credit risk (incorporating concentration risk and residual risk) (Outlook: Stable)

Credit risk is the potential that a borrower or counterparty is unable or unwilling to meet its obligations in accordance with agreed terms.

Concentration risk arises where the Bank is considered to be over exposed to a particular lending sector or region and materialises if the particular lending category (e.g. region, industry) performs badly.

Residual risk is the risk that credit risk mitigation techniques such as haircut parameter and credit models used by the Bank prove less effective than expected.

The management of credit risk within the Bank is achieved through both the traditional focuses on approval and monitoring of individual transactions together with analysis of the performance of the various credit risk portfolios. Portfolio monitoring covers such areas as industry or geographic concentrations and delinquency trends.

The Bank values long-term customer relationships. To maintain such relationships, the Bank must always be able to offer competitive financial solutions. It must also identify, at an early stage, any adverse developments in a customer's financial condition and through discussions with the customer, take the actions necessary to avoid future losses. Consequently, when extending and monitoring credits, the Bank makes detailed assessments of individual customers and their financial positions.

Clear Board approved risk appetite limits (including early warning indicators) are in place to monitor and control lending mix and portfolios within acceptable parameters.

- Credit granting process

The Bank has established processes for the granting of credit. These include:
- establishment of overall credit limits at the level of individual borrowers and counterparties, and groups of connected counterparties for both on-balance sheet and off-balance sheet exposures;
- satisfaction with repayment capacity and integrity of the counterparty;
- use of financial covenants;
- use of collateral;
- consideration of economic and industry conditions; and
- an objective customer rating assessment system.

At least on an annual basis, the Bank reviews all exposures to take account of new financial and other data. If the review identifies a need to adjust the risk assessment, the Bank will prepare suitable action plans.

This approach to credit risk is supported by documented policies and processes for the granting of credit within the Bank. The key elements of the process include:
- authorities for the approving of credit; and
- sample review of credit approvals to ensure adherence to policies and good credit practice.

The delegated authorities are aligned to the counterparty by the inclusion of customer ratings in the authority matrix. The system, based on probability of default of the counterparty, provides meaningful differentiation of credit risk, enabling greater focus in pricing for risk.

For consumer lending, credit scoring solutions are supported by the mandatory use of appropriate monitoring tools. These tools provide the essential continual review of data integrity, scorecard performance and decision strategies. Software to validate and verify input data is used to support data integrity and prevent fraudulent activity.

- Maintaining an appropriate credit administration, measurement and monitoring process

Effective credit administration operations and adequate control over back office procedures such as monitoring documentation, contractual requirements, legal covenants and collateral are recognised as being vitally important aspects of the end-to-end credit process. These responsibilities are assigned to various business units within the Bank together with centralised structures supporting the branch network and business bankers.

- Ensuring adequate controls over credit risk

Regular reports are submitted to the Bank's Credit Oversight Forum and the Board of Directors. Additionally, credit processes and policy compliance are subject to Internal Audit and targeted credit reviews of specific business units are undertaken within defined timescales and/or as considered appropriate.

Principal risks and uncertainties (continued)

Credit risk (incorporating concentration risk and residual risk) (Outlook: Stable) (continued)

- Ensuring adequate controls over credit risk (continued)

The Bank constantly monitors exposures to identify any signs of weakness in customer earnings or liquidity as early as possible. Credit facilities that are outside agreed arrangements are reported to the appropriate levels of authority for attention and monitoring of actions taken. Customers that show adverse operating trends or other signs of credit weakness are put on the "Watch List". Customer exposures that are on the "Watch List" are passed to a specialist internal unit of experienced credit officers, supported by external service providers where necessary. This unit also undertakes the collection and recovery processes.

When exposures are placed on the "Watch List", the Bank reduces the size of credits that can be extended without approval by the Board of Directors via the Danske Bank Group's credit function.

The Bank sets aside specific provisions, if required, for exposures placed on the "Watch List" after evaluating each of them individually.

- Management of the credit portfolio

To support the management of credit risk, the Bank has established a portfolio management system that sets limits on country, sector and industry concentrations. The segmentation of the credit portfolio enables the Bank to manage the composition and size of its portfolio in accordance with its risk policy.

Liquidity risk (Outlook: Stable)

Liquidity risk is the risk of losses because funding costs become excessive, lack of funding prevents the Bank from maintaining its business model, or lack of funding prevents the Bank from fulfilling its payment obligations.

The Bank conducts regular liquidity risk stress testing in accordance with its liquidity stress testing policy.

From 1 October 2015, following the introduction of the Liquidity Coverage Requirements under the Capital Requirements Directive (CRD) IV, the Bank is obliged to comply with the PRA's new liquidity regime, specifically under the PRA Rulebook PRA 2015/49 and Supervisory Statement SS24/15 which replaced the previous BIPRU regime. The Bank is obliged to produce an Individual Liquidity Adequacy Assessment Process (ILAAP) report at least annually. In addition, a Board approved liquidity framework document sets out the principles and standards of liquidity/funding management in the Bank. The objectives of the Bank's liquidity/funding management are to:
- ensure that the Bank is able to meet its obligations at all times;
- effectively and appropriately identify, measure, monitor and control the Bank's liquidity/funding risk within the approved liquidity/funding appetite;
- ensure an effective oversight of liquidity funding management;
- meet all internal liquidity/funding limits and regulatory requirements; and
- effectively manage the Bank in times of liquidity crisis.

Taking on liquidity risk is an integral part of the Bank's business strategy. By its nature, the Bank will, in most instances, lend funds for a much longer period than it will take deposits. The Bank must always have a liquidity position that enables it to meet its obligations and strategies, in particular regulatory obligations and business strategies. In the current market environment the Bank's liquidity risk appetite is conservative and the Bank maintains a strong liquidity and funding position.

The Bank must maintain at all times a liquidity buffer sufficient to cover the need for liquidity that may arise over a period of both normal and stressed conditions. The assets in the liquidity buffer must be freely available at all times and of a quality sufficient to ensure that they can provide liquidity to the Bank even in a stressed situation. The minimum size of the liquidity buffer is determined by internal stress test analyses and regulatory requirements. In particular, the Bank must comply with the PRA regulatory requirement to maintain a liquidity buffer based on Liquidity Coverage Ratio (LCR) requirements. The assets held within the liquidity buffer must comply with Articles 6-19 of the European Commission Delegated Regulation (EU) 2015/61 (Delegated Act), dated 10 October 2014, at all times.

The liquid asset portfolio is primarily comprised of cash at the Bank of England, UK Government Securities (Gilts) and listed securities. The Bank has evolved its approach to managing the liquid asset buffer (LAB) to more effectively utilise cash to reduce the cost of the LAB while still holding high quality, low risk liquid assets, by broadening the composition of the portfolio. The Bank has diversified by investing in a broader range of European covered bond issuances, non-domestic sovereign and multilateral development banks. Previously, liquidity was mainly held in Bank of England accounts, earning base rate, alongside holdings of UK Sovereign Bonds (Gilts).

The Bank conducts two forms of stress tests:
- internal stress tests including three standard scenarios: a scenario specific to the Bank, a general market crisis scenario and a combination of the two; and
- LCR regulatory stresses, ensuring that the Group has sufficient liquidity to survive for a 30 day period.

All stress testing assumptions, methodology and results are documented in the current ILAAP document. The Risk Appetite Statement details the current Board approved survival days. This forms the Board approved stress test appetite.

Principal risks and uncertainties (continued)

Liquidity risk (Outlook: Stable) (continued)

The Board has issued a risk appetite which details a minimum customer loan to deposit ratio. This risk appetite is designed to prevent aggressive asset growth being funded by excessive levels of wholesale funds, which could prove volatile in a stressed situation. Retail deposits are a valuable, stable funding source for the Bank. Most of the retail deposits are covered by a deposit insurance scheme, and analysis indicates that they are indeed stable over time.

Market risk (Outlook: Stable)

Market risk is the risk that the Bank will suffer losses caused by changes in the market value of financial assets and liabilities resulting from changes in market prices or rates (interest rates, foreign exchange, equity prices, commodity prices and indices). Interest rate risk is described separately below. The main market risk factor relevant to the Bank is foreign exchange rate risk. Market risk is relevant to the Bank's activity in which it primarily acts as a counterparty to satisfy customers' needs through the provision of a full range of foreign exchange and interest rate related services including derivative financial instruments. In compliance with Bank policies since 2006, the Bank enters into similar but opposite transactions for derivatives with Danske Bank Group counterparties to hedge these positions and effectively mitigate any market risk.

The Bank does not trade in derivatives. Derivatives are only entered into to manage net open positions deriving from transactions with customers.

Interest rate risk (Outlook: Stable)

The operations of the Bank are subject to the risk of interest rate fluctuations, to the extent that there is a difference between the amount of the interest-earning assets and interest-bearing liabilities that mature or reprice in specified periods. The principal objectives of asset and liability management are to protect levels of net interest income, while maintaining acceptable levels of interest rate and liquidity risk and to facilitate the funding needs of the Bank. To achieve these objectives, the Bank uses a combination of derivative financial instruments and debt securities.

Structural interest rate risk is calculated using balance sheet simulation processes that are undertaken across banking operations. The results of balance sheet simulations, together with other balance sheet risk management information and strategies, are presented and reviewed at Asset and Liability Committee (ALCO) and at scheduled Board meetings.

Interest rate risk is the risk of losses the Bank will incur as a result of an increase or a decrease in interest rates. Specifically this relates to the Bank's banking book only, as the Bank does not take any active proprietary positions and does not engage in any active trading in equity, debt or derivative markets. The specific types of interest rate risk include re-pricing/yield curve risk, basis risk, margin compression risk (including floor risk) and option risk. The Bank calculates interest rate risk using both Earnings at Risk (EAR) and Economic Value of Equity (EVE).

Pension risk (Outlook: Decreasing)

Pension risk is the risk of a shortfall in the Bank's defined benefit pension scheme that necessitates the Bank to make additional contributions to cover its pension obligations. The potential for a deficit in a defined benefit plan arises from a number of factors which could include:

- investments delivering a return below that required to provide the projected plan benefits. This could arise, for example, when there is a fall in the market value of equities, or when increases in long-term interest rates cause a fall in the value of fixed income securities held;
- the prevailing economic environment leading to corporate failures, thus triggering write-downs in assets;
- a change in either interest rates or inflation which causes an increase in the value of the scheme liabilities; and
- scheme members living longer than expected i.e. longevity risk.

The trustees are solely responsible for the investment of the Scheme's assets which are held separately from the assets of the Bank. The Bank and the trustees must agree on the investment principles and the funding plan. The trustees of the defined benefit pension scheme and the Bank have agreed a three year valuation cycle for obtaining a full actuarial valuation i.e. a written report, prepared and signed by the actuary, valuing the plan's assets and calculating its liabilities and assessing the overall plan solvency. The purpose of the valuation is to advise the trustees on the financial position of the plan and on the appropriate level of future contributions to be paid by the participating employers.

Based on the report and having obtained actuarial, financial and legal advice, the trustees enter into negotiations with the Bank in order to agree a schedule of contributions i.e. contributions required to meet the cost of future service pension accruals of active members, to meet the cost of the death in service benefits payable and potential deficiency contributions. The advice given includes an independent assessment of the sponsor's covenant.

Pension risk has been partly mitigated by the purchase in 2015 of a bulk buy-in annuity which covers all pensions in payment to retirees as at 1 February 2015 and by the decision taken in 2017 to cease future accrual from 1 October 2018.

Pension risk is assessed by way of an economic capital model that takes into account potential variations in factors, using a Value-at-Risk measure. The Bank has established procedures to be followed in the case of deviations from these objectives. The Board has defined risk targets for the Bank's defined benefit pension fund. To follow up on the objectives, the Bank uses quarterly risk reports that analyse the financial status of the plan by means of sensitivity analyses and the Value-at-Risk measure. The Bank has fixed limits for risk exposure levels.

The Bank's strategic focus for pension risk is to continue to review and oversee implementation of strategies to reduce pension risk.

Principal risks and uncertainties (continued)

Investment risk (Outlook: Stable)

The Bank's exposure to investment risk results from its holdings of cash at the Bank of England, UK government securities (gilts), European covered bonds, non-domestic sovereign and multilateral development banks. The investment portfolio fluctuates according to the Bank's liquidity and interest rate management requirements as well as its cash positions.

Group risk (Outlook: Stable)

This is the risk that the financial position of the business may be adversely affected by its relationship (financial and non financial) with other entities in the same group or by risks which may affect the financial position of the whole group. The impact of group risk is considered as part of all the Bank's risk assessment activities and across all risk categories. The Bank's parent, Danske Bank A/S, reported a return on equity of 13.6% for the year ended 31 December 2017. Furthermore, its capital position remained strong with a Common Equity Tier 1 ratio of 17.6% at 31 December 2017.

Capital adequacy risk (Outlook: Stable)

This is the risk that the Bank holds insufficient capital to absorb extreme and unexpected losses which could eventually result in insolvency.

Capital adequacy risk is central to the strategic planning process. There is regular senior management reporting in relation to forward-looking capital limits and early warning indicators and onward reporting to accounts. A comprehensive Individual Capital Adequacy Assessment Process (ICAAP) is undertaken annually showing the Bank's capital adequacy and capital quality under stress.

Capital position (unaudited)

The Bank's Common Equity Tier 1 ratio (on a UK Prudential Regulation Authority basis) decreased from 14.6% in December 2016 to 13.0% in December 2017.

Regulatory capital

	31 December 2017 £'000	31 December 2016 £'000
Common Equity Tier 1 capital		
Permanent share capital	**218,170**	218,170
Profit and loss account	**260,516**	102,378
Profit to be verified for inclusion in regulatory capital	**(119,663)**	(12,588)
Share premium account	**306,590**	306,590
Revaluation reserve	**35,364**	33,963
Available for sale reserve	**(1,119)**	-
Less : pension fund asset	**(154,261)**	(39,949)
Less : deferred tax asset	**(534)**	(18,489)
Less : prudent valuation adjustment	**(337)**	(83)
Less : intangible asset	**(274)**	-
Total common equity tier 1 capital after deductions	**544,452**	589,992
Additional Tier 1 capital		
CRD IV compliant instrument	**97,020**	81,002
Tier 2 capital		
Dated CRD IV compliant subordinated loan instruments	**126,000**	100,000
Total capital after deductions	**767,472**	770,994

Principal risks and uncertainties (continued)

Capital position (continued)

Risk-weighted exposure amounts (standardised approach)

	31 December 2017 £'000	31 December 2016 £'000
Credit risk	**3,816,468**	3,647,891
Operational risk	**376,183**	386,470
Market risk	**14**	6
Credit value adjustment	**44**	92
	4,192,709	4,034,459

Capital ratios

	31 December 2017	31 December 2016
Common Equity Tier 1 ratio	**13.0%**	14.6%
Tier 1 ratio	**15.3%**	16.6%
Total capital ratio	**18.3%**	19.1%
Total Capital Requirement (TCR)	**13.4%**	13.2%
Leverage ratio	**7.1%**	7.8%

The capital ratios are lower at 31 December 2017 compared to the previous year primarily because the full year 2017's profits will only be included in the Bank's capital in the first quarter of 2018.

Regulatory capital to statutory total equity reconciliation

	31 December 2017 £'000	31 December 2016 £'000
Regulatory Common Equity Tier 1 capital	**544,452**	589,992
Add back:		
- Pension fund asset	**154,261**	39,949
- Deferred tax asset	**534**	18,489
- Profit to be verified for inclusion in Common Reporting (COREP)	**119,663**	12,588
- Intangible assets	**274**	-
- Cash flow hedge reserve	**4**	-
Additional tier 1 capital	**97,020**	81,002
Prudent valuation adjustment	**337**	83
Statutory total equity	**916,545**	742,103

Minimum Pillar 1 capital requirements

	31 December 2017 £'000	31 December 2016 £'000
Credit risk	**305,317**	291,831
Operational risk	**30,095**	30,918
Market risk	**1**	-
Credit value adjustment	**4**	7
Pillar 1 regulatory capital	**335,417**	322,756

Principal risks and uncertainties (continued)

Regulatory capital flow of funds

	31 December 2017 £'000	31 December 2016 £'000
Common Equity Tier 1 capital		
Common Equity Tier 1 capital at 1 January	**589,992**	600,797
Profit for the year	**119,663**	46,403
Adjustment for profit to be verified for inclusion in regulatory capital	**(107,075)**	100,657
Property revaluation	**1,474**	948
Tax movement on revaluation reserve	**(73)**	2,183
Available for sale reserve	**(1,119)**	-
Additional Tier 1 interest (net of tax)	**(3,277)**	(3,324)
Pension surplus adjustment (net of tax)	**(72,561)**	15,049
Dividend	**-**	(200,000)
Deferred tax asset movement	**17,955**	27,362
Prudent valuation adjustment movement	**(253)**	(83)
Intangible asset movement	**(274)**	-
Total Common Equity Tier 1 capital after deductions at 31 December	**544,452**	589,992
Additional Tier 1 capital		
Additional Tier 1 capital at 1 January	**81,002**	81,034
Issuance of capital	**16,000**	-
Movement in interest accrual	**18**	(32)
Additional Tier 1 capital at 31 December	**97,020**	81,002
Tier 2 Capital		
Tier 2 capital at 1 January	**100,000**	100,000
Issuance of CRD IV compliant subordinated loan instruments	**26,000**	-
Total Tier 2 capital after deductions at 31 December	**126,000**	100,000
Total capital after deductions at 31 December	**767,472**	770,994

Capital requirements for calculating risk-weighted exposure amounts - Credit risk

As at 31 December 2017

	Capital required £'000	**RWA £'000**	**Exposure £'000**
Corporate	187,662	2,345,773	3,587,723
Retail	92,087	1,151,093	3,318,941
Institutions	4,286	53,577	116,221
Sovereign	-	-	3,889,187
Other	21,282	266,025	308,486
	305,317	**3,816,468**	**11,220,558**

As at 31 December 2016

	Capital required £'000	RWA £'000	Exposure £'000
Corporate	200,032	2,500,420	3,638,194
Retail	84,271	1,053,377	3,049,505
Institutions	2,959	36,985	92,483
Sovereign	-	-	3,943,035
Other	4,569	57,109	57,109
	291,831	3,647,891	10,780,326

Approved by order of the Board and signed on behalf of the Board of Directors.

Fiona Sturgess
Company Secretary
23 March 2018

The Directors of Northern Bank Limited (the "Bank") submit their annual report and audited financial statements (Income Statement, Statement of Comprehensive Income, Balance Sheet, Cash Flow Statement and Statement of Changes in Equity) for the year ended 31 December 2017.

The Bank's profits, strategic highlights, business developments and management of risk are set out in the Strategic Report on pages 3 to 12.

Financial instruments

The financial risk management objectives and policies of the Bank are detailed in Note 39 of the Financial Statements.

Dividends

The Directors paid interim dividends during the year of £Nil (2016: £200m). The Directors do not recommend the payment of a final dividend in respect of this financial year (2016: £Nil).

Directors and Directors' interests

The Directors during the year and to the date of this report were:

Michael Black
Vicky Davies
Jim Ditmore
Gerald Gregory
Kevin Kingston
Margaret Lesley Jones
Stephen Matchett
Lars Stensgaard Mørch
Paul Rooney

The Articles of Association do not require the Directors to retire by rotation.

No Director had any disclosable interest in the shares of any Danske Bank company.

Directors' liabilities

In terms of section 236 of the Companies Act 2006, the Bank paid a premium for a contract insuring the Directors and officers of Northern Bank Limited, its subsidiaries and controlled entities against personal liabilities which may arise in the course of the performance of their duties, as well as protecting the Group itself to the extent that it is obligated to indemnify Directors and officers for such liability.

Employee involvement

The Bank carries out an information programme to keep staff informed of business objectives and results. This is achieved through regular meetings, circulars, bulletins and specially commissioned videos as well as training courses for staff.

The Bank consults employees and their representatives within the Financial Services Union on a regular basis so that the views of the employees are considered in making decisions which are likely to affect their interests.

Employment policy

The Bank fully supports and complies with all legislation which is designed to promote equality of opportunity.

Employment of disabled persons

It is the policy of the Bank to promote equality of employment opportunities by giving full and fair consideration to applications from disabled people for vacancies where particular job requirements are considered to be within their ability. If existing employees become disabled, every effort is made to retain them within the workforce, wherever reasonable and practicable. The Bank also endeavours to provide equal opportunities in the training, promotion and general career development of disabled employees.

Political donations

No political donations were made by the Bank during the financial year (2016: £Nil).

Bribery Act 2010

The Bank adheres to the Bribery Act 2010 and supports a zero tolerance approach to bribery by any person associated with it whether acting in the UK or abroad.

Going concern

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

Note 39 to the Financial Statements together with "Principal risks and uncertainties" in the Strategic Report describe the risks the Bank is exposed to and how they are managed.

The key factors considered in the going concern assessment were:
- Capital and profitability i.e. the expected future profitability and thus self-sufficiency from a capital perspective of the Bank. The current Corporate Plan and ICAAP demonstrate that the Bank is expected to generate profits in excess of the capital required for projected lending growth;
- Liquidity. At 31 December 2017 the portfolio of liquid assets was £1.9bn and significantly in excess of that required to meet the most stressful liquidity scenario. The Bank is fully funded by customer deposits and has a low loan-to-deposit ratio of 77%; and
- Availability of Group support. The Bank has a supportive parent that is profitable and well capitalised.

As a consequence, the Directors believe the Bank is well placed to manage its business risks successfully.

After making enquiries, the Directors have a reasonable expectation that the Bank has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Financial Statements.

Future developments

Going forward, the Bank will continue to leverage from its strong competitive position by expanding its range of competitive banking products and services in the market, to support the growth of the Bank and its customers.

Disclosure of information to the auditor

The Directors who hold office at the date of approval of this Report of the Directors confirm that, so far as they are each aware, there is no relevant audit information of which the Bank's auditor is unaware; and each Director has taken all the steps he/she ought to have taken as a director to make himself/herself aware of any relevant audit information and to establish that the Bank's auditor is aware of that information. The Directors have pleasure in submitting their annual report and audited Financial Statements for the year ended 31 December 2017 to the shareholders.

Auditor

Deloitte LLP resigned as auditor on 10 February 2017 and Deloitte (NI) Limited was appointed as auditor of the Bank, in place of the resigning auditor, with effect from 24 February 2017. Pursuant to section 487, the auditor will be deemed to be reappointed and Deloitte (NI) Limited will therefore continue in office.

By order of the Board

Fiona Sturgess
Company Secretary

23 March 2018

NORTHERN BANK LIMITED
Statement of Directors' Responsibilities
For the year ended 31 December 2017

The Directors are responsible for preparing the Annual Report and the 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 the Directors have elected to prepare the Financial Statements in accordance with the International Financial Reporting Standards (IFRSs) as adopted by the European Union. 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 Bank and of the profit or loss of the Bank for that period. In preparing these Financial Statements, International Accounting Standard 1 requires that Directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the company's ability to continue as a going concern.

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

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Bank's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

On behalf of the Board

Kevin Kingston
Director and Chief Executive Officer

23 March 2018

Independent Auditor's Report to the members of Northern Bank Limited

Report on the Audit of the Financial Statements
Opinion on the Financial Statements of Northern Bank Limited (the 'Bank')

In our opinion the financial statements:
- give a true and fair view of the state of the Bank's affairs as at 31 December 2017 and of the profit for the financial year then ended;
- have been properly prepared in accordance with the relevant financial reporting framework.

The financial statements we have audited comprise:
- the Income Statement;
- the Statement of Comprehensive Income;
- the Balance Sheet;
- the Cash Flow Statement;
- the Statement of Changes in Equity; and
- the related notes 1 to 44 , including a summary of significant accounting policies as set out in note 1.

The relevant financial reporting framework that has been applied in their preparation is the Companies Act 2006 and International Financial Reporting Standards (IFRS) as adopted by the European Union ("the relevant financial reporting framework").

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 below in the "Auditor's responsibilities for the audit of the financial statements" section of our report.

We are independent of the Bank 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 public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We confirm that the non-audit services prohibited by the FRC's Ethical Standard were not provided to the Bank.

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

Summary of our audit approach

Key audit matters	The key audit matters that we identified in the current year were: - Loan loss provisions; - Deferred tax asset recognition; and - Defined benefit pension scheme obligations.
Materiality	The materiality that we used in the current year was £5,000,000 which was determined on the basis of profit before tax.
Significant changes in our approach	There have been no significant changes in our approach compared to the audit for the year ended 31 December 2017. Materiality is consistent with the prior year.

Conclusions relating to going concern

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

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 including 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 forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matters (continued)

Loan loss provisions	
Key audit matter description	The determination of appropriate provisions requires a significant amount of management judgment over key assumptions and relies on available data to determine both the timing of recognition and value of loan loss provisions. The risk is that provisions for impairment of loans do not represent an appropriate estimate of the losses incurred. This includes the risk that the estimate of cashflows on restructuring cases is not appropriately measured. At 31 December 2017, loan loss provisions as disclosed in note 14 to the financial statements, amounted to £91 million, representing a coverage level of 1.7% on a total portfolio of £5,513 million. (2016: 2.8% on a total portfolio of £5,239 million). The Bank's accounting policy for loan loss provisions is disclosed in note 1(d) to the financial statements. The key sources of estimation uncertainty in relation to loan loss provisions are disclosed in note 1(b) to the financial statements.
How the scope of our audit responded to the key audit matter	We undertook an assessment of the current provisioning practices in operation by the Bank to compare them with the requirements of IFRS. We have evaluated the design and implementation and tested the operating effectiveness of controls over: - impairment identification and calculation; - credit management processes, new lending, restructuring transactions and front line credit monitoring and assessment; and - collective and latent models, including source data and calculations, and the work of the credit review function. In examining both the sample of loan cases and the loan loss impairment models, we challenged management on the judgments made regarding the application of impairment triggers, status of restructures, collateral valuation and realisation time frames; and examined the credit risk functions analysis of data at a portfolio level. We tested the data used in the models, management adjustments to the modelled provisions, together with the calculations involved and the output from the models. Where appropriate, this work involved assessing third party valuations of collateral, internal valuation guidelines derived from market benchmark data, and external expert reports on borrowers' business plans. This allowed us to determine whether appropriate valuation methodologies were employed and to also make an assessment of the objectivity of the external experts used. We evaluated the disclosures made in the financial statements. In particular, we focused on challenging management that the disclosures were sufficiently clear in highlighting the significant uncertainties that exist in respect of loan impairment provisioning and the sensitivity of the provisions to changes in the underlying assumptions.
Key observations	Based on the evidence obtained, we found that the data and assumptions used by management in loan impairment provisioning are within a range we consider to be reasonable.

Key audit matters (continued)

Deferred tax asset recognition	
Key audit matter description	The risk that projection of profitability over a long time period presents inherent uncertainty, involving significant management judgements. The Bank has recognised a gross deferred tax asset based on the Bank's forecast profitability over a period of 5 years ended 31 December 2022 and has not recognised an asset in respect of tax losses that will be utilised after this date. A net deferred tax asset of £534k (2016: £18.4 million) has been recognised at 31 December 2017 in respect of brought forward tax losses and other timing differences. This comprises a gross deferred tax asset of £37.3 million (2016: £30.8 million) and a gross deferred tax liability of £36.8 million (2016: £12.4 million). The period supporting the recognition is consistent with the period that the Bank prepares its strategic plan for, including profit, capital and liquidity forecasts, and which management have concluded can be forecast with reasonable certainty. The Bank's accounting policy for deferred tax is disclosed in Note 1, and further disclosure of deferred tax is contained in Note 19.
How the scope of our audit responded to the key audit matter	We have tested the calculation of the deferred tax asset recognised. We have agreed the accounting profit used in the model to the approved strategic plan for the years ending 31 December 2018 to 31 December 2022. We assessed whether the forecast profits were appropriate by challenging both the growth, profitability and economic assumptions. We reviewed the model used by management to assess the likelihood of future profitability and challenged management's assessment of a range of evidence for the projection of long-term future profitability. We have tested the adjustments recorded by management relating to non-taxable expenditure of approximately £3.5 million per annum, made to the accounting profit to determine the taxable profit for accuracy. We have tested the corporation tax rates used to determine the net deferred tax asset by agreeing to the enacted UK corporation tax rates in the five year period. We have assessed the governance and control processes supporting the development of budgets and the strategic plan within the bank. We have also considered the Danske A/S group accounting policy to determine if the policy applied by the Bank is consistent with the group.
Key observations	We are satisfied that the appropriate tax rates have been used. We are satisfied that management's judgement of the recoverability of the asset is properly disclosed. We did not identify any materials errors in the valuation of the deferred tax asset.

Defined benefit pension scheme obligations	
Key audit matter description	Determining the key assumptions used to calculate the present value of the £1,194 million (2016: £1,239 million) defined benefit pension scheme obligations requires significant management judgement in relation to discount rates, inflation rates and mortality assumptions. This presents a risk that the principal assumptions used to determine the valuation of the pension liability are not supportable and the valuation is inaccurate. The Bank has recognised a curtailment gain in the year of £40.4m in relation to the closure of the defined benefit scheme to future accrual, which includes a number of significant assumptions in calculating. We note that the selection of the discount and inflation rates has a large impact on the overall valuation as set out in sensitivity analysis in note 23 to the financial statements. The Bank's accounting policy for pension costs is disclosed in note 1(d) to the financial statements. The key sources of estimation uncertainty in relation to pension costs are disclosed in note 1(b) to the financial statements.
How the scope of our audit responded to the key audit matter	We utilised actuarial specialists as part of our team to assist in evaluating the appropriateness of the principal actuarial assumptions used in the calculation of the retirement benefit obligation, as set out in note 23. This involved benchmarking management's assumptions against those used by a range of organisations as at 31 December 2017 and considering the consistency of those assumptions compared to the prior year. Our actuarial specialists also independently assessed the reasonableness of the curtailment gain recognised. This was considered to be within a reasonable range.
Key observations	Based on our audit of the principal assumptions, we are satisfied that they are within the reasonable range of estimates. We are satisfied that the retirement benefit obligation has been appropriately estimated by management.

Key audit matters (continued)

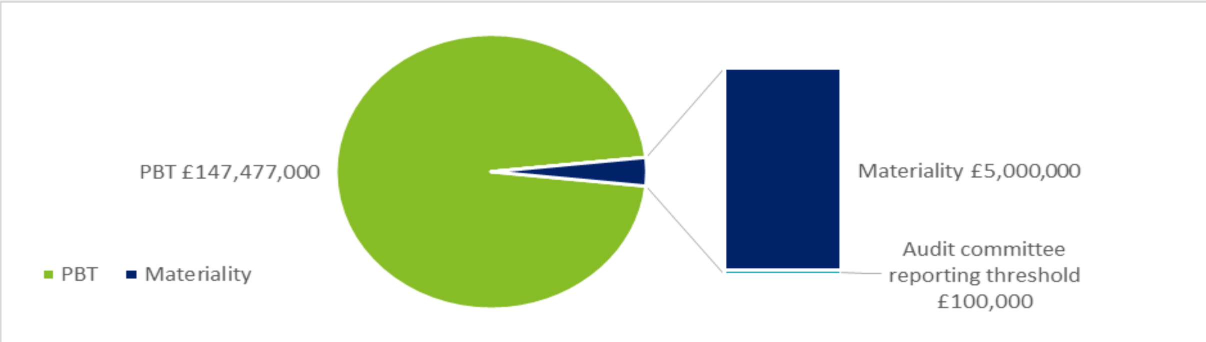
Our audit procedures relating to these matters were designed in the context of our audit of the financial statements as a whole, and not to express an opinion on individual accounts or disclosures. Our opinion on the financial statements is not modified with respect to any of the risks described above, and we do not express an opinion on these individual matters.

Our application of materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Materiality	£5,000,000 (2016: £5,000,000)
Basis for determining materiality	3.4% (2016: 4.3%) of pre-tax profit. We maintained materiality at £5,000,000 consistent with the financial year ended 31 December 2017 as the balance sheet of Northern Bank Limited had not changed significantly. The percentage applied to pre-tax profit is within the typical range we apply.
Rationale for the benchmark applied	The key driver of performance is pre-tax profit and the economics decisions of a reasonably knowledgeable person would be changed or influenced by a change in profitability.



We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £100,000 (2016: £100,000), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

An overview of the scope of our audit

Our audit was scoped by understanding the Bank and its environment, including controls, and assessing the risk of material misstatement. Based on that assessment, the audit was performed primarily by Deloitte (NI) Limited in Belfast, with centralised processes within the Danske A/S Group, (primarily General IT controls and collective loan loss provisions), being audited by a separate audit team in Copenhagen, Denmark, under our supervision.

Other information

The Directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our 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 this other information, we are required to report that fact.

We have nothing to report in this regard.

Responsibilities of Directors

As explained more fully in the Directors' Responsibilities Statement, 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 Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

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

As part of an audit in accordance with ISAs (UK), we exercises professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the entity's financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusion is based on the audit evidence obtained up to the date of the auditor's report. However, future events or conditions may cause the entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation (i.e. gives a true and fair view).

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that the auditor identifies during the audit.

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

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:
- the information given in the strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the Directors' report have been prepared in accordance with applicable legal requirements.

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

Matters on which we are required to report by exception

Under the Companies Act 2006 we are required to report to you if, in our opinion:
- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of Directors' remuneration have not been made.

We have nothing to report in respect of these matters.

Other matters which we are required to address

Following the recommendation of the Danske Bank A/S audit committee, we were appointed by the Board of Directors in 2015 to audit the financial statements for the year ending 31 December 2015 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of Deloitte is 3 years, covering the years ending 31 December 2015 to 31 December 2017.

Our audit opinion is consistent with the additional report to the audit committee we are required to provide in accordance with ISA (UK) 260.

John McCarroll, CA (Senior Statutory Auditor)
for and on behalf of Deloitte (NI) Limited
Chartered Accountants and Statutory Auditor
Belfast, United Kingdom

23 March 2018

NORTHERN BANK LIMITED
Income Statement
for the year ended 31 December 2017

	Note	2017 £'000	2016 £'000
Interest and similar income		**174,892**	177,243
Interest expense and similar charges		**(12,221)**	(16,831)
Net interest income	2	**162,671**	160,412
Fee and commission income	3	**58,051**	58,446
Fee and commission expense	3	**(5,532)**	(4,526)
Net trading income	2	**12,100**	14,119
Other operating income	4	**5,610**	1,947
Non interest income		**70,229**	69,986
Operating income		**232,900**	230,398
Operating expenses	5	**(111,675)**	(136,433)
Depreciation and amortisation expense	16,17	**(2,934)**	(2,915)
Profit before loan impairment credits		**118,291**	91,050
Loan impairment credits	40	**29,186**	25,933
Profit before tax		**147,477**	116,983
Tax expense	8	**(27,814)**	(70,580)
Profit for the year		**119,663**	46,403
Portion attributable to:			
Shareholders of Northern Bank Limited		**115,167**	41,772
Additional tier 1 capital holders		**4,496**	4,631
		119,663	46,403

All material items dealt with in arriving at the profit on ordinary activities before tax relate to continuing activities.

The notes on pages 27 to 75 form part of these Financial Statements.

NORTHERN BANK LIMITED
Statement of Comprehensive Income
for the year ended 31 December 2017

	Note	2017 £'000	2016 £'000
Profit for the year		119,663	46,403
Items that will not be reclassified to profit or loss			
Other comprehensive income/(loss):			
Actuarial gain/(loss) recognised in retirement benefit scheme	23	55,600	(67,449)
Tax on actuarial gain/(loss) recognised in retirement benefit scheme	19	(13,849)	18,132
Gain on property revaluation	17,18	1,444	841
Tax on property revaluation	19	(73)	2,183
Items that may be reclassified subsequently to profit or loss			
Property write down taken to income statement in year		30	107
Change in available for sale reserve			
Gains/ (losses) during the year		(1,492)	-
Tax	19	373	-
Change in cash flow hedge reserve			
Gains during the year	11	5	-
Tax	19	(1)	-
Total other comprehensive income/ (loss)		42,037	(46,186)
Total comprehensive income for the year		161,700	217
Portion attributable to:			
Shareholders of Northern Bank Limited		157,204	(4,414)
Additional tier 1 capital holders		4,496	4,631
Total comprehensive income for the year		161,700	217

The notes on pages 27 to 75 form part of these Financial Statements.

NORTHERN BANK LIMITED
Balance Sheet as at 31 December 2017

	Note	31 December 2017 £'000	31 December 2016 £'000
Assets			
Cash and balances at central bank	9	1,880,091	2,079,935
Items in the course of collection from other banks		55,463	53,916
Due from other banks	10	52,016	22,102
Derivative financial instruments	11	7,258	15,084
Investments - held to maturity securities	12	637,310	817,434
Investments - available for sale securities	13	370,629	-
Loans and advances to customers	14	5,422,293	5,094,188
Investment in subsidiaries	15	250	250
Intangible assets	16	274	-
Property, plant and equipment	17	45,983	43,288
Assets held for sale	18	150	180
Deferred tax assets	19	534	18,489
Defined benefit pension asset	23	154,261	39,949
Other assets	20	29,000	28,492
Total assets		8,655,512	8,213,307
Liabilities			
Due to other banks	21	34,420	32,687
Items in course of transmission to other banks		17,826	15,796
Derivative financial instruments	11	13,958	25,394
Deposits from customers	22	7,030,089	6,814,292
Notes in circulation		470,601	436,141
Other liabilities	24	38,680	39,501
Provisions	25	7,393	7,393
Subordinated debt	26	126,000	100,000
Total liabilities		7,738,967	7,471,204
Equity			
Share capital		218,170	218,170
Share premium account		306,590	306,590
Revaluation reserve		35,364	33,963
Available for sale reserve		(1,119)	-
Cash flow hedge reserve		4	-
Retained earnings		260,516	102,378
Shareholders of Northern Bank Limited		819,525	661,101
Additional tier 1 capital holders		97,020	81,002
Total equity		916,545	742,103
Total liabilities and equity		8,655,512	8,213,307

The notes on pages 27 to 75 form part of these Financial Statements.

These Financial Statements were approved by the Board of Directors on 23 March 2018 and were signed on its behalf by:

Kevin Kingston
Director and Chief Executive Officer

Stephen Matchett
Director and Chief Financial Officer

Company Number R0000568

NORTHERN BANK LIMITED
Statement of Changes in Equity
for the year ended 31 December 2017

	Note	Attributable to equity holders of the parent								
		Share Capital	Share Premium	Revaluation Reserve	Cash Flow Hedge Reserve	Available for sale Reserve	Retained Earnings	Total	Additional Tier 1 Capital	Total
		£,000	£,000	£,000	£,000	£,000	£'000	£'000	£'000	£'000
At 1 January 2016		218,170	306,590	34,153	-	-	305,296	864,209	81,034	945,243
Profit for the year		-	-	-	-	-	41,772	41,772	4,631	46,403
Other comprehensive income/(loss):										
Actuarial gain/(loss) recognised in retirement benefit scheme	23	-	-	-	-	-	(67,449)	(67,449)	-	(67,449)
Transfer re property disposals		-	-	(3,321)	-	-	3,321	-	-	-
Property revaluation		-	-	841	-	-	-	841	-	841
Property write down taken to income statement		-	-	107	-	-	-	107	-	107
Tax		-	-	2,183	-	-	18,132	20,315	-	20,315
Total other comprehensive income		-	-	(190)	-	-	(45,996)	(46,186)	-	(46,186)
Total comprehensive income for the year		-	-	(190)	-	-	(4,224)	(4,414)	4,631	217
Transactions with owners:										
Paid interest on additional tier 1 capital		-	-	-	-	-	-	-	(4,663)	(4,663)
Dividends paid		-	-	-	-	-	(200,000)	(200,000)		(200,000)
Tax		-	-	-	-	-	1,306	1,306	-	1,306
		-	-	-	-	-	(198,694)	(198,694)	(4,663)	(203,357)
At 31 December 2016		218,170	306,590	33,963	-	-	102,378	661,101	81,002	742,103
Profit for the year		-	-	-	-	-	115,167	115,167	4,496	119,663
Other comprehensive income/(loss):										
Actuarial gain recognised in retirement benefit scheme	23	-	-	-	-	-	55,600	55,600	-	55,600
Change in cash flow hedge reserve	11	-	-	-	5	-	-	5	-	5
Property revaluation		-	-	1,444	-	-	-	1,444	-	1,444
Property write down taken to income statement		-	-	30	-	-	-	30	-	30
Available for sale		-	-	-	-	(1,492)	-	(1,492)	-	(1,492)
Tax		-	-	(73)	(1)	373	(13,849)	(13,550)	-	(13,550)
Total other comprehensive income		-	-	1,401	4	(1,119)	41,751	42,037	-	42,037
Total comprehensive income for the year		-	-	1,401	4	(1,119)	156,918	157,204	4,496	161,700
Transactions with owners:										
Issuance of additional tier 1 capital									16,000	16,000
Paid interest on additional tier 1 capital		-	-	-	-	-	-	-	(4,478)	(4,478)
Tax		-	-	-	-	-	1,220	1,220	-	1,220
		-	-	-	-	-	1,220	1,220	11,522	12,742
At 31 December 2017		**218,170**	**306,590**	**35,364**	**4**	**(1,119)**	**260,516**	**819,525**	**97,020**	**916,545**

NORTHERN BANK LIMITED
Cash Flow Statement
for the year ended 31 December 2017

	Note	2017 £'000	2016 £'000
Cash flow from operating activities			
Profit before tax		**147,477**	116,983
Adjustments for:			
Group relief for tax losses		**(910)**	(1,544)
Tax paid		**(23,494)**	(14,896)
Adjustment for non-cash operating items:			
Amortisation and impairments of intangible assets	16	**85**	-
Amortisation of investments - held to maturity		**7,669**	5,785
Depreciation of property, plant and equipment	17	**2,849**	2,915
Loan impairment credits	40	**(29,186)**	(25,933)
Derivative financial instruments		**(3,610)**	5,191
Net defined benefit pension (credit)/expense	23	**(25,514)**	7,911
Other non-cash items		**129**	(901)
Total		**75,495**	95,511
Cash flow from operating capital			
Cash and balances at central bank	9	**(110,820)**	(70,383)
Items in transit		**483**	3,280
Loans and advances to customers		**(298,919)**	(181,439)
Due to other banks	21	**1,733**	25,893
Deposits		**215,797**	508,656
Notes in circulation		**34,460**	26,560
Defined benefit pension contributions	23	**(33,198)**	(10,993)
Other assets/liabilities		**1,774**	1,590
Cash flow from operations		(113,195)	398,675
Cash flow from investing activities			
Strike off of subsidiary companies		**-**	15,650
Acquisition of intangible assets		**(86)**	-
Maturity of investments - held to maturity		**260,000**	150,000
Purchase of investments - held to maturity		**(87,545)**	(207,400)
Purchase of investments - available for sale		**(383,098)**	-
Sale of investments- available for sale		**9,994**	-
Purchase of tangible assets	17	**(4,342)**	(1,698)
Sale of tangible fixed assets		**-**	6,319
Cash flow from investing activities		**(205,077)**	(37,129)
Cash flow from financing activities			
Increase in subordinated debt		**26,000**	-
Dividends paid to parent		**-**	(200,000)
Payments of AT1 interest		**(4,478)**	(4,663)
Increase in AT1 capital		**16,000**	-
Cash flow from financing activities		**37,522**	(204,663)
Cash and cash equivalents, beginning of year		**1,306,594**	1,149,711
Net change in cash and cash equivalents		**(280,750)**	156,883
Cash and cash equivalents, end of year		1,025,844	1,306,594
Cash in hand and demand deposits with central banks	9	**973,828**	1,284,492
Deposits with credit institutions and central banks with terms shorter than 3 months	10	**52,016**	22,102
Total		1,025,844	1,306,594

1. Basis of preparation

(a) General

Northern Bank Limited is a private limited company that is domiciled and incorporated in the UK. Its registered office is in Northern Ireland as set out on page 2.

The Bank's Financial Statements have been prepared on the going concern basis, in accordance with International Financial Reporting Standards (IFRS) and with applicable interpretations (IFRIC), issued by the International Accounting Standards Board (IASB) as adopted by the European Union as applied in accordance with the provisions of the Companies Act 2006.

The Bank does not prepare consolidated Financial Statements as the consolidated results are included in the consolidated financial statements of Danske Bank A/S and all subsidiaries of Northern Bank Limited are dormant (Note 15).

For the purpose of clarity, the primary Financial Statements and the notes to the Financial Statements are prepared using the concepts of materiality and relevance. This means that line items not considered material in terms of quantitative and qualitative measures or relevant to financial statement users are aggregated and presented together with other items in the primary Financial Statements. Similarly, information not considered material is not presented in the notes.

Basis of measurement

The Financial Statements of the Bank have been prepared under the historical cost convention, as modified by the revaluation of certain fixed assets and financial instruments that are measured at fair value.

Currency of presentation

All amounts are expressed in pounds sterling and whole thousands, unless otherwise stated. As a result, rounding discrepancies may occur because sum totals have been rounded off and the underlying hundreds are not presented to the users of the Financial Statements.

Going concern

The Bank's management has made an assessment of the Bank's ability to continue as a going concern and is satisfied that the Bank has the resources to continue in business for the foreseeable future.

Note 39 to the Financial Statements together with "Principal risk and uncertainties" in the Strategic Report describe the risks the Bank is exposed to and how they are managed.

The Bank has access to financial resources, the support of its ultimate parent, Danske Bank A/S and a strong customer loan to deposit ratio. As a consequence, the Directors believe that the Bank is well placed to manage its business risks successfully.

After making enquiries, the Directors have a reasonable expectation that the Bank has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Financial Statements.

Segmental reporting

A business segment is defined as a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments.

A geographical segment is defined as a group of assets and operations engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

The Bank's business is organised as one operating segment and as such, the assets, liabilities and results of the Bank are derived from the business of banking and other related financial services in the UK. The Bank has no material operations outside the UK and therefore no geographical information is presented. Revenues from no one single customer are greater than 10% of the Bank's revenues.

1. Basis of preparation (continued)

(b) Significant accounting estimates

There are no critical accounting judgements and the key estimates are set out below.

Management's estimates and assumptions of future events that will significantly affect the carrying amounts of assets and liabilities underlie the preparation of the Financial Statements. Those estimates and assumptions are presented in the following sections.

The estimates and assumptions are based on premises that management finds reasonable but which are inherently uncertain and unpredictable. The premises may be incomplete, unexpected future events or situations may occur, and other parties may arrive at other estimated values.

Measurement of loans

The Bank makes impairment charges to account for any impairment of loans and advances that occurs after initial recognition. Impairment charges consist of individual and collective charges and rely on a number of estimates, including identification of loans or portfolios of loans with objective evidence of impairment, expected future cash flows and the value of collateral. The Bank determines the need for impairment charges on the basis of the customer's expected ability to repay debt. This ability depends on a number of factors, including the customer's earnings capacity and trends in general economic growth and unemployment. Expectations of deteriorating repayment ability reduce credit quality and lead to downgrading of the customer.

The losses incurred under non-performing loan agreements depend, among other factors, on the value of collateral held. If the value of collateral decreased by 10%, individual impairment charges would increase by approximately £5,001,000 (2016: £7,941,000). If all customers were downgraded one rating category, collective impairment charges would increase by approximately £27,419,000 (2016: £46,081,000). Note 40 provides more details on impairment charges for loans. At the end of 2017, loans and advances accounted for approximately 63% of total assets (2016: 62%).

Recognition of deferred tax asset

A deferred tax asset is recognised for unused tax assets to the extent that (defined for this purpose as more likely than not) there will be sufficient future taxable profits against which losses can be used. The recognition of the deferred tax asset relies on the assessment of future profitability and the sufficiency of those profits to absorb losses carried forward. It requires significant estimates to be made about the projection of medium term future profitability because of the period over which recovery extends. If future profits increased by 10% per annum, this would lead to an increase in the deferred tax asset of £1.9m.

In assessing the future profitability of the Bank, the Board has considered a range of positive and negative evidence for this purpose. Among this evidence, the principal positive factors include:

- management actions taken to return the Bank to a normalised earnings path;
- the absence of any expiry date for tax losses; and
- external forecasts for Northern Ireland which indicate continued economic recovery.

The Board considered negative evidence and the inherent uncertainties in any medium term financial assumptions and projections, including:

- the quantum of profits required to be earned and the period over which it is projected that the tax losses will be utilised;
- the challenges of forecasting over the medium term, taking account of the level of competition, market dynamics and resultant margin and funding pressures; and
- the recent taxation changes and the likelihood of future developments and their impact on profitability and utilisation.

From 1 April 2016, only 25% of the Bank's taxable profits can be relieved by brought forward losses. This has increased the horizon over which losses can be used. As a result, the Bank has restricted the deferred tax asset such that it only reflects those losses that can be relieved against expected profits for the 5 year period to 31 December 2022 i.e. the current corporate planning horizon.

Defined benefit pension scheme

As disclosed in Note 23 the Bank operates a defined benefit pension scheme. The year end recognition of the liabilities under this scheme and the valuation of assets held to fund these liabilities require a number of significant assumptions to be made, relating to levels of scheme membership, key financial market indicators such as inflation and expectations on future salary growth and asset returns. These assumptions are made by the Bank in conjunction with the scheme's actuary and the Directors are of the view that any estimation should be prudent and in line with consensus opinion. Information on the sensitivity of significant actuarial assumptions is given in Note 23.

1. Basis of preparation (continued)

(c) Changes and forthcoming changes to accounting policies and presentation

Changes to basis of significant accounting policies and presentation during the year

No new standards were applied during 2017. The Bank applied the amendments to standards effective in the European Union (EU) during 2017. Those amendments relate to IAS 7, IAS 12 and IFRS 12 included in the annual Improvements to IFRS standards 2014-2016 cycle. The amendments to IAS 7 added a requirement to provide disclosures on changes to liabilities arising from financing activities including both changes arising from cash flows and non-cash flows. The Bank has implemented the amendment in Note 37. The application of the amendments to IAS 12 and IFRS 12 had no effect on the financial statements.

Standards and interpretations not yet in force

The IASB has issued four new IFRSs (IFRS 9, IFRS 15, IFRS 16 and IFRS 17) and some amendments to IFRSs that have not yet come into force. Similarly, the IFRIC has issued new interpretations that have not yet come into force. The Bank has not early adopted any of these changes to IFRS. The sections below explain the changes that are likely to affect the Bank's future financial reporting. For the other changes to IFRS's not described below, no significant impact is expected.

IFRS 9 Financial instruments

In July 2014, the IASB issued IFRS 9 Financial Instruments that will replace IAS 39. The standard provides principles for classification and measurement of financial instruments and introduces the expected credit losses impairment model and the new general hedge accounting model. The general hedge accounting model will be supplemented by a new macro hedge accounting model, which the IASB is working on.

IFRS 9 is effective from 1 January 2018, at which date the Bank will implement the standard. It is expected that the implementation of IFRS 9 will result in an increase in the allowance account of approximately £17m. The impact, net of tax, will be recognised as a reduction in shareholders' equity of approximately £12.8m. The Bank will continue to refine its estimate during the transition period in 2018 as processes are fully embedded.

In Note 38, the expected impact from the application of IFRS 9 at 1 January 2018 is disclosed, including changes to the Bank's accounting policy.

IFRS 15 Revenue from Contracts with Customers

In May 2014, the IASB issued IFRS 15, Revenue from Contracts with Customers. IFRS 15 replaces IAS 18, Revenue, and other existing IFRSs on revenue recognition. Under IFRS 15, revenue is recognised when the performance obligations inherent in the contract with a customer are satisfied. IFRS 15 is effective from 1 January 2018, at which date the Bank will implement the standard. The implementation is not expected to have an impact on shareholders' equity.

IFRS 16 Leases

In January 2016, the IASB issued IFRS 16 Leases. IFRS 16, which replaces IAS 17 Leases, will result in insignificant changes to the accounting for lessors. For lessees, the accounting will change significantly, as all leases (except short term leases and small asset leases) will be recognised in the balance sheet as a right-of-use asset. Initially, the lease liability and the right-of-use asset are measured at the present value of future lease payments (defined as economically unavoidable payments). The right-of-use asset is subsequently depreciated in a similar way to depreciation of other assets such as tangible assets, i.e. typically in a straight-line over the lease term.

IFRS 16 is effective from 1 January 2019 at which date the Bank will implement the standard. The Bank is currently assessing the impact from IFRS 16 on the Bank's Financial Statements. It is not yet possible to give an estimate of the effect on the Financial Statements of the changes to the accounting treatment when the Bank acts as a lessee. However, no significant impact on shareholders' equity is expected.

1. Basis of preparation (continued)

(d) Accounting policies

Translation of transactions in foreign currency

Transactions in foreign currency are translated at the exchange rate on the transaction date. Gains and losses on exchange rate differences between the transaction date and the settlement date are recognised in the income statement.

Monetary assets and liabilities in foreign currency are translated at the exchange rates at the balance sheet date. Exchange rate adjustments of monetary assets and liabilities arising as a result of differences in the exchange rates at the transaction date and at the balance sheet date are recognised in the income statement. Non-monetary assets and liabilities in foreign currency that are subsequently revalued at fair value are translated at the exchange rates at the date of revaluation. Exchange rate adjustments are included in the fair value adjustment of an asset or liability. Other non-monetary items in foreign currency are translated at the exchange rates at the transaction date.

Derivative financial instruments and hedge accounting

All derivatives are recognised on the balance sheet at fair value on trade date and are classified as hedging. 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 Bank makes use of derivative instruments to manage exposures to interest rates and foreign currency, including exposures arising from forecast transactions and firm commitments. In order to manage particular risks, the Bank applies hedge accounting for transactions which meet the specified criteria.

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.

Cash flow hedge

The Bank 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-sterling 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 11.

Loans and advances to customers

Loans and advances include overdrafts, credit card lending, market rate advances, invoice financing, housing loans, lease finance and other term lending.

At initial recognition, loans and advances are measured at fair value plus transaction costs less origination fees and other charges. This usually corresponds to the amount disbursed to the customer. Subsequently, they are measured at amortised cost, using the effective interest method, less any impairment charges. The difference between the value over the term to maturity and the redemption value is amortised over the term to maturity and recognised under Interest income. If fixed-rate loans and advances and amounts due are hedged effectively by derivatives, the fair value of the hedged interest rate risk is added to the amortised cost of the assets.

1. Basis of preparation (continued)

(d) Accounting policies (continued)

Loans and advances to customers (continued)

Impairment

- *Specific impairment provision*

For significant loans where default or other objective evidence of impairment exists the Bank determines the impairment charge individually.

Objective evidence of impairment of loans and advances exists if at least one of the following events has occurred:

- the borrower is experiencing significant financial difficulty;
- the borrower's actions, such as default or delinquency in interest or principal payments, lead to a breach of contract;
- the Bank, for reasons relating to the borrower's financial difficulty, grants to the borrower a concession that the Bank would not otherwise have granted; and
- it becomes probable that the borrower will enter bankruptcy or other financial restructuring.

If a customer facility is past due 90 days or more, the customer is considered in default and assessed for impairment.

Significant loans, advances and amounts due are tested individually for impairment at the end of each reporting period.

The impairment charge equals the difference between the carrying amount of the loan or advance and the present value of the most likely future cash flows from the loan or advance and is assessed by credit officers. The present value of fixed-rate loans and advances is calculated at the original effective interest rate, whereas the present value of loans and advances with a variable rate of interest is calculated at the current effective interest rate.

The cash flows used to determine the present value of future cash flows are specified by means of parameters used for solvency calculations and historical loss data adjusted for use in the Financial Statements. The adjustment reflects the loss identification period shown by the Bank's empirical data. This period is the period from the first evidence of impairment to the determination of a loss at customer level.

Impairment charges for loans, advances and guarantees are booked in an allowance account and set off against loans and advances or recognised as provisions for guarantees. Impairment charges for loans and advances are recorded under loan impairment charges in the income statement. If subsequent events show that impairment is not permanent, charges are reversed.

Loans and advances that are considered uncollectible are written off. Write-offs are debited to the allowance account. Loans and advances are written off once the usual collection procedure has been completed and the loss on the individual loan or advance can be calculated. If the full loss is not expected to be realised until after a number of years, for example in the event of administration of complex estates, a partial write-off is recognised, reflecting the Bank's claim less collateral, estimated dividend and other cash flows.

In accordance with the effective interest method, interest is recognised on the basis of the value of the loans and advances less impairment charges. Consequently, part of the allowance account balance is set aside for future interest income.

For non significant loans where default or other objective evidence of impairment is identified the Bank calculates the individual impairment charge statistically. Loans where objective evidence of impairment has not been identified are included in an assessment of collective impairment at portfolio level. For individual impairment charges calculated statistically and for the collectively assessed loans, the impairment charges are calculated as the difference between the carrying amount of the loans of the portfolios and the present value of expected future cash flows.

The customer's debt is written down to the amount that the borrower is expected to be able to repay after financial restructuring. If financial restructuring is not possible, the write-down equals the estimated recoverable amount in the event of bankruptcy. If the borrower's ability to repay depends significantly on the assets that have been provided as collateral (asset financing), the customer's debt is written down to the fair value of the collateral.

- *Collective impairment provision*

Loans and advances without objective evidence of impairment are included in a collective assessment of the need for impairment charges. The collective assessment also includes customers with objective evidence of impairment, but without need for impairment. Collective impairment charges are calculated for loans with similar credit characteristics when impairment of expected future cash flows from a portfolio has occurred but no interest rate change has been agreed on to adjust the credit margin. The collective impairment charge reflects the lowering of customer ratings over time (migration). When external market information indicates that an impairment event has occurred even though it has not yet caused a change in rating, the Bank registers an "early event" impairment charge. Early events represent an expected rating change because of deteriorating market conditions in an industry. If a rating downgrade does not occur as expected the charge is reversed. The loans and advances are divided into portfolios on the basis of current ratings. Calculation of charges also factors in portfolios of loans held by customers with improved ratings.

Management judgements are applied to adjust the collective impairment charge if the Bank becomes aware of market conditions at the balance sheet date that are not fully reflected in the Bank's models.

1. Basis of preparation (continued)

(d) Accounting policies (continued)

Offsetting of financial assets and liabilities

Assets and liabilities are offset when the Bank and the counterparty have a legally enforceable right to offset recognised amounts and have agreed to settle balances on a net basis or to realise the asset and settle the liability simultaneously. Positive and negative fair values of derivatives with the same counterparty are offset if the Bank has agreed with the counterparty to settle contractual cash flows net and to make cash payments or provide collateral on a daily basis to cover changes in the fair value of the derivative position. Master netting agreement or similar agreements give the right to additional offset in the event of default. Such agreements reduce the exposure further in the event of default, but do not qualify for offsetting in accordance with IFRS.

Investments - Hold-to-maturity

Hold-to-maturity financial assets consist of bonds with quoted prices in an active market held for the purpose of generating a return until maturity. The bonds are measured at amortised cost. Interest income is recognised according to the effective interest method, including amortisation of the difference between cost and the redemption value over the term to maturity of the bonds.

Investments - Available for sale

Financial assets available for sale can be listed or unlisted, and are non-derivative financial assets that are designated as available for sale and are not classified into any of the categories of (i) fair value through profit or loss; or (ii) loans and receivables and are recognised on trade date.

Financial assets available for sale are initially recognised at fair value including direct and incremental transaction costs. They are 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 when the cumulative gain or loss is transferred to the income statement.

Interest income is determined using the effective interest method. Impairment losses and translation differences on monetary items are recognised in the income statement within the year in which they arise.

Intangible assets

Software acquired is measured at cost, including expenses incurred to make a software application ready to use. Software acquired is amortised over its expected useful life, usually three years, according to the straight line method. Software is tested for impairment if indications of impairment exist and is written down to its value in use.

Property, plant and equipment

All freehold and long-term leasehold land and buildings are revalued annually on an open market basis by the Directors to reflect current market values, based on advice received from independent valuers. In addition, full independent valuations are carried out on a three year cycle on an open market basis, including directly attributable acquisition costs but without deducting expected selling costs. Revaluation increments are credited to the revaluation reserve, unless these reverse deficits on revaluations charged to the income statement in prior years. To the extent that they reverse previous revaluation gains, revaluation losses are charged against the revaluation reserve. This policy is applied to assets individually. Revaluation increases and decreases are not offset, even within a class of assets, unless they relate to the same asset.

All other items of property, plant and equipment are carried at cost, less accumulated depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to acquisition.

Property, plant and equipment carrying amounts are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of (i) the asset's fair value less costs to sell and (ii) the asset's value in use.

With the exception of freehold 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 Bank.

The estimated useful life is 20-50 years for property and 3-10 years for plant and equipment.

Assets residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

Gains or losses on the disposal of property, plant and equipment, which are determined as the difference between the net sale proceeds and the carrying amount at the time of sale, are included in the income statement.

Any realised amounts in the asset revaluation reserve are transferred directly to retained earnings.

1. Basis of preparation (continued)

(d) Accounting policies (continued)

Assets held for sale

Assets held for sale are tangible assets actively marketed for sale within 12 months.

Such assets are measured at the lower of their carrying amount at the time of reclassification and their fair value less expected costs to sell and are no longer depreciated.

Subordinated debt

Subordinated debt is a liability in the form of subordinated loan capital and other capital investments which, in case of the Bank's voluntary or compulsory winding-up, will not be repaid until the claims of its ordinary creditors have been met.

Subordinated debt is measured at amortised cost.

Financial guarantees

The Bank provides guarantees in the normal course of business on behalf of its customers. Guarantees written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Guarantees are primarily issued to support direct financial obligations such as commercial bills or other debt instruments issued by a counterparty. It is the credit worthiness of the Bank as a guarantee provider that enhances the marketability of the paper issued by the counterparty in these circumstances.

The financial guarantee contract is recorded as a contingent liability of the Bank. Fee income is booked in the income statement when earned.

A provision for financial guarantees is established within "Other liabilities" when there is reasonable doubt over individual customers' ability to fulfil their settlement obligations. Amounts provided for are determined according to management's assessment, taking into account available objective and subjective factors. When a loss is considered realised, the corresponding provision is transferred from the provisions account and the loss is written off.

Provisions and contingent liabilities

Provisions are recognised when a legal or constructive obligation exists as a result of past events and it is probable that an outflow of economic benefit will be necessary to settle the obligation and it can be reliably estimated. Provisions are not discounted to the present value of their expected net future cash flows except where the time value of money is considered material.

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 in the balance sheet but are disclosed unless they are remote.

Pension costs

Employees of the Bank are entitled to benefits on retirement, disability or death from the Bank's pension plans. The Bank operates both defined benefit and defined contribution pension schemes.

Defined contribution pension scheme

The Bank's obligation for contributions to these plans is recognised as an expense in the income statement as incurred.

Defined benefit pension scheme

The defined benefit scheme currently provides defined benefits based on years of service and career averaged revalued earnings. A liability or asset in respect of the defined benefit scheme is recognised in 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 Bank's defined benefit obligation.

The Bank's policy where actuarial remeasurements arise is to fully recognise such amounts directly in retained earnings 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.

1. Basis of preparation (continued)

(d) Accounting policies (continued)

Tax

Current tax

Current tax assets and liabilities are recognised in the balance sheet as the estimated tax payable on the profit for the year adjusted for prepaid tax and prior-year tax payables and receivables. Tax assets and liabilities are offset if the Bank has a legally enforceable right to set off such assets and liabilities and intends either to settle the assets and liabilities on a net basis or to realise the assets and settle the liabilities simultaneously.

Deferred tax

Deferred tax on all temporary differences between the tax base of assets and liabilities and their carrying amounts is accounted for in accordance with the balance sheet liability method. Deferred tax is measured on the basis of the tax regulations and rates that, according to the rules in force at the balance sheet date, are applicable at the time the deferred tax is expected to crystallise as current tax. Changes in deferred tax as a result of adopted changes in tax rates are recognised in the income statement on the basis of expected cash flows. Tax assets arising from unused tax losses are only recognised where, it is more likely than not that, there will be sufficient future taxable profits against which losses can be used. Deferred tax assets and liabilities are offset when they relate to the same tax jurisdiction.

Current and deferred tax is calculated on the profit for the year, and adjustments of prior-year tax charges are recognised in the income statement. Tax on items recognised in other comprehensive income is recognised in other comprehensive income. Similarly, tax on items recognised in equity is recognised in equity.

Repurchase and reverse repurchase agreements

Securities sold under agreements to repurchase are retained within the investment or other securities portfolios and accounted for accordingly. Liability accounts are used to record the obligation to repurchase. The difference between the sale and repurchase price represents interest expense and is recognised in the income statement over the term of the repurchase agreement. The consideration paid for securities held under reverse repurchase agreements is recorded in receivables. The difference between the purchase and sale price represents interest income and is recognised in the income statement over the term of the reverse repurchase agreement.

Shares in subsidiary undertakings

Shares in subsidiary undertakings are stated in the Bank's balance sheet at original cost less any necessary provision for impairment. Losses relating to the impairment in the value of shares in subsidiary undertakings are recognised in the income statement.

Revenue recognition

Interest income and expenses arising from interest-bearing financial instruments measured at amortised cost are recognised in the income statement according to the effective interest method on the basis of the cost of the individual financial instrument. Interest includes amortised amounts of fees that are an integral part of the effective yield on a financial instrument, such as origination fees, and amortised differences between cost and redemption price, if any. Interest on loans and advances subject to individual impairment is recognised on the basis of the impaired value.

Fee income and expenses

Fee income and expenses are broken down into fees generated by activities and fees generated by portfolios. Fees generated by activities comprises fees for the execution of one-off transactions. Fees generated by portfolios comprises recurring fees from the product portfolio.

Income from and expenses for services provided over a period of time are accrued over the period. Fees that form an integral part of the effective rates of interest on loans are carried under interest income.

Share-based payment

Part of the performance-based remuneration for the year is paid in the form of conditional shares. Rights to conditional shares vest up to seven years after the grant date, provided that the employee, with the exception of retirement, has not resigned from the Bank. In addition to this requirement, the vesting of rights is conditional on certain targets being met.

The fair value of share-based payments at the grant date is expensed over the vesting period with the intrinsic value expensed in the year in which the share-based payments are earned and the time value, if any, is accrued over the remaining service period. Expenses are set off against shareholders' equity. Subsequent fair value adjustments are not recognised in the income statement.

2. Net interest and net trading income

	2017 £'000	2016 £'000
Interest income		
Financial assets at amortised cost:		
Due from other banks and central bank	5,323	6,788
Investments - held to maturity	9,025	10,236
Investments - available for sale	1,017	-
Loans and advances to customers	161,455	159,774
Interest income on defined benefit pension scheme surplus (Note 23)	1,200	4,100
	178,020	180,898
Financial portfolios at fair value:		
Derivative financial instruments	(3,128)	(3,655)
Total interest income	174,892	177,243
Interest expense		
Due to other banks	580	666
Deposits from customers	9,282	13,635
Subordinated debt	2,359	2,530
Total interest expense	12,221	16,831
Net interest income	162,671	160,412
Net trading income		
Gains less losses on financial instruments at fair value	517	614
Margin on foreign exchange brokerage	10,775	10,020
Gain on disposal of VISA Inc. preference shares	808	-
Gain on disposal of VISA Europe Limited share	-	3,485
	12,100	14,119

Interest on financial assets subject to individual impairment is recognised on the basis of the impaired value and amounted to £4,686,000 (2016: £9,973,796).

Interest income includes £81,000 (2016 £3,000) received from Danske Bank A/S. Interest expense includes £6,000 (2016: £25,000) paid to Danske Bank A/S.

Trading income in 2016 includes a one-off gain arising on the sale of the investment held in Visa Europe Limited following its acquisition by Visa Inc. in June 2016. The Bank received a cash payment of £3,485,000 and circa 1,400 series C convertible preference shares in VISA Inc. Given the inherent uncertainty regarding the ultimate value of these shares, they were reported as having a £Nil value.

Trading income in 2017 includes a one-off gain of £808,000 arising on the sale of 1,400 series C convertible preference shares in VISA Inc. to its parent, Danske Bank A/S. These shares were acquired from the above sale of the investment held in Visa Europe Limited following its acquisition by Visa Inc.

3. Fee and commission income/expense

	2017 £'000	2016 £'000
Fee income		
Financing (loans, advances and guarantees)	6,817	6,691
Investment (securities trading, asset management, custody and advisory services)	5,387	5,308
Services (insurance and payment services)	45,847	46,447
Total	58,051	58,446
Fee expenses		
Financing (loans, advances and guarantees)	482	208
Investment (securities trading, asset management, custody and advisory services)	162	129
Services (payment services)	4,888	4,189
Total	5,532	4,526

4. Other operating income

Other income includes rental income, invoice finance fee income, profit on sale of tangible assets and sundry income.

	2017 £'000	2016 £'000
Profit on disposal of property, plant and equipment	-	587
Profit on sale of wealth business	4,454	-
Other income	1,156	1,360
Total	5,610	1,947

5. Operating expenses

	2017 £'000	2016 £'000
Staff costs		
- wages and salaries	42,523	39,820
- social security costs	4,515	3,711
- pension costs		
- defined benefit cost (Note 23)	12,658	10,059
- past service cost (Note 23)	(38,049)	860
- defined contribution	1,265	1,189
	22,912	55,639
Property related expenses	9,805	9,291
Information technology expenses	20,542	16,641
Administrative expenses	58,416	54,862
	111,675	136,433

Operating expenses include net recharges from Danske Bank A/S of £28,511,000 (2016: £26,233,000).

The average number of full time equivalent employees of the Bank during the year is outlined in Note 42.

6. Operating profit

	2017 £'000	2016 £'000
This is stated after:		
Income		
Aggregate amounts receivable, including capital repayments under finance leases and hire purchase contracts (net of depreciation £123,176,000 (2016: £116,465,000))	8,849	8,916
Profit on disposal of property, plant and equipment	-	587
Charges		
Depreciation of tangible fixed assets (Note 17)	2,849	2,915
Amortisation of intangible fixed assets (Note 16)	85	-
Hire of computers and equipment	510	591
Rental of premises held under operating leases	2,221	2,408
Auditor's remuneration		
Audit of these Financial Statements		
- Audit fee	138	102
- IFRS reporting requirements	40	30
Amounts receivable by the auditor and their associates in respect of:		
- Audit of the financial statements of subsidiary companies	28	28
- Other assurance services	80	90
	286	250

7. Directors' emoluments

	2017	2016
	£'000	£'000
Aggregate emoluments	1,176	1,272
Bank pension contributions to money purchase pension schemes	40	58
	1,216	1,330

In addition to the amounts shown above, social security costs were payable in respect of emoluments to Directors amounting to £152,000 (2016: £166,000). This includes £59,000 in respect of the emoluments of the highest paid Director in the year ended 31 December 2017 (2016: £58,000).

Where Non Executive Directors are employed by Danske Group, they are remunerated for their services by Danske Bank A/S.

Three Directors hold conditional shares (2016: three) and 493 were exercised during the year (2016: 5,188 shares). Further details are disclosed in Note 43 of the financial statements. For the year ended 31 December 2017 the total emoluments disclosed do not include the value of shares or share rights awarded under long term incentive schemes in accordance with Schedule 5 paragraph 1(3)(a) of the Large and Medium-sized Companies and Group (Accounts and Reports) Regulations 2008.

Two Directors (2016: Two) accrued retirement benefits under a money purchase pension scheme and no Director (2016: None) accrued retirement benefits under the Bank's defined benefit pension scheme.

The aggregate emoluments (including benefits in kind and pension contributions paid by the Bank) of the highest paid Director were £455,000 (2016: £438,000). The Director is a member of the Northern Bank Defined Contribution Pension Scheme to which the Bank paid contributions of £Nil (2016: £Nil) on his behalf. The highest paid Director exercised conditional shares during the year.

8. Tax expense

	2017	2016
	£'000	£'000
Current tax		
UK corporation tax		
Current year	15,713	15,976
Current year - corporation tax surcharge on Banking profits	6,987	7,525
Adjustment in respect of prior years	709	(598)
	23,409	22,903
Deferred tax note (Note 19)		
Current year	16,161	12,259
Adjustment in respect of prior years	(1,572)	502
Change in deferred tax charge as a result of lowered tax rate	-	1,086
Deferred tax asset derecognised	-	33,830
Previously unrecognised tax losses recognised in the year	(10,184)	-
	4,405	47,677
Tax charge	27,814	70,580

The effective taxation rate for the year ended 31 December 2017 is a charge of 18.9% (2016: 60.3%).

The tax assessed for the year differs from the standard rate of corporation tax in the UK (19.25%). A reconciliation from the expense implied by the standard rate to the actual tax expense is as follows:

	2017	2016
	£'000	£'000
Profit on ordinary activities before tax	147,476	116,983
Tax charge based on the standard rate of Corporation Tax in the UK of 19.25% (2016 20%)	28,389	23,397
Effects of:		
Expenses not deductible for tax purposes	1,248	754
Rate differences	(1,628)	1,712
Adjustments in respect of prior years	(862)	(96)
Effect of change in tax rates on the carrying value of the net deferred tax asset	-	1,086
Deferred tax asset (recognised)/derecognised	-	33,830
Previously unrecognised tax losses recognised in the year	(10,184)	-
Effect of corporation tax surcharge on Banking profits	10,851	9,897
	27,814	70,580

8. Tax expense (continued)

The statutory rate of UK corporation tax is 19% from 1 April 2017. A reduction in that rate was enacted by Finance Act 2016 to 17% from 1 April 2020. Finance Act (No.2) 2015 also introduced the Bank Surcharge from 1 January 2016, being an 8% charge on taxable profits above £25m before the offset of brought forward losses or group relief.

The impact of the corporation tax rate change, restriction on loss utilisation, and the impact of management's concurrent reassessment of the recoverability of the deferred tax asset is discussed in Note 17, Deferred Tax.

9. Cash and balances at central bank

	2017 £'000	2016 £'000
Cash in hand	614,590	588,132
Balances at central bank	1,265,501	1,491,803
	1,880,091	2,079,935

Cash and balances at central bank include mandatory deposits of £906,263,000 (2016: £795,443,000) which are not available for the Bank's day to day activities . Balances at central bank include cash ratio deposits which are non-interest bearing deposits placed with the Bank of England under the provisions of the Bank of England Act 1998.

10. Due from other banks

Amounts due from other banks are stated at amortised cost.

	2017 £'000	2016 £'000
Other amounts due	52,016	22,102

	2017 £'000	2016 £'000
Analysed by remaining maturity:		
- on demand or at short notice	52,016	22,102

	2017 £'000	2016 £'000
Amounts include:		
Due from parent and fellow subsidiary undertakings	32,161	7,153

11. Trading portfolio assets and liabilities

Trading portfolio assets and liabilities comprise all derivatives with positive and negative fair values, respectively.

(a) Trading portfolio assets

	2017 £'000	2016 £'000
Derivatives with positive fair value	7,258	15,084

(b) Trading portfolio liabilities

	2017 £'000	2016 £'000
Derivatives with negative fair value	13,958	25,394

11. Trading portfolio assets and liabilities (continued)

(c) Explanation of derivatives

The Bank uses derivatives to hedge positions created by customer transactions. The Bank does not trade in any financial instruments including derivatives and therefore does not have a trading book.

The most common type of interest rate and currency derivatives used by the Bank are:
- swaps;
- forwards; and.
- options.

Derivatives are recognised and measured at fair value. Some of the Bank's loans carry fixed rates. Generally, such items are recognised at amortised cost. The Bank uses fair value hedge accounting if the interest rate risk on fixed rate financial assets is hedged by derivatives. Some of the Bank's loans carry floating rates. The Bank uses cash flow hedge accounting if the exposure to variability in interest rates is hedged by derivatives.

Derivatives - hedging

	Positive Fair Value		Negative Fair Value	
	Notional amount £'000	Carrying amount £'000	Notional amount £'000	Carrying amount £'000
At 31 December 2017				
Currency contracts				
Forwards	245,950	5,877	312,938	5,922
Options	2,308	17	2,663	20
Interest rate contracts				
Swaps	156,420	1,294	307,685	7,946
Options	67,562	70	67,562	70
Total derivatives	472,239	7,258	690,848	13,958
Counterparty				
Ultimate parent and fellow subsidiary undertakings	345,704	5,137	562,061	8,534
Other	126,535	2,121	128,787	5,424
Total	472,239	7,258	690,848	13,958

	Positive Fair Value		Negative Fair Value	
	Notional amount £'000	Carrying amount £'000	Notional amount £'000	Carrying amount £'000
At 31 December 2016				
Currency contracts				
Forwards	246,700	13,088	248,742	12,583
Options	3,591	99	4,617	107
Interest rate contracts				
Swaps	19,727	919	311,458	11,726
Options	64,869	159	64,869	159
Other contracts				
Commodities	2,075	819	2,075	819
Total derivatives	336,962	15,084	631,761	25,394
Counterparty				
Ultimate parent and fellow subsidiary undertakings	205,841	5,725	545,091	19,200
Other	131,121	9,359	86,670	6,194
Total	336,962	15,084	631,761	25,394

11. Trading portfolio assets and liabilities (continued)

(d) Fair value hedge accounting

The interest rate risk on some fixed rate assets is hedged by derivatives. The Bank uses the interest rate risk on core free funds, net free reserves and investments in government securities, on both hold to maturity and available for sale bases, to manage the remaining interest rate risk within limits approved by the Board.

The fair values of the hedged interest rate risk and the hedging derivatives are measured at frequent intervals to ensure that changes in the fair value of the hedged interest rate risk lie within a band of 80% - 125% of the changes in the fair value of the hedging derivatives.

With effective hedging, the hedged interest rate risk on hedged assets is measured at fair value and recognised as a value adjustment of the hedged items. Value adjustments are reported in the income statement under net trading income.

At 31 December 2017 the carrying amounts of effectively hedged fixed rate assets were £420,406,000 (2016: £312,723,000). The table below shows the value adjustments of these assets and the hedging derivatives. The value adjustments have been recognised in the income statement as net trading income.

	2017 £'000	2016 £'000
Effect of interest rate asset hedging on profit		
Hedged loans and advances to customers	(3,149)	5,405
Hedging derivatives	3,151	(5,364)
Total	2	41

(e) Cash flow hedge accounting

The exposure to variability in cash flows attributable to interest rate risk associated with some floating rate assets is hedged by derivatives.

A portfolio cash flow hedge approach has been adopted, and effectiveness is assessed on a monthly basis by means of a capacity test. There is no change to the accounting for the hedged item and the derivative is carried at fair value, with changes in value reported in other comprehensive income to the extent that the hedge is effective.

	Positive Fair Value		Negative Fair Value	
	Notional amount £'000	Carrying amount £'000	Notional amount £'000	Carrying amount £'000
Cash flow hedges				
Swaps	15,000	10	-	-

These hedges are included in the derivatives table above.

	2017 £'000	2016 £'000
Derivatives held as cash flow hedges	15,000	-

	2017 £'000	2016 £'000
Gains recognised in Other Comprehensive Income for the year	5	-

12. Investments - held to maturity securities

	2017 £'000	2016 £'000
Issued by public bodies		
Investment securities		
- listed	**637,310**	817,434
Unamortised premiums/(discounts)		
- on investment securities	**22,310**	17,434

13. Investments - available for sale securities

	2017 £'000	2016 £'000
Listed investments	**370,629**	-

14. Loans and advances to customers

Loans and advances to customers are stated at amortised cost.

	2017 £'000	2016 £'000
Analysed by remaining maturity:		
- on demand or at short notice	**1,088,091**	1,130,449
- 3 months or less	**389,011**	297,106
- 1 year or less but over 3 months	**522,005**	568,648
- 5 years or less but over 1 year	**1,314,998**	1,278,118
- over 5 years	**2,198,485**	1,965,040
	5,512,590	5,239,361
Collective and specific bad and doubtful debt provisions (Note 40)	**(90,297)**	(145,173)
	5,422,293	5,094,188

15. Investment in subsidiaries

	2017 £'000	2016 £'000
Ordinary shares in subsidiaries	**250**	250

Movements on shares and investments in subsidiary undertakings

	2017 £'000	2016 £'000
At start of year	**250**	15,900
Companies dissolved	**-**	(15,650)
At end of year	**250**	250

Investments in subsidiary undertakings are included at historical cost.

	2017 £'000	2016 £'000
Subsidiary undertakings		
- other	**250**	250
Total - all unlisted	**250**	250

The Bank holds 100% of the ordinary share capital of its subsidiaries. All its subsidiary undertakings are incorporated in the UK. None of the subsidiaries of the Bank traded during the current year.

The subsidiary undertakings of the Bank are:

	Share class	Country of registration/ origination	% of equity share capital and voting rights held	Company number
Northern Bank Factors Limited	Ordinary	Northern Ireland	100%	NI 13062
Northern Bank Nominees Limited	Ordinary	Northern Ireland	100%	NI 4468
Northern Bank Pension Trust Limited	Ordinary	Northern Ireland	100%	NI 3155
Northern Bank Executor and Trustee Company Limited	Ordinary	Northern Ireland	100%	NI 4467

These subsidiaries of the Bank are dormant and are expected to remain so.

The registered office of all the subsidiary undertakings is Donegall Square West, Belfast BT1 6JS.

16. Intangible assets

	2017 £'000	2016 £'000
Cost at 1 January 2017	**-**	-
Additions	**86**	-
Transfer from property, plant and equipment	**273**	-
Cost at 31 December 2017	**359**	-
Accumulated amortisation at 1 January 2017	**-**	-
Amortisation charge for the year	**85**	-
Accumulated amortisation at 31 December 2017	**85**	-
Net book value at 31 December 2017	**274**	-

Intangible assets consist of acquired software.

17. Property, plant and equipment

	Freehold land and buildings	Leases of 50 years and over unexpired	Leases of under 50 years unexpired	Motor vehicles, fixtures and equipment	Total 2017
	£'000	£'000	£'000	£'000	£'000
Cost at 1 January 2017	11,952	24,704	2,413	23,310	62,379
Additions	-	-	978	3,364	4,342
Disposals	-	-	-	(104)	(104)
Transferred to intangible assets	-	-	-	(273)	(273)
Revaluation	(603)	1,169	(13)	-	553
Cost at 31 December 2017	11,349	25,873	3,378	26,297	66,897
Accumulated depreciation at 1 January 2017	145	346	711	17,889	19,091
Depreciation charge for the year	235	613	177	1,824	2,849
Accumulated depreciation on disposals	-	-	-	(104)	(104)
Revaluation	(268)	(647)	(7)	-	(922)
Accumulated depreciation at 31 December 2017	112	312	881	19,609	20,914
Net book value at 31 December 2017	11,237	25,561	2,497	6,688	45,983

	Freehold land and buildings	Leases of 50 years and over unexpired	Leases of under 50 years unexpired	Motor vehicles, fixtures and equipment	Total 2016
	£'000	£'000	£'000	£'000	£'000
Cost at 1 January 2016	12,738	23,923	1,767	22,242	60,670
Additions	-	-	673	1,025	1,698
Disposals	-	-	-	(40)	(40)
Transferred to assets held for sale	-	-	-	83	83
Revaluation	(786)	781	(27)	-	(32)
Cost at 31 December 2016	11,952	24,704	2,413	23,310	62,379
Accumulated depreciation at 1 January 2016	151	346	563	15,971	17,031
Depreciation charge for the year	260	615	154	1,886	2,915
Disposals	-	-	-	(30)	(30)
Transferred to assets held for sale	-	-	-	62	62
Revaluation	(266)	(615)	(6)	-	(887)
Accumulated depreciation at 31 December 2016	145	346	711	17,889	19,091
Net book value at 31 December 2016	11,807	24,358	1,702	5,421	43,288

Freehold properties and leasehold properties where the original lease is more than thirty years, are revalued on a five year cycle. An interim valuation was carried out by external qualified valuers (as defined in the Royal Institution of Chartered Surveyors (RICS) "RICS Valuation Standards 6th Edition"), Osborne King, Chartered Surveyors as at 30 June 2017. The basis of valuation is existing use value and the professional valuations have been made in accordance with RICS Practice Statements and Guidance Notes

Land and buildings occupied for own activities

	2017	2016
	£'000	£'000
Net book value	39,295	37,867

On the historical cost basis, freehold and leasehold land and buildings would have been included as follows:

	2017	2016
	£'000	£'000
Cost	19,943	19,087
Accumulated depreciation	(18,575)	(17,674)
Net book value	1,368	1,413

18. Assets held for sale

	2017 £'000	2016 £'000
Assets held for sale	**150**	180

Assets held for sale are measured at the lower of cost and fair value less expected costs to sell. During the year assets held for sale were written down by £30,000 (2016: £14,000).

Property held for sale consists of property which has been closed as part of a review of the business. During the year no property was transferred back to property, plant and equipment (2016: £21,000) . No properties were sold during the year (2016: properties were sold at a carrying value of £5,722,000 with a profit of £560,000).

19. Deferred tax

Movement in net deferred tax asset

	2017 £'000	2016 £'000
At 1 January	**18,489**	45,851
Recognised in the income statement (Note 8)	**(4,405)**	(47,677)
Recognised directly in equity:		
- Tax on actuarial gain	**(13,849)**	16,863
- Tax on available for sale fair value	**372**	-
- Effect of change in defined benefit pension asset as a result of surcharge and lowered tax rate	**-**	1,269
- Transfer to revaluation reserve	**(73)**	2,183
At 31 December	**534**	18,489

The Bank recognises deferred tax attributable to the following items:

	31 December 2017 £'000	31 December 2016 £'000
Deferred tax assets		
Tax losses carried forward	**24,220**	16,746
Available for sale assets	**373**	-
Accelerated capital allowances	**5,757**	6,205
Other timing differences	**6,978**	7,899
	37,328	30,850
Deferred tax liabilities		
Defined benefit pension asset	**34,228**	9,870
Net gain on revaluation of properties	**2,565**	2,491
Cash flow hedge reserve	**1**	-
	36,794	12,361
Net deferred tax asset	**534**	18,489

At 31 December 2017 the Bank had an unrecognised deferred tax asset of £23,600,000 (2016: £33,800,000) representing trading losses with a gross value of £139,000,000 (2016: £199,000,000). 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. Under current UK tax legislation there is no prescribed time period for loss utilisation however, the UK tax environment for banks in particular is unsettled and has been subject to repeated change and increased restrictions, principally on the use of historic losses as discussed below. As a result the period over which brought forward losses will be used to offset taxable profits has increased considerably.

The statutory rate of UK corporation tax is 19% from 1 April 2017. A reduction in that rate was enacted by Finance Act 2016 to 17% from 1 April 2020. In accordance with IAS 12, these rates are taken into account in assessing the value at which assets are expected to be realised and liabilities settled. From 1 April 2016, only 25% of a bank's profits can be relieved by brought forward losses, significantly extending the timeframe taken to realise value for existing tax losses.

As a result and in accordance with IAS 12, the Directors have assessed the recoverability of the deferred tax asset and have chosen to recognise deferred tax assets relating only to those losses that the Bank expects to utilise within the Bank's current corporate planning horizon. The combined impact of the legislative changes outlined above, and the Directors' reassessment of the recoverability horizon, results in a tax credit of £10,184,000, within a total deferred tax charge of £4,405,000.

20. Other assets

	2017 £'000	2016 £'000
Accrued interest	22,192	22,788
Prepayments and other amounts due	6,808	5,704
	29,000	28,492

21. Due to other banks

	2017 £'000	2016 £'000
Transaction balances with other banks	34,420	7,687
Deposits from other banks	-	25,000
	34,420	32,687

	2017 £'000	2016 £'000
Analysed by remaining maturity		
Repayable on demand	34,420	32,687

Amounts include:		
Due to parent and fellow subsidiary undertakings	29,790	29,274

22. Deposits from customers

	2017 £'000	2016 £'000
Current accounts	4,047,184	3,731,708
Demand deposits	2,189,217	2,082,695
Time deposits	793,688	999,889
	7,030,089	6,814,292

	2017 £'000	2016 £'000
Analysed by remaining maturity		
Repayable on demand	6,236,401	5,529,751
- 3 months or less but not repayable on demand	441,167	701,863
- 1 year or less but over 3 months	316,233	495,713
- 5 years or less but over 1 year	36,288	74,956
- over 5 years	-	12,009
	7,030,089	6,814,292

23. Pension asset

The Bank operates a defined benefit scheme (the Scheme) within which benefits built up before 1 January 2008 are linked to final salary and benefits built up after this date are based on career average earnings. With effect from 1 January 2004, the Scheme was closed to new members and a sponsored stand-alone defined contribution pension scheme was created for new staff. This does not affect the pension arrangements of existing employees. The Scheme will close to future accrual on 30 September 2018 and has resulted in a negative past service cost of £40,400,000 being recognised in the year ending 31 December 2017 (2016; £Nil). All future contributions from the date of cessation of accrual will be made to an alternative pension arrangement.

In relation to the defined contribution scheme the pension charge for the Bank for the year to 31 December 2017 was £1,265,000 (2016: £1,189,000). There were no outstanding contributions or prepayments made in the current or prior financial year in respect of the defined contribution scheme. The figures that follow relate to the defined benefit scheme only.

In future years, the service cost of the Scheme will be zero, following closure of the Scheme to future accrual from 30 September 2018. For the year-ending 31 December 2018, there will be a pro-rated service cost.

The latest triennial funding valuation was carried out as at 31 December 2015. The results of this valuation were updated by an independent actuary to an IAS 19 basis and the major assumptions used were:

	2017	2016
	% p.a.	% p.a.
Inflation (RPI)	**3.15**	3.25
Inflation (CPI)	**2.15**	2.25
Rate of future increase in salaries	**4.15**	4.25
Rate of increase for pre-1997 pensions in payment	**2.15**	2.25
Rate of increase for 1997-2008 pensions in payment	**2.95**	3.05
Rate of increase for post-2008 pensions in payment	**2.30**	2.30
Discount rate	**2.40**	2.60
Post retirement mortality		
Current pensioners at 60 - males (years)	**28.30**	28.50
Current pensioners at 60 - females (years)	**29.70**	30.00
Future pensioners at 60 - males (years)	**29.80**	30.40
Future pensioners at 60 - females (years)	**31.30**	32.00

The assumptions used by the actuary are the best estimate chosen from a range of possible actuarial assumptions which, due to the timescale covered, may not necessarily be borne out in practice.

The expected defined benefit pension fund contribution to be paid by the Bank and other participating employers within the Danske Bank Group in the year ending 31 December 2018 is £9,800,000.

Members contributions to the Scheme are currently 6% of pensionable salary.

A salary sacrifice arrangement was introduced with effect from March 2008. The service cost reflects the notional salary (i.e. before any allowance for salary sacrifice) paid to relevant employees. The Bank's share of the service cost has been calculated by netting off the actual contributions paid by those members who do not participate in the salary sacrifice arrangement.

Scheme asset information

The fair values of the Scheme's assets and liabilities are inherently uncertain because:
- the Scheme's assets are based on the value at the balance sheet date even though they are not intended to be realised in the short term and may be subject to significant change before they are realised; and
- the Scheme's liabilities are derived from cash flow projections over long periods.

23. Pension asset (continued)

Scheme asset information (continued)

	Market value 31 December 2017 £'000	Market value 31 December 2016 £'000
Equity securities	194,173	217,115
Debt securities	397,795	315,774
Real estate/property	59,940	55,310
Derivatives	66,983	69,119
Other	10,625	8,131
Buy-in annuity	618,845	613,800
Fair value of Scheme assets	1,348,361	1,279,249

The Scheme has not invested in any of the Bank's own financial instruments nor in other assets used by the Bank.

Reconciliation to the Balance Sheet

	2017 £'000	2016 £'000
Analysis of defined benefit obligation by status		
- Active members	357,700	379,700
- Deferred pensioner members	211,300	224,700
- Pensioners	625,100	634,900
Present value of defined benefit obligation	1,194,100	1,239,300
Fair value of plan assets	1,348,361	1,279,249
Net defined benefit asset	154,261	39,949

	2017 £'000	2016 £'000
Net defined benefit asset at beginning of year	39,949	104,316
Service cost (including past service costs)		
- the Bank	25,390	(10,919)
- other participating employers	(42)	(41)
Administration costs incurred over the year	(1,076)	(1,092)
Net interest on net defined benefit asset	1,200	4,100
Employers' contributions		
- the Bank	33,198	10,993
- other participating employers	42	41
Remeasurement effects recognised in OCI	55,600	(67,449)
Net defined benefit asset at end of year	154,261	39,949

Movement in present value of defined benefit obligation

	2017 £'000	2016 £'000
Defined benefit obligation at beginning of year	1,239,300	991,300
Gross current service cost		
- the Bank	12,658	10,059
- other participating employers	42	41
- contributions paid by members	11	13
Past service costs		
- the Bank	(39,048)	860
Interest cost on the defined benefit obligation	31,700	36,400
Actuarial gain - experience	(20,917)	(27,705)
Actuarial gain - demographic assumptions	(18,300)	(2,000)
Actuarial loss - financial assumptions	34,879	266,200
Benefits paid by the Scheme	(47,225)	(35,868)
Defined benefit pension obligation at end of year	1,193,100	1,239,300

23. Pension asset (continued)

Movement in fair value of Scheme assets

	2017 £'000	2016 £'000
Fair value of Scheme assets at beginning of year	1,279,249	1,095,616
Interest income on Scheme assets	32,900	40,500
Return on Scheme assets greater than discount rate	51,262	169,046
Employers' and employees' contributions paid into the Scheme		
- participating employers	33,197	10,993
- other participating employers	42	41
- member contributions	12	13
Benefits paid by the Scheme	(47,225)	(35,868)
Administration costs paid	(1,076)	(1,092)
Fair value of Scheme assets at end of year	1,348,361	1,279,249

Scheme expense recognised in the Income Statement

	2017 £'000	2016 £'000
Current service cost		
- the Bank included within operating expenses	12,658	10,059
- other participating employers	42	41
Past service cost and curtailments	(38,049)	860
	(25,349)	10,960
Net interest on net defined benefit asset	(1,200)	(4,100)
Administration costs incurred during the year	1,076	1,092
Scheme expense	(25,473)	7,952

Amount recognised in Other Comprehensive Income (OCI)

	2017 £'000	2016 £'000
Return on Scheme assets (greater)/less than discount rate	(51,262)	(169,046)
Actuarial gain due to liability experience	(20,917)	(27,705)
Actuarial loss/(gain) due to assumption changes	16,579	264,200
Remeasurement effects recognised in OCI - loss	(55,600)	67,449

Actual return on Scheme assets

	2017 £'000	2016 £'000
Interest income on Scheme assets	32,900	40,500
Return on Scheme assets greater/(less) than discount rate	51,262	169,046
Actual return on Scheme assets	84,162	209,546

Plan characteristics and associated risks

	2017 £'000	2016 £'000
Maturity profile of Defined Benefit Obligation		
- Expected benefit payments during fiscal year ending 31 December 2016	48,200	36,700
- Expected benefit payments during fiscal year ending 31 December 2017	49,200	37,500
- Expected benefit payments during fiscal year ending 31 December 2018	50,300	38,300
- Expected benefit payments during fiscal year ending 31 December 2019	51,400	39,200
- Expected benefit payments during fiscal year ending 31 December 2020	52,500	40,100
- Expected benefit payments during fiscal year ending 31 December 2021 through 31 December 2025	280,000	214,300

	2017 Years	2016 Years
Weighted average duration of Defined Benefit Obligation (years)	20	20

23. Pension asset (continued)

The Bank is exposed to a number of risks relating to the Scheme including assumptions not borne out in practice. The most significant risks are as follows:

Asset volatility
There is a risk that a fall in asset values is not matched by a corresponding reduction in the value placed on the Scheme's defined benefit obligation (DBO). The Scheme holds a proportion of growth assets, which are expected to outperform corporate and government bond yields in the long-term but give exposure to volatility and risk in the short-term.

Change in bond yields
A decrease in the corporate bond yields will increase the value placed on the Scheme's DBO, although this will be partially offset by any increase in the value of the Scheme's corporate bond holdings.

Inflation risk
Part of the Scheme's DBO is linked to inflation where higher inflation will lead to a higher value being placed on the DBO. Some of the Scheme's assets are either unaffected by inflation or loosely correlated with inflation (e.g. growth assets), meaning that an increase in inflation will generally increase the deficit.

Life expectancy
An increase in life expectancy will lead to an increased value being placed on the Scheme DBO. Future mortality rates cannot be predicted with certainty.

Significant actuarial assumption sensitivities

	2017 £'000
Discount rate	
Change in DBO at year end from a 50 basis points increase	(102,000)
Change in DBO at year end from a 50 basis points decrease	118,000
Price inflation (RPI measure)*	
Change in DBO at year end from a 50 basis points increase	59,000
Change in DBO at year end from a 50 basis points decrease	(80,000)
Pension increases**	
Change in DBO at year end from a 50 basis points increase	39,000
Change in DBO at year end from a 50 basis points decrease	(61,000)
Post retirement longevity	
Change in DBO at year end from a one year increase in longevity	46,000
Change in DBO at year end from a one year decrease in longevity	(46,000)

*Including consistent change to the pension increases, CPI related increases in deferment and salary growth.
**Derived assuming RPI has increased and decreased by 0.5% per annum respectively. This does not include a consistent change to any CPI related increases in deferment or salary growth.

23. Pension asset (continued)

Significant actuarial assumption sensitivities (continued)

The Scheme is exposed to a number of investment and demographic risks. The sensitivity of the defined benefit obligation to different scenarios is illustrated above. Note that these scenarios do not represent upper or lower bounds on what could happen. In addition, the sensitivity figures are based on indicative calculations and therefore may not be sufficiently accurate for use in any actuarial calculations whose results are intended for disclosure in the Bank's Financial Statements.

It should be noted that a change in the RPI assumption does not have a linear effect due to the relevant caps and collars on inflation linked increases.

The Bank quantifies and holds capital specifically in respect of pension risk.

24. Other liabilities

	2017	2016
	£'000	£'000
Accrued interest	**4,540**	6,522
Provision for off balance sheet financial guarantees	**819**	1,294
Accruals and sundry creditors	**23,446**	19,595
Corporation tax	**9,875**	12,090
	38,680	39,501

The Bank has issued a number of guarantees. Provisions are made if it is likely that drawings will be made under a guarantee and the amount payable can be reliably measured. The liability is measured at the present value of expected payments.

25. Provisions

	PPI	**FSCS levy**	**Other**	**Total**
	£'000	**£'000**	**£'000**	**£'000**
At 1 January 2017	**5,747**	**932**	714	**7,393**
Charge to income statement	**3,081**	**313**	**149**	**3,543**
Provisions utilised	(2,908)	(622)	(13)	(3,543)
At 31 December 2017	5,920	623	850	7,393

Provisions broken down by expected due date:

	2,017	2016
	£'000	£'000
Provisions due:		
- 1 year or less	**4,287**	3,124
- over 1 year	**3,106**	4,269
Total	7,393	7,393

25. Provisions (continued)

Payment Protection Insurance "PPI"

In common with the wider UK retail banking sector, the Bank continues to deal with complaints and redress issues arising out of historic sales of PPI. During the year, the Bank 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 £3,081,000 was required incorporating the Bank's estimate of the impact of PS17/3 issued on 2 March 2017 relating to a proposed time bar for complaints in August 2019. The increase in provision has taken into account a revision of the Bank's expectation of new customer initiated complaints in light of current experience, with the overall provision 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, 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; (iv) any additional amounts that may need to be paid in respect to previously handled claims; and (v) the response rates to the proactive customer contact.

As such, the factors discussed above mean that there is a risk that existing provision for PPI customer redress may not cover all potential costs. In light of this, the eventual costs of PPI redress may therefore differ materially from that estimated and further provision could be required.

The number of complaints received is monitored against past experience and future expectations and the Bank will continue to reassess the adequacy of the provision for this matter and the assumptions underlying the provision calculation based upon experience and other relevant factors as matters develop.

Financial Services Compensation Scheme (FSCS) levy

The Financial Services Compensation Scheme (FSCS) provides compensation to depositors in the event that a financial institution is unable to repay amounts due. Following the failure of a number of financial institutions, claims were triggered against the FSCS, initially to pay interest on borrowings which the FSCS has raised from the UK Government to support the protected deposits. During 2015, the FSCS levy was also invoiced to institutions for the third of three annual levies to cover capital repayments to the UK Government. The principal of these borrowings, which remains after the three annual levies have been paid, is anticipated to be repaid from the realisation of the assets of the defaulted institutions. The FSCS has however confirmed that the size of the future levies will be kept under review in light of developments from the insolvent estates. The FSCS has estimated levies due to 31 March 2018 and a provision of £623,000 (2016: £932,000) is held for the Bank’s calculated liability to that date. The ultimate FSCS levy as a result of the failures is uncertain.

Other

This represents provision for costs arising in respect of a number of legal actions and claims arising in the ordinary course of the Bank's business, together with onerous leases.

26. Subordinated debt

	2017	2016
	£'000	£'000
Balance at 1 January	**100,000**	100,000
Additions	**26,000**	-
Balance at 31 December	**126,000**	100,000

On 12 January 2015 £100,000,000 of CRD IV compliant subordinated instruments were issued to Danske Bank A/S. The rate of interest applied to these instruments is 200bps over 3 month LIBOR. The subordinated instruments are dated loan capital and may be redeemed by the issuer, Northern Bank Limited, subject to regulatory approval, on 12 January 2022.

On 19 December 2017, £26,000,000 of CRD IV compliant subordinated instruments were issued to Danske Bank A/S. The rate of interest applied to these instruments is 140bps over 3 month LIBOR. The subordinated instruments are dated loan capital and may be redeemed by the issuer, Northern Bank Limited, subject to regulatory approval and to giving the appropriate notice on 19 December 2024 or on each interest payment date thereafter. In the absence of this, Northern Bank Limited must redeem the Tier 2 instrument on the maturity date which is 19 December 2029.

27. Balance sheet items broken down by expected due date

The Bank presents the balance sheet items in order of liquidity instead of distinguishing between current and non-current items. The table below shows the balance sheet items expected to mature within the year (current) and after more than one year (non-current).

	2017	2017	2016	2016
	< 1 year	> 1 year	< 1 year	> 1 year
	£'000	£'000	£'000	£'000
Assets				
Cash and balances at central bank	973,828	906,263	1,284,492	795,443
Items in the course of collection from other banks	55,463	-	53,916	-
Due from other banks	44,383	7,633	19,115	2,987
Derivative financial instruments	4,333	2,925	11,753	3,331
Investments - held to maturity	150,321	486,989	259,851	557,583
Investments- available for sale	-	370,629	-	-
Loans and advances to customers	1,762,519	3,659,774	1,747,714	3,346,474
Investment in subsidiaries	-	250	-	250
Intangible assets	-	274	-	-
Property, plant and equipment	-	45,983	-	43,288
Assets held for sale	150	-	180	-
Deferred tax assets	-	534	-	18,489
Defined benefit pension asset	-	154,261	-	39,949
Other assets	28,020	980	21,630	9,862
Total assets	3,019,017	5,636,495	3,398,651	4,817,656
Liabilities				
Due to other banks	34,420	-	32,687	-
Items in course of transmission to other banks	17,826	-	15,796	-
Derivative financial instruments	4,633	9,325	11,473	13,921
Deposits from customers	4,793,486	2,236,603	5,590,343	1,223,949
Notes in circulation	-	470,601	-	436,141
Provisions	4,287	3,106	3,385	4,008
Other liabilities	14,415	24,265	18,612	20,889
Subordinated debt	-	126,000	-	100,000
Total liabilities	4,869,067	2,869,900	5,672,296	1,798,908

Deposits include fixed term deposits and demand deposits. Fixed term deposits are recognised according to maturity. Demand deposits have short contractual maturities but are considered a stable funding source with an expected maturity of more than one year.

28. Contractual dates of financial liabilities

The contractual due dates of financial liabilities are broken down by maturity time bands in the table below. The maturity analysis is based on the earliest date on which the Bank can be required to pay and does not reflect the expected due date. The sections on liquidity risk in the Strategic Report and risk management notes provide information about the Bank's liquidity risk and liquidity risk management.

	On demand	Not more than three months	More than three months but not more than one year	More than one year but not more than five years	More than five years
	£'000	£'000	£'000	£'000	£'000
At 31 December 2017					
Liabilities					
Due to other banks	34,420	-	-	-	-
Deposits from customers	6,236,401	441,167	316,233	36,288	-
Derivative financial instruments	-	2,289	3,583	6,370	1,945
Subordinated debt	-	-	-	-	126,000
	6,270,821	443,456	319,816	42,658	127,945
Off balance sheet items					
Contingent liabilities	104,965	-	-	-	-
Commitments	854,874	-	-	-	-
	959,839	-	-	-	-
At 31 December 2016					
Liabilities					
Due to other banks	32,687	-	-	-	-
Deposits from customers	5,529,751	701,863	495,713	74,956	12,009
Derivative financial instruments	-	5,235	8,649	9,240	2,607
Subordinated debt	-	-	-	-	100,000
	5,562,438	707,098	504,362	84,196	114,616
Off balance sheet items					
Contingent liabilities	90,438	-	-	-	-
Commitments	569,307	-	-	-	-
	659,745	-	-	-	-

For liabilities with variable cash flows, for example variable rate financial liabilities, disclosure is based on the contractual conditions at the balance sheet date.

Usually deposits are contractually very short term funding but, in practice, they are considered a stable funding source as amounts disbursed largely equal amounts received. A number of loan commitments and guarantees expire without being utilised. Loan commitments and guarantees are included at the earliest date on which the Bank can be required to pay.

For guarantees to result in a payment obligation to the Bank, a number of individual conditions must be met. As it is not possible to breakdown the earliest dates on which such conditions are met by maturity bands, all guarantees are included in the 'on demand' column.

29. Offsetting of financial assets and liabilities

There is no offsetting of financial assets and liabilities in the Financial Statements. In the event the counterparty or the Bank defaults, further offsetting will take place. This note shows netting according to enforceable master netting agreements (i.e. in the event of default) and collateral provided or received under these agreements.

	Gross amount	Legal right of offset	Further offsetting, master netting agreement	Collateral /offset	Net amount
	£'000	£'000	£'000	£'000	£'000
At 31 December 2017					
Financial assets					
Cash and balances at central bank	1,880,091	-	-	(470,601)	1,409,490
Due from other banks	52,016	-	(29,790)	(1,291)	20,935
Derivatives with positive fair value	7,258	-	(5,137)	-	2,121
Loans and advances to customers	5,422,293	(399,496)	-	-	5,022,797
Financial liabilities					
Due to other banks	34,420	-	(29,790)	-	4,630
Derivatives with negative fair value	13,958	-	(5,137)	(1,291)	7,530
Deposits from customers	7,030,089	(399,496)	-	-	6,630,593
Notes in circulation	470,601	-	-	(470,601)	-
At 31 December 2016					
Financial assets					
Cash and balances at central bank	2,079,935		-	(436,141)	1,643,794
Due from other banks	22,102		(7,153)	(1,827)	13,122
Derivatives with positive fair value	15,084	-	(5,725)	-	9,359
Loans and advances to customers	5,094,188	(490,406)	-	-	4,603,782
Financial liabilities					
Due to other banks	32,687	-	(7,153)	-	25,534
Derivatives with negative fair value	25,394	-	(5,725)	(1,827)	17,842
Deposits from customers	6,814,292	(490,406)	-		6,323,886
Notes in circulation	436,141	-	-	(436,141)	-

30. Fair value information for financial instruments

Financial instruments are carried in the balance sheet at fair value or amortised cost. The Bank breaks down its financial instruments by valuation method (Note 1 provides additional information).

(a) Financial instruments at fair value

The only financial instruments that are recognised at fair value are derivatives and available for sale securities.

The fair value is the amount for which a financial asset or a financial liability can be exchanged between knowledgeable, willing parties. Fair value is measured on the basis of the following hierarchy:

The fair value hierarchy

- Quoted price (level 1) consists of financial instruments that are quoted in an active market. The Bank uses the price quoted in the principal market.
- Valuation based on observable input (level 2) consists of financial instruments valued substantially on the basis of observable input other than a quoted price for the instrument itself. If a financial instrument is quoted in a market that is not active, the Bank bases its measurement on the most recent transaction price. Adjustment is made for subsequent changes in market conditions, for instance, by including transactions in similar financial instruments that are assumed to be motivated by normal business considerations. For a number of financial assets and liabilities, no market exists and in such cases, the Bank uses recent transactions, in similar instruments and discounted cash flows or other generally accepted estimation and valuation techniques based on market conditions at the balance sheet date, to calculate an estimated value.
- Valuation based on significant non-observable input (level 3): The valuation of certain financial instruments is based substantially on non-observable input.

If, at the balance sheet date, a financial instrument's classification differs from its classification at the beginning of the year, the classification of the instrument changes. Such changes are considered to have taken place at the balance sheet date.

Valuation techniques

The most frequently used valuation techniques include the pricing of transactions with future settlement and swap models that apply present value calculations, credit pricing models and options models, such as Black & Scholes models. As part of the Bank's control environment, valuation models are validated by units that are independent of the business units that develop the models and trade in the products covered by the models. Validation is made to test the implementation, quality and operating stability of models to ensure that the models can be used for pricing and risk management of financial products.

The valuation of available for sale securities is based on quotations on an active market.

The value of derivatives, primarily long-term contracts, is determined on observable yields extrapolated using yield curves for the full duration of the contracts.

Amortisation of initial margin

If, at the time of acquisition, a difference arises between the model value of a financial instrument, calculated on the basis of non-observable input and actual cost (day-one profit or loss), and the difference is not the result of transaction costs, the Bank adjusts model parameters to actual cost to take account of the initial margin. The valuation of derivatives thus includes amortisation of the value of initial margins over the remaining term to maturity. The initial margins cover future administrative expenses, capital consumption, funding costs, initial credit risk, etc.

	2017	2016
	£'000	£'000
Unamortised initial margins at 1 January	**440**	397
Amortised to the income statement during the year	**(1,126)**	(1,221)
Initial margins on new derivatives contracts	**1,128**	1,264
Terminated derivatives contracts	**(43)**	-
Unamortised initial margins at 31 December	**399**	440

30. Fair value information for financial instruments (continued)

	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
At 31 December 2017				
Financial assets				
Investments- available for sale securities	370,629	-	-	370,629
Interest rate and equity contracts	-	1,359	5	1,364
Currency contracts	-	5,881	13	5,894
Total	370,629	7,240	18	377,887
Financial liabilities				
Interest rate and equity contracts	-	8,011	5	8,016
Currency contracts	-	5,927	15	5,942
Total	-	13,938	20	13,958
At 31 December 2016				
Financial assets				
Interest rate and equity contracts	-	1,056	11	1,067
Currency contracts	-	13,134	63	13,197
Other derivatives	-	820	-	820
Total	-	15,010	74	15,084
Financial liabilities				
Interest rate and equity contracts	-	11,876	10	11,885
Currency contracts	-	12,623	67	12,690
Other derivatives	-	818	-	818
Total	-	25,317	77	25,394

Derivatives valued on the basis of non-observable input

	2017 £'000	2016 £'000
Fair value at 1 January	3	2
Acquisitions	2	4
Sale and redemption	(4)	(3)
Fair value at 31 December	1	3

The value adjustment through the income statement is recognised under net trading income.

30. Fair value information for financial instruments (continued)

(b) Financial instruments at amortised cost

In this section, the fair value of financial instruments recognised at amortised cost is presented. The fair value is based on quoted market prices, if available. If quoted prices are not available, the value is approximated to reflect the price that would have been fixed, had the terms been agreed at the balance sheet date.

The fair values disclosed below are determined on the basis of the following principles:

Investment securities

Quoted prices in an active market exist for these financial instruments.

Other financial instruments

The determination of the fair value of financial instruments recognised at amortised cost is based on the following preconditions relating to interest rate risk:

- For a number of the Bank's loans, the interest rate depends on the standard variable rate fixed by the Bank. The rate is adjusted only upon certain changes in market conditions. Such loans are considered to carry interest at a variable rate, as the standard variable rate applied by the Bank at any time applies to both new and existing arrangements.

- The interest rate risk on some fixed-rate financial assets is hedged by derivatives. The Bank uses the interest rate risk on core free funds and investments on both a hold to maturity and available for sale basis to manage the remaining interest rate risk. Consequently, the fair value of unhedged fixed-rate loans is presented in the table below.

For financial instruments that are only to a limited extent influenced by changes in credit risk, the amortised cost, including the adjustment for the fair value hedge accounting of the interest rate risk, is a reasonable approximation of fair value. This is the case for due from/to other banks, cash and balances at central bank and deposits from customers.

For loans, impairment charges are assumed to equal the fair value of the credit risk with the following adjustments:

- The calculation of impairment charges for loans subject to individual impairment is based on the most likely outcome, and loans that are considered asset finance are written down to the fair value of collateral provided, i.e. assuming that restructuring is not possible. The fair value is adjusted by weighting all possible outcomes. For other loans, impairment charges are recognised if a customer is downgraded to reflect a change in the probability of default.
- The credit margins on individual risks are accounted for by adjusting the fair value for the difference between the current credit premium and the credit premium demanded at the balance sheet date.

In the table below, fair value is presented for classes of financial instruments for which the carrying amount is not a reasonable approximation of fair value.

	Carrying amount £'000	Fair value £'000	Level 1 £'000	Level 2 £'000	Level 3 £'000
Financial assets					
Investments - held to maturity securities	**637,310**	**645,777**	**645,777**	**-**	**-**
Loans at amortised cost	**5,422,293**	**5,430,935**	**-**	**-**	**5,430,935**
At 31 December 2017	**6,059,603**	**6,076,712**	**645,777**	**-**	**5,430,935**
Financial assets					
Investments - held to maturity securities	817,434	835,391	835,391	-	-
Loans at amortised cost	5,094,188	5,096,819	-	-	5,096,819
At 31 December 2016	5,911,622	5,932,210	835,391	-	5,096,819

31. Share capital

	2017 £'000	2016 £'000
Allotted, called up and fully paid		
Ordinary shares of £1 each - equity		
At 31 December	**218,170**	218,170

The share capital consists of shares of a nominal value of £1 each. All shares carry the same rights therefore there is only one class of share.

32. Additional tier 1 capital

At the end of 2017, the total nominal value of issued additional tier 1 capital amounted to £96,000,000 (2016: £80,000,000). Capital notes of £16,000,000 were issued on 19 December 2017 to the Bank's immediate parent, Danske A/S. This is in addition to the capital notes of £80,000,000 issued on 12 January 2015.

The capital issued includes no contractual obligation to deliver cash or another financial asset to the holders, as the Bank may, at its sole discretion, omit payment of interest and principal payments to the bondholders. As a result the issue does not qualify as a financial liability according to IAS32. The net amount received at the time of issue is recognised as an increase in equity. Interest payments are accounted for as dividends, which are recognised directly in equity at the time the payment obligation arises. If the Bank chooses to redeem the bonds, equity will be reduced by the redemption amount at the time of redemption. Amounts received or paid for the sale or acquisition of additional tier 1 capital instruments are recognised directly in equity, similarly to holdings of own shares.

The reserve includes the net proceeds at the time of issuance and accrued interest not yet paid to holders of the capital.

As described above, the Bank may, at its sole discretion, omit interest and principal payments to bond holders. Any interest payments must be paid out of retained earnings of the Bank. The additional tier 1 capital will be written down temporarily if the common equity tier 1 ratio falls below 7% for the Bank [or Danske Bank Group]. The ratio at 31 December 2017 is disclosed in the Strategic Report. In respect of the capital notes issued, interest is paid at a rate of 525 bps over three month LIBOR for capital notes issued on 12 January 2015 and 355 bps over 3 month LIBOR for the capital notes issued on 19 December 2017. If certain conditions are fulfilled, including approval of the Prudential Regulatory Authority, the issued bonds may be redeemed at par from January 2022 and December 2022 respectively.

33. 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 31 December 2017, the cash flow hedge reserve reflected a cumulative gain of £5,000. This was offset by a deferred tax liability of £1,000.

34. Contingent liabilities

Contingent liabilities consist of possible liabilities arising from past events. The existence of such liabilities will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the Bank's control. Contingent liabilities that can, but are not likely to, result in an outflow of economic resources are disclosed.

The Bank uses a variety of loan-related financial instruments to meet customers' financial requirements. Instruments include loan offers and other credit facilities, guarantees and instruments not recognised in the balance sheet. If an instrument is likely to result in a payment obligation, a liability is recognised under other liabilities corresponding to the present value of expected payments.

	2017 £'000	2016 £'000
Contingent liabilities		
Guarantees and irrevocable letters of credit	**104,965**	90,438
Commitments		
Irrevocable loan commitments shorter than 1 year	**584,774**	394,952
Irrevocable loan commitments longer than 1 year	**270,100**	174,355
	854,874	569,307

The Bank is named in and is defending a number of legal actions arising in the ordinary course of business. The current provision is deemed adequate based on the known facts and circumstances of each case.

35. Capital commitments

The Bank had future capital expenditure which had been contracted but not provided for in the Financial Statements at 31 December 2017 of £Nil (2016: £24,000).

36. Leasing

The Bank leases a variety of assets to third parties under finance lease arrangements, including vehicles and general plant and machinery. The costs of assets acquired by the Bank during the year for the purpose of letting under finance leases and hire purchase contracts amounted to £12,623,000 (2016: £6,774,000) and £124,255,000 (2016: £113,875,000) respectively.

The total closing balances of finance leases and hire purchase contracts were £18,966,000 (2016: £15,092,000) and £204,385,000 (2016: £185,051,000) respectively.

Finance lease and hire purchase receivables

	2017	2016
	£'000	£'000
Gross investment in finance lease and hire purchase receivables		
Due within one year	**15,902**	13,942
Due within one to five years	**202,654**	184,596
Due after five years	**17,662**	14,214
Total gross investment in finance lease receivables	**236,218**	212,752
Unearned income	**(12,865)**	(13,108)
Net investment in finance lease and hire purchase receivables	**223,353**	199,644

Within the Bank, at 31 December 2017, there are specific provisions of £779,000 (2016: £566,000) in relation to finance lease receivables with a collective provision of £Nil (2016: £Nil).

Operating leases

	Land and buildings	Land and buildings
	2017	2016
	£'000	£'000
Operating lease expiring		
- within 1 year	**148**	244
- in 1 - 5 years	**1,056**	1,057
- after 5 years	**988**	917
	2,192	2,218
Where the Bank is the lessee the future minimum lease payments under non-cancellable operating leases are:		
- within 1 year	**2,192**	2,218
- between 1 and 5 years	**6,423**	5,322
- over 5 years	**3,646**	2,473
	12,261	10,013

37. Reconciliation of liabilities arising from financing activities

This note provides further information on the cash flow statement, including a reconciliation of the cash flows arising from financing activities.

Financing activities include cash flows from the Bank's issued subordinated debt and AT1 capital.

	AT 1 Capital	**Subordinated debt**
	£'000	**£'000**
At 1 January 2017	**80,000**	**100,000**
Instruments issued	**16,000**	**26,000**
At 31 December 2017	**96,000**	**126,000**
At 31 December 2016	80,000	100,000

38. Implementation of IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with customers

Changes and impact on the Bank's financial statements from IFRS 9

On 1 January 2018, the Bank adopted IFRS 9 Financial Instrument issued by IASB in July 2014. The standard provides revised principles for classification and measurement of financial instruments, introduces the expected credit loss impairment model and the new general hedge accounting model.

In accordance with the transition requirements of IFRS 9, comparatives will not be restated as retrospective application of the impairment requirements is not possible without the use of hindsight. Further, the Bank has decided to use the option in IFRS 9 to continue to apply the hedge accounting requirements of IAS 39.

When IFRS 9 has been implemented, the allowance account will increase as expected credit losses are to be recognised for all financial assets. Impairments will be made for at least 12 months' expected credit losses and the portfolio of financial assets for which life time-expected credit losses will increase. Currently, impairments are made only for incurred losses. It is expected that the allowance account will increase by approximately £17,000,000. The Bank will continue to refine its estimate during the transition period in 2018 as processes are fully embedded.

The total impact on shareholders' equity, net of tax, of the implementation of IFRS 9 is expected to be approximately £12,750,000.

The classification of financial instruments under IFRS 9 is not expected to have a significant impact.

Below, the changes due to the implementation of IFRS 9, including the new accounting policy, are explained further.

Classification and measurement under IFRS 9 – general

Under IFRS 9, financial assets are classified on the basis of the business model adopted for managing the assets and on their contractual cash flow characteristics (including embedded derivatives) into one of the following measurement categories:
- Amortised cost (AMC);
- Fair value through other comprehensive income (FVOCI); or
- Fair value through profit or loss (FVPL).

Financial assets are measured at AMC if they are held within a business model with the objective of collecting contractual cash flows (held to collect) and if cash flows are solely payments of principal and interest on the principal amount outstanding.

Financial assets are measured at FVOCI if they are held within a business model with the objective of both collecting contractual cash flows and selling (held to collect and sell) and if cash flows are solely payments of principal and interest on the principal amount outstanding. FVOCI results in the assets being recognised at fair value in the balance sheet and at AMC in the income statement. Hence, gains and losses, except for expected credit losses and foreign exchanges gains and losses, are recognised in other comprehensive income until the financial asset is derecognised. When the financial asset is derecognised the cumulative gains and losses previously recognised in other comprehensive income is reclassified to the income statement.

All other financial assets are mandatorily measured at FVPL including financial assets within other business models such as financial assets managed at fair value or held for trading and financial assets with contractual cash flows that are not solely payments of principal and interest on the principal amount outstanding.

Like IAS 39, IFRS 9 includes an option to designate financial assets at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities or recognising the gains or losses on them on different bases.

The principles applicable to financial liabilities are largely unchanged from IAS 39. Generally, financial liabilities are still measured at amortised cost with bifurcation of embedded derivatives not closely related to the host contract. Financial liabilities measured at fair value comprise derivatives, the trading portfolio and liabilities designated at fair value through profit or loss under the fair value option. Value adjustments relating to the inherent credit risk of financial liabilities designated at fair value are recognised in other comprehensive income unless this leads to an accounting mismatch.

The business model assessment

The business model assessment in the Bank is based on observable factors for the different portfolios such as: (1) how the performance of the business model and the financial assets held within that business model are evaluated and reported to the Executive Committee and the Board of Directors, (2) the risks that affect the performance of business model and the way such risks are managed, and (3) past and expected frequency, value and timing of sales from the portfolio. In general, the business model assessment in the Bank can be summarised as follows:

- The Bank's financial assets consist primarily of loans and has a "held to collect" business model. The management and the reporting of performance is based on the collecting of the contractual cash flows and loans are only very infrequently sold; and
- Treasury within the Bank has portfolios of bonds within the "held to collect" business model and the "held to collect and sell" business models.

The SPPI test (solely payment of principal and interest on the principal amount outstanding)

The second step in the classification of the financial assets in portfolios being 'held to collect' and 'held collect and sell' relates to the assessment of whether the contractual cash flows are consistent with the SPPI test. The principal amount reflects the fair value at initial recognition any subsequent changes, e.g. due to repayment. The interest shall represent only consideration for the time value of money, credit risk, other basic lending risks and a profit margin consistent with basic lending features. If the cash flows introduce more than de minimis exposure to risk or volatility that are not consistent with basic lending features, the financial asset is mandatorily recognised at FVPL.

38. Implementation of IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with customers (continued)

In general, the assessment of the Bank's portfolios of financial assets that are 'held to collect' or 'held to collect and sell' (loans and bonds) has, amongst others, covered the following elements:

- compensation for the time value of money. For some of the Bank's variable rate loans, the market standard for those loans is that the reset frequency and the tenor of the reference rate does not match. It has been assessed that the mismatch does not significantly modify the compensation for the time value of money. No loans have interest rates that are leveraged or linked to e.g. development in share prices etc;
- prepayment options are consistent with the SPPI test, if the prepayment amount represent principal amount outstanding, accrued interest and may include a reasonable compensation for the early repayment;
- extension options are consistent with the SPPI test, if the cash flows during the extension period represents cash flows that are solely payment of principal and interest on the principal amount outstanding; and
- compensation for credit risk. The interest rate includes a credit margin to compensate the Bank for the credit risk, and may be fixed initially. The Bank does not incorporate profit sharing agreement, e.g. by contractual terms that increases in the credit margin if the customer's earnings increases.

All equity instruments have contractual cash flows that do not pass the SPPI test. All such holdings are recognised at FVPL since the Bank has decided not to use the option to designate equity instruments at FVOCI.

The expected credit loss impairment model

Impairments for expected credit losses apply to financial assets recognised at amortised cost or at fair value through other comprehensive income, lease receivables and certain loan commitments and financial guarantee contracts. For financial assets recognised at amortised cost, expected credit losses are recognised in the income statement and set off against the asset in the balance sheet. However, on loan commitments and financial guarantee contracts, expected credit losses are recognised as a liability. For financial assets recognised at fair value through other comprehensive income, the expected credit losses are recognised in the income statement and set off against other comprehensive income since such assets are recognised at fair value on the balance sheet.

The impairment for expected credit losses depends on whether the credit risk has increased significantly since initial recognition and follows a three stage model:

- Stage 1: If the credit risk has not increased significantly, the impairment equals the expected credit losses resulting from default events that are possible within the next 12 months;
- Stage 2: If the credit risk has increased significantly, the financial assets are transferred to 'stage 2' and an impairment equal to the lifetime-expected credit losses is recognised; and
- Stage 3: If a financial asset is in default or otherwise credit impaired, it is transferred to 'stage 3', which is the same as stage 2, except that interest income is recognised on the net carrying amount.

The assessment of whether credit risk has increased significantly since initial recognition is performed by considering the change in the risk of default occurring over the remaining life of the instrument rather than by considering the increase in expected credit losses. A financial asset is transferred from stage 1 to stage 2 based on observed increases in the probability of default (PD):

- For facilities originated below 1% in PD: An increase in the facility's 12-month PD of at least 0.5 percentage points since origination and a doubling of the facility's lifetime PD since origination; and
- For facilities originated above 1% in PD: An increase in the facility's 12-month PD of 2 percentage points since origination or a doubling of the facility's lifetime PD since origination.

Further, financial assets that are more than 30 days past due are moved into stage 2. Finally, customers subject to forbearance measures are placed in stage 2, if the Bank in the most likely outcome expects no loss or the customers are in the 2-year probation period for performing forborne exposures.

The major change from IAS 39 is the calculation of expected credit losses (either as 12 months expected credit losses or lifetime expected credit losses depending on whether facilities are at stage 1, 2 or 3) and the inclusion of forward-looking elements.

The expected credit loss is calculated on all individual exposures as a function of the probability of default (PD), the exposure at default (EaD) and the loss given default (LGD). In general, the Bank's IFRS 9 impairment models and parameters draw on the Bank's existing internal models in order to ensure alignment of models across the Bank. New models and calculations have been developed especially for IFRS 9 purposes including models for lifetime PD, prepayment, and forward-looking LGD.

The lifetime expected credit losses cover the expected remaining lifetime of an instrument. For most instruments, the expected lifetime is limited to the remaining contractual maturity and adjusted for expected prepayment. For exposures with weak credit quality, the likelihood of prepayment is not included. For instruments that include both a loan and an undrawn commitment and where a contractual ability to demand prepayment and cancellation of the undrawn commitment do not limit the Bank's exposure to credit losses to the contractual notice period, the expected lifetime is the period during which the Bank expects to be exposed to credit losses. This period is estimated on the basis of the normal credit risk management actions. Products identified as in scope of an expected lifetime longer than the remaining contractual maturity include credit cards, overdraft balances and certain revolving credit facilities.

38. Implementation of IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with customers (continued)

The expected credit loss impairment model (continued)

The forward-looking elements of the calculation reflect the current unbiased expectations of the Bank's senior management. The process consists of the creation of macroeconomic scenarios (base case, upside and downside) including an assessment of the probability for each scenario, the review and sign-off of the scenarios (throughout the organisation) and a process for adjusting scenarios given new information during the quarter. Management's approval of scenarios can include adjustments to the scenarios, probability weighting and management overlays to cover the outlook for particular high-risk portfolios, which are not provided by the Bank's economist. The approved scenarios are used to calculate the impairment levels. Technically, the forward looking information is used directly in the PD's through an estimate of general changes to the PDs and the LGDs in the expected credit loss calculation. However, for significant exposures at stage 3, an individual assessment of the scenarios, changes to expected credit losses and the related probabilities are performed by senior credit officers.

The definition of default used in the measurement of expected credit losses and the assessment to determine movements between stages will be consistent with the definition of default used for internal credit risk management purposes and is aligned with CRR. Hence, exposures which are considered to be in default for regulatory purposes will always be considered stage 3 under IFRS 9. This applies to both 90-days-past-due considerations and unlikely-to-pay factors leading to a regulatory default.

All impairments will be allocated to individual impairments and the Bank will cease to recognise collective impairments under IFRS 9. Existing collective impairments aimed at capturing specific high-risk areas are incorporated as forward-looking elements into the individual expected credit loss calculation

Changes and impact on the Bank's Financial Statements from IFRS 15

On 1 January 2018, the Bank will adopt IFRS 15 Revenue from Contracts with Customers issued by IASB in May 2014. Applying the standard will have no effect on the Group's retained earnings or opening balance at 1 January 2018. Most of the Bank's revenue, including net interest income, is not impacted by the implementation of IFRS 15. The Bank's current accounting for revenue from contracts with customers complies with the new accounting policy after IFRS 15.

39. Management of risk and types of risk

a) Management of risk

Financial services organisations face an array of risks. Management of such risks is fundamental to the Bank as a Northern Ireland financial services provider and an essential element of the Bank's overall strategy.

The Risk Management Framework is designed to direct risk management activities and behaviours in the Bank, and defines the Bank's key risk frameworks and policies, the linkages between them and how they have been embedded throughout the Three Lines of Defence model (3LoD).

A sound risk management framework is a pre-requisite for an effective assessment of the Bank's overall risk. The framework supports strategic risk decision making, and assists the Risk Management function fulfil its vision "To deliver a forward looking, dynamic risk culture that helps the Bank to be recognised as the best bank in Northern Ireland".

The framework presents all risks identified in the Bank's business activities, allowing the Bank to focus risk mitigation techniques on risk- related business activities. It supports the Internal Capital Adequacy Assessment Process (ICAAP), which ensures an adequate allocation of capital to cover the Bank's total risk exposure.

The framework, with the ICAAP, provides the Bank's Board of Directors (the Board) with clear line of sight of all risk policies for all material risk types.

Corporate Governance Framework (CGF)

The Board is responsible for the overall sound business and risk management of the Bank and for ensuring that it acts in the best interests of shareholders and customers. Good corporate governance and effective risk management is a fundamental part of the culture and operations of the Bank and is an essential element of the Bank's strategy.

The CGF is comprised of the key governing committees that direct the Bank's activities and is supported by the risk tools, policies and procedures the Bank

The Board determines the overall risk management framework of the Bank and has, through the Chief Executive Officer (CEO) and the All Risk Management Committee (ARMC), delegated the implementation of the risk management framework to the individual governing committees. As a result individual committees are responsible for recommending the Bank's risk appetite to the Board, as well as risk identification, assessment, control and monitoring in respect of the specific risk categories delegated to that committee.

The Banks' Executive Committee (ExCo) (through the ARMC) and the Board challenge and approve the risk appetite and underlying risk management framework developed by the governing committees.

The Board of Directors (Board)

The Board is responsible for determining the strategic direction of the Bank and for creating the environment and structures for risk management to operate effectively. It ensures that management have established effective and proper procedures to achieve corporate goals and to comply with regulatory requirements, internal risk management and compliance policies and procedures. The Board has established the Bank's overall risk appetite as well as risk appetite statements for material risks.

39. Management of risk and types of risk (continued)

a) Management of risk (continued)

Board Audit Committee (BAC)

The Board Audit Committee of the Board of Directors is instrumental in the Board's fulfilment of its oversight responsibilities relating to:
- the integrity of the Bank's Financial Statements;
- risk management and internal control;
- the Bank's compliance with legal and regulatory requirements;
- the qualifications, independence and performance of the Bank's external auditor;
- monitoring the performance of the Bank's internal audit function and;
- the business practices and ethical standards of the Bank.

During 2017, the Audit Committee met four times. In the Chairman's report, tabled on 24th October, it was confirmed that all its responsibilities had been fulfilled via consideration, and approval where appropriate, of the various papers and items tabled. The Committee has also considered the independence of the audit function and has no concerns in this regard.

Board Risk Committee (BRC)

The Risk Committee of the Board of Directors is instrumental in the Board's fulfilment of its oversight responsibilities relating to:
- the Bank's overall risk profile and risk appetite, being the extent and types of risks that the Board considers acceptable for the Bank, keeping in mind current and potential risks and the operating environment;
- the Bank's risk culture;
- the Bank's compliance with legal and regulatory requirements and best practice in risk matters and internal control;
- approving the adequacy and effectiveness of the Bank's risk management framework which shall cover principles, policies, guidelines, instructions, methodologies, systems, processes, procedures and people;
- monitoring the robustness and application of the policies and processes for identifying and assessing business risks and the management of those risks by the Bank.
- in particular, but not exclusively the BRC is responsible for oversight of risk relating to capital and liquidity, credit and impairments, whistleblowing, regulation and anti money laundering, IT and related security risks.

Board Remuneration Committee (RemCo)

The Remuneration Committee of the Board of Directors is instrumental in the Board's fulfilment of its governance responsibilities relating to:
- approval of the remuneration policy of the Board;
- assurance on an annual basis of compliance with the remuneration policy;
- awareness of and provision of advice to the Board on major changes to employee benefits;
- overviewing and recommending approval of the remuneration of the CEO and Code Staff;
- overviewing the KRAs (Key Result Area) and KPIs (Key Performance Indicators) of the CEO and Code Staff by reference to corporate goals and objectives resolved by the Board;
- consideration of and recommending for approval the compensation payable to the CEO and Code Staff in connection with any loss or termination of office or early retirement arrangements;
- agreeing the policy for authorising expenses for the CEO;
- ensuring no Director, Senior Executive or member of Code Staff is involved in deciding their own remuneration; and
- reviewing the content of the Directors' emoluments note in the annual report and accounts for submission to the Board as a whole.

The Executive Committee (ExCo)

ExCo is responsible for the strategic and day to day operational management of the Bank. Within this remit, ExCo implements the Bank's business strategy, provides oversight of the Bank's systems and controls, determines the Bank's priorities and targets and manages the Bank's resources. In broad terms the ExCo will:
- recommend and implement strategy;
- manage priorities, targets and resources;
- share key strategic and operational management information;
- ensure the core values are embedded in the organisation; and
- consider the risk of treating customers unfairly or delivering inappropriate outcomes.

Risk governing committees

The Bank operates under an enterprise risk management framework that is designed to identify, assess, measure and manage its exposures to risks.

The Bank has various risk governance committees which are each responsible for specific risk areas within the Bank. The CEO through the All Risk Management Committee (ARMC) is responsible for the oversight and management of the underlying committees and the overall risks to which the Bank is exposed.

The ARMC is a sub-committee of ExCo. The purpose of ARMC is to provide oversight and take overall responsibility for the risks associated with the Bank ensuring the risks are managed within the Bank's risk appetite. Whilst not replacing the individual risk governing committees, the ARMC ensures an appropriate enterprise risk view is provided for emerging and existing risks, both across the business units and within the industries that may impact on the Bank and from a Danske Bank Group (the Group) risk perspective.

39. Management of risk and types of risk (continued)

a) Management of risk (continued)

Risk governing committees (continued)

The ARMC has delegated individual risk categories to the following key governing committees:

Risk Committee	*Type of Risk*
Operational Risk and Compliance Committee	Operational risk (excluding IT risk) Regulatory risk
Information Technology Risk Committee	IT risk and security
Asset and Liability Committee	Liquidity risk Interest rate risk in the Banking Book Market risk Capital adequacy risk
Credit Oversight Forum	Credit risk Concentration risk Residual risk
Commercial and Pricing Committee	Business risk Reputational risk
Change Control Committee	All risks in relation to projects
Pension Risk Committee	Pension obligation risk

The 'Three Lines of Defence' concept (3LoD)

The Bank's risk structure is based on the 3LoD concept. An effective risk framework is not limited to the risk function but requires a comprehensive risk management structure and culture throughout the Bank:

- the business is the first line of defence and primary accountability for risk management lies with the business, it should have sufficient controls in place to demonstrate a strong risk management framework in its own right;

- Risk Management department is the main second line of defence and is responsible for the independent oversight of risk and the provision of a suitable Bank wide risk management framework (subject to the exclusions noted for specialist business units); and

- the third line of defence is Internal Audit which undertakes independent assessment of the risk framework and control environment providing assurance to the Board.

Risk Appetite Framework (RAF)

The RAF sets out the Board Risk Committee approved risk appetite which, in turn, drives business unit and risk owner risk appetites across the Bank. The RAF defines Board risk limits and tolerances as well as high level risk principles defining the Board's core risk ethos.

The Bank's Risk Appetite Framework comprises:

- *High level risk principles*

These principles are a qualitative statement of the Board's core risk ethos with the Board:
- having a conservative risk appetite reflected through the implementation of specific risk limits. The Board seeks that the Bank, at all times, has optimal control of all types of risk to ensure a stable basis for the Bank's future development;
- responsible for the overall sound business and risk management of the Bank and for ensuring that it acts in the best interests of shareholders and treats customers fairly and delivering good customer outcomes;
- supporting the promotion of an acceptable level of regulatory risk;
- viewing good corporate governance and effective risk management as a fundamental part of the culture and operations of the Bank and an essential element of the Bank's strategy; and
- approving the three lines of defence model which includes placing primary risk ownership with the business units and independent risk oversight with Risk Management; with Internal Audit assessing the risk framework and internal control environment.
- control operational risks within tolerances set to ensure that financial or non-financial exposures do not cause material damage to the Group and manage operational risk based on realistic trade off decisions between the cost of mitigating a risk and the potential loss of accepting risk without mitigation;

39. Management of risk and types of risk (continued)

a) Management of risk (continued)

Risk Appetite Framework (RAF) (continued)

- *High level financial principles (continued)*

These principles are a qualitative statement, setting out the broad parameters within which the Board seeks that management guides the business with the focus to be on:
- Financial Performance: generating a strong financial performance;
- Cost Management: maintaining a strong control of discretionary costs, and FTEs, and attracting customers towards lower cost to serve distribution channels and;
- Capital Management: maintaining a strong capital position that is able to withstand severe stress tests, meet the regulatory requirements and the Bank's own risk appetite, while seeking to maximise the return on capital.

- *Strategic boundaries*

These boundaries are a qualitative statement, setting out the broad parameters within which the Board seeks that management guides the business with the focus to be on:
- Personal Customers: aiming to be the first choice for affluent and mass affluent personal customers, the Bank will operate mainly in Northern Ireland. In the personal market, the Bank will focus on maintaining an appropriate level of deposits and acquisition of current accounts, mortgages and private banking. Any growth of the personal loan and credit card portfolios will be on the basis of acceptable credit quality;
- Business Customers: aiming to be the first choice for top business customers the Bank will operate mainly in Northern Ireland. Lending acquisition will focus on SME and corporate acquisition, with no appetite for complex high risk based lending relationships;
- Credit: maintaining a sound credit quality that is higher than the local average in the Northern Ireland market and improving credit expertise generally among employees;
- Information Technology (IT): aiming to develop, deliver and maintain effective IT solutions that make the Bank the first choice for technologically literate customers. At the same time the Bank's IT infrastructure and systems are to be resilient, recoverable and secure, with successful change control processes minimising the risk of incidents impacting on availability of service; and
- People: aiming to attract, develop and retain high performing motivated people who feel encouraged to create sustainable results. Focus will remain on offering a competitive employee value proposition that links shareholder and employee interests. At the same time ensuring that our employees are appropriately skilled and display behaviours in line with our Code of Conduct.

- *Risk limits and tolerances*

These quantitative risk appetite measures articulate the Bank's risk appetite, linking the above principles and boundaries with actual risk taking activities.

The measures in place for all key risk classes, are articulated at length in the ICAAP and Risk Management Framework, and the key targets are reported to the Board.

Risk Identification Assessment (RIA)

Risk Management has overall responsibility for the RIA framework. It provides business units with advice and guidance in relation to the implementation, completion and maintenance of their RIA. In addition, it advises the business in the formation of risk strategies and shares industry information with the business as appropriate.

The RIA is conducted on an ongoing basis with a view to identifying all material risks the Bank is subject to through its products, systems, activities and external events. The RIA bases the risk assessment on four parameters: likelihood, consequence, reputational and financial impacts on an extreme case loss on a 20 year time horizon.

We prioritise the highest inherent risks for a residual risk assessment and identify key causes of each prioritised risk. We undertake a control effectiveness review and report key findings to the relevant committee for oversight.

b) Types of risk

The Bank is exposed to a number of risks which are reviewed in the Strategic Report.

40. Credit risk disclosures

Credit Exposure

Credit exposure consists of balance sheet items and off-balance-sheet items that carry credit risk. Most of the exposure derives from lending activities in the form of secured and unsecured loans. The overall management of credit risk covers credit risk from direct lending activities, counterparty risk on derivatives and credit risk from security positions.

Breakdown of credit exposure

At 31 December 2017	Lending activities	Counterparty risk derivatives	Inter group	Other	Total
	£'000	£'000	£'000	£'000	£'000
Balance sheet items					
Balances at central bank	1,265,500	-	-	-	1,265,500
Items in the course of collection from other banks	55,463	-	-	-	55,463
Due from other banks	19,855	-	32,161	-	52,016
Trading portfolio assets	-	7,258	-	-	7,258
Investment securities- held to maturity	-	-	-	637,310	637,310
Investment securities- available for sale				370,629	370,629
Loans and advances at amortised cost	5,422,293	-	-	-	5,422,293
Investment in subsidiaries	-	-	250	-	250
Off-balance sheet items					
Guarantees	104,965	-	-	-	104,965
Irrevocable loan commitments shorter than 1 year	584,774	-	-	-	584,774
Irrevocable loan commitments longer than 1 year	270,100	-	-	-	270,100
Total	7,722,950	7,258	32,411	1,007,939	8,770,558

At 31 December 2016	Lending activities	Counterparty risk derivatives	Inter group	Other	Total
	£'000	£'000	£'000	£'000	£'000
Balance sheet items					
Balances at central bank	1,491,803	-	-	-	1,491,803
Items in the course of collection from other banks	53,916	-	-	-	53,916
Due from other banks	14,949	-	7,153	-	22,102
Trading portfolio assets	-	15,084	-	-	15,084
Investment securities- held to maturity	-	-	-	817,434	817,434
Loans and advances at amortised cost	5,094,188	-	-	-	5,094,188
Investment in subsidiaries	-	-	250	-	250
Off-balance sheet items					
Guarantees	90,438	-	-	-	90,438
Irrevocable loan commitments shorter than 1 year	394,952	-	-	-	394,952
Irrevocable loan commitments longer than 1 year	174,355	-	-	-	174,355
Total	7,314,601	15,084	7,403	817,434	8,154,522

40. Credit risk disclosures (continued)

Breakdown of credit exposure (continued)

Credit exposure from lending activities

Credit exposure from lending activities in the Bank's banking business includes loans, amounts due from credit institutions and central banks, guarantees and irrevocable loan commitments. The exposure is measured net of accumulated impairment charges and includes repo loans. For reporting purposes, all collateral values are net of haircuts and capped at the exposure amount.

Classification of customers

The main objectives of risk classification are to rank the Bank's customers according to risk and to estimate each customer's probability of default (PD). As part of the credit process, the Bank classifies customers according to risk and updates their classifications upon receipt of new information. Risk classification comprises rating and credit scoring of customers.

The Bank has developed a number of classification models to assess customer PD and to classify customers in various segments. Large business and financial customers are classified on the basis of rating models, while small business and personal customers are classified by means of scoring models.

In its credit risk management, the Bank uses point-in-time (PIT) PD estimates for risk classification. These PIT PD estimates express a customer's probability of default in the current economic situation. The Bank's classification scale consists of 11 main rating categories with fixed PD bands. During a downturn, a customer's PIT PD may increase, and the customer may migrate to a lower rating category. The effect from a downturn is thus larger when PIT PD is used than if the classification were based on through-the-cycle (TTC) PD, which the Bank uses to calculate the risk of exposure amount for credit risk.

Loans to customers for which objective evidence of impairment exists are placed in rating category 10 or 11, including loans for which no impairment charges have been recognised, for example, because adequate collateral has been provided.

At 31 December 2017, the exposure-weighted average PD was 1.04%, against 2.15% in 2016.

Credit portfolio broken down by rating category

	31 December 2017				31 December 2016			
	Gross exposure	**Impairment charges**	**Net exposure**	**Net exposure, ex collateral**	Gross exposure	Impairment charges	Net exposure	Net exposure, ex collateral
	=a+b	b	a		=a+b	b	a	
	£'000	**£'000**	**£'000**	**£'000**	£'000	£'000	£'000	£'000
Rating Category								
1	**78,317**	**-**	**78,317**	**3,071**	10,402	-	10,402	2,975
2	**1,987,238**	**-**	**1,987,238**	**1,667,407**	2,087,002	1	2,087,001	1,980,924
3	**489,183**	**-**	**489,183**	**126,322**	502,664	4	502,660	181,171
4	**1,015,275**	**4**	**1,015,271**	**402,509**	940,664	-	940,664	388,699
5	**1,029,902**	**1**	**1,029,901**	**337,276**	811,858	-	811,858	267,419
6	**1,037,049**	**2,515**	**1,034,534**	**387,392**	817,750	7,256	810,494	266,468
7	**1,311,651**	**2,546**	**1,309,105**	**526,329**	1,201,808	1,364	1,200,444	299,382
8	**454,555**	**354**	**454,201**	**133,437**	544,811	3,134	541,677	142,794
9	**64,218**	**62**	**64,156**	**19,116**	64,949	-	64,949	15,971
10	**119,129**	**15,457**	**103,672**	**25,821**	279,154	32,188	246,966	42,067
11	**227,550**	**70,177**	**157,373**	**78,014**	200,006	102,520	97,486	15,977
Total	**7,814,066**	**91,116**	**7,722,950**	**3,706,696**	7,461,068	146,467	7,314,601	3,603,847

40. Credit risk disclosures (continued)

Credit exposure broken down by industry

The table below breaks down credit exposure by industry. The industry segmentation follows the classification principles of the Statistical Classification of Economic Activities in the European Community (NACE) Standard.

	31 December 2017				31 December 2016			
	Gross exposure	Impairment charges	Net exposure	Net exposure, ex collateral	Gross exposure	Impairment charges	Net exposure	Net exposure, ex collateral
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Public institutions	1,618,678	73	1,618,605	1,616,355	1,887,852	28	1,887,824	1,885,615
Agriculture	548,970	3,049	545,921	165,864	561,442	10,606	550,836	151,140
Commercial property	754,868	22,195	732,673	173,848	718,880	55,669	663,211	159,994
Non-profit and associations	524,304	1,722	522,583	239,213	432,420	1,651	430,769	202,276
Personal customers	2,419,783	26,661	2,393,122	469,514	2,104,034	31,203	2,072,831	356,229
Business customers	1,927,162	36,598	1,890,564	1,022,556	1,738,109	47,310	1,690,799	830,314
Other	20,300	819	19,481	19,346	18,331	-	18,331	18,279
Total	7,814,066	91,116	7,722,950	3,706,696	7,461,068	146,467	7,314,601	3,603,847

Concentration risk

The Bank has implemented a set of frameworks to manage concentration risk encountered by the Bank. These frameworks improve risk control limits and guide points which cover single-name borrower concentration, industry sector concentration and geographical concentration.

These limits are set as part of the Bank's credit risk appetite and form part of the Bank's risk strategy.

Industry sector concentration

The Industry Concentration Framework outlines the principles of managing industry exposures and includes various sector caps or limits to be observed in relation to lending within the major industry sectors. These controls are established by senior personnel within the Bank's business units, Credit and Risk Management departments and are approved by the Bank's Board as part of the credit risk appetite process.

Geographical concentration

The Country Risk Framework outlines the principles of managing country exposures. The Bank's strategy is to target markets in which it has the greatest understanding and experience and therefore the Bank accepts its geographical concentration in Northern Ireland as being within its risk appetite as this risk is inherent to the Bank's business model.

Single-name borrower concentration

The Bank has set internal limits regarding its maximum exposure to a single name in the context of the total customer lending and the Bank's total regulatory capital. The Bank's performance against the concentration risk control limits detailed above is reported to the Bank's internal credit risk governance committee and the Board.

40. Credit risk disclosures (continued)

Collateral

The Bank uses a number of measures to mitigate credit risk, including collateral, guarantees and covenants. The main method is obtaining collateral.

The market value of collateral is monitored and evaluated by advisers, internal or external assessors, or automatic valuation models. Automatic valuation models are validated annually and monitored quarterly. The Bank regularly evaluates the validity of external inputs on which the valuation models are based. The collateral system supports the process of reassessing the market value to ensure that the Bank complies with regulatory requirements.

The market value of collateral is subject to a haircut. The haircut reflects the risk that the Bank will not be able to obtain the estimated market value upon the sale of the individual asset in a distressed situation and thus includes forced sale reduction, price volatility during the sales period, realisation costs and maintenance costs. The haircut applied depends on the type of collateral.

The composition of the Bank's collateral base reflects the product composition of the credit portfolio. The most important collateral type, measured by volume, is real estate/property. For reporting purposes, all collateral values are net of haircut and capped by the exposure amount at facility level.

Collateral value by type (after haircut)

	2017	2016
	£'000	£'000
Real estate/property		
Personal	**1,922,126**	1,714,857
Commercial	**1,230,293**	1,220,078
Agricultural	**364,732**	365,134
Equipment	**350,340**	225,064
Guarantees	**1,992**	4,186
Deposits	**43,475**	19,098
Other assets	**103,281**	161,795
Total collateral	**4,016,239**	3,710,212
Total unsecured credit exposure	**3,706,711**	3,604,389
Unsecured portion of credit exposure (%)	**48%**	49%

Past due amounts (no evidence of impairment)

	Total past due amounts		**Total due under loans**	
	2017	2016	**2017**	2016
	£'000	£'000	**£'000**	£'000
6-30 days	**911**	255	**8,038**	5,406
31-60 days	**88**	364	**5,358**	4,227
> 60 days	**667**	1,157	**4,055**	1,865
Total past due amounts	**1,666**	1,776		
Total due under loans			**17,451**	11,498

Measurement of credit risk

Credit grading and scoring systems facilitate the early identification and management of any deterioration in loan quality. The following credit classifications have been used:

Good upper:	Strong credit with no weakness evident.
Good lower:	Satisfactory credit with weakness evident.
Marginal:	The credit is exhibiting weakness but with the expectation that existing debt can be fully repaid from normal cash flows.
Vulnerable:	Credit where repayment is in jeopardy from normal cash flows and may be dependant on other sources.
Impaired:	A loan is impaired if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event/events has an impact such that the present value of future cash flows is less than the current carrying value of the financial asset or group of assets and requires an impairment provision to be recognised in the income statement.

40. Credit risk disclosures (continued)

Measurement of credit risk (continued)

The portfolio of good, marginal, vulnerable and impaired loans and advances to customers (pre impairment provisions) is as follows:

Neither past due nor impaired

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2017	2017	2017	2017	2017
	£'000	£'000	£'000	£'000	£'000
Good upper	1,413,830	47,638	226,860	1,137,051	2,825,379
Good lower	564,870	29,355	391,941	869,655	1,855,821
Marginal	124,129	19,295	77,823	149,801	371,048
Vulnerable	11,496	924	18,316	19,481	50,217
Total : Neither past due nor impaired	2,114,325	97,212	714,940	2,175,988	5,102,465

Neither past due nor impaired

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2016	2016	2016	2016	2016
	£'000	£'000	£'000	£'000	£'000
Good upper	918,211	38,682	235,603	1,127,205	2,319,701
Good lower	755,896	39,389	307,542	782,528	1,885,355
Marginal	187,364	21,319	124,945	167,208	500,836
Vulnerable	24,007	1,619	11,949	19,625	57,200
Total : Neither past due nor impaired	1,885,478	101,009	680,039	2,096,566	4,763,092

Six days plus past due not impaired

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2017	2017	2017	2017	2017
	£'000	£'000	£'000	£'000	£'000
Good upper	1,686	118	3,000	69	4,873
Good lower	1,444	254	64	1,662	3,424
Marginal	2,120	323	174	1,663	4,280
Vulnerable	157	79	368	56	660
Total : Days past due not impaired	5,407	774	3,606	3,450	13,237

Six days plus past due not impaired

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2016	2016	2016	2016	2016
	£'000	£'000	£'000	£'000	£'000
Good upper	625	66	85	18	794
Good lower	1854	348	2147	1925	6274
Marginal	711	300	190	1046	2247
Vulnerable	1170	65	407	542	2184
Total : Days past due not impaired	4,360	779	2,829	3,531	11,499

40. Credit risk disclosures (continued)

Measurement of credit risk (continued)

	Mortgages	**Other Personal**	**Property & Construction**	**Non Property Business**	**Total**
	2017	**2017**	**2017**	**2017**	**2017**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Impaired	**70,575**	**54,643**	**164,157**	**107,513**	**396,888**

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2016	2016	2016	2016	2016
	£'000	£'000	£'000	£'000	£'000
Impaired	62,357	38,751	167,178	196,487	464,773

Gross loans and receivables

	Mortgages	**Other Personal**	**Property & Construction**	**Non Property Business**	**Total**
	2017	**2017**	**2017**	**2017**	**2017**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Good Upper	**1,415,516**	**47,756**	**229,860**	**1,137,120**	**2,830,252**
Good Lower	**566,314**	**29,609**	**392,005**	**871,317**	**1,859,245**
Marginal	**126,249**	**19,618**	**77,997**	**151,464**	**375,328**
Vulnerable	**11,653**	**1,003**	**18,684**	**19,537**	**50,877**
Impaired	**70,575**	**54,643**	**164,157**	**107,513**	**396,888**
Gross loans and receivables	**2,190,307**	**152,629**	**882,703**	**2,286,951**	**5,512,590**

Gross loans and receivables

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2016	2016	2016	2016	2016
	£'000	£'000	£'000	£'000	£'000
Good Upper	918,836	38,748	235,688	1,127,223	2,320,495
Good Lower	757,750	39,737	309,689	784,453	1,891,629
Marginal	188,075	21,619	125,135	168,254	503,083
Vulnerable	25,177	1,684	12,356	20,167	59,384
Impaired	62,357	38,751	167,178	196,487	464,773
Gross loans and receivables	1,952,195	140,539	850,046	2,296,584	5,239,364

Forbearance

Forbearance occurs when a concession is made on the contractual terms of a loan in response to the actual or apparent financial stress of a borrower with the purpose of avoiding default, foreclosure or repossession. The Bank operates a policy of providing forbearance to its customers when it is appropriate to the individual's circumstances. The concession can be granted on a permanent or temporary basis following an assessment of the customer's individual circumstances and ability to pay.

The Bank operates a range of forbearance measures across its retail home loan portfolio when customers have been identified as experiencing, or likely to experience, a period of financial difficulty or distress. The Bank considers that forbearance takes place when a concession is granted to a customer with affordable terms and conditions that are more suitable to the customer's current circumstances than those originally contracted for. The Bank remains committed to ensuring that any forbearance strategy agreed with the customer is both affordable and sustainable for the customer with the ultimate aim of minimising the risk of losses for the Bank and its customers.

The Bank makes every effort to follow its principles of treating customers fairly by working with customers at as early a stage as possible in times of distress in order to find a mutually acceptable solution for both the customer and the Bank.

40. Credit risk disclosures (continued)

Forbearance (continued)

The Bank utilises a range of forbearance measures for retail home loan customers which are in arrears or facing potential arrears on contractual loan repayments, determined on a case by case basis.

The type of forbearance offered by the Bank normally falls into three types or strands:

Variation forbearance

In this case, the Bank may consider a temporary variation to the customer's contract with the Bank for an agreed period of time. This may be appropriate where the financial hardship experienced by the customer is deemed to be temporary in nature. After the agreed period of forbearance, it would be expected that the customer would return to the terms of their existing contract with the Bank.

Renegotiation forbearance

This involves a renegotiation of the customer's contract with the Bank, following normal credit assessment, which can include a change to one or more of the following:
- structure;
- repayment amount;
- interest rate;
- term; and
- collateral.

Post default mutual agreement

This is applicable to customers who have defaulted and the Bank seeks to put in place a mutually acceptable arrangement with the customer to avoid repossession. This may include one or more of the following:
- accepting an agreed minimum payment over a period of time pending receipt of funds to repay the debt from a defined source e.g. pending receipt of a lump sum; and
- providing the customer with time to effect a voluntary sale of the property.

Retail home loans subject to forbearance are of low financial significance in the context of the Bank's overall portfolio. The table below summarises the forbearance arrangements in place together with the loan balances and impairment provisions associated with those arrangements.

A small number of customers have agreed a range of forbearance arrangements with the Bank on their loan arrangements. For disclosure purposes, such customers have been categorised under their primary forbearance arrangement.

Where a customer has unsecured personal borrowings of £1,000 or more, the normal approach would be to restructure the debt into a personal loan if affordability can be demonstrated in line with normal criteria. In these cases the personal loan is not considered a forbearance case.

Where a customer has unsecured personal borrowings of less than £1,000 and is experiencing difficulties the main solution is to agree a repayment plan with the customer to repay the debt over a period of time. The Bank has a small number of such arrangements.

In addition forbearance measures are provided to 22 non defaulted business customers as at 31 December 2017, having associated facilities of £27,600,000.

	Number of loans	Loan balance £'000	% of total mortgage portfolio	Impairment allowance £'000	Coverage %
At 31 December 2017					
Variation to the customer's existing contract with the Bank	**40**	**6,139**	**0.3%**	**179**	**2.9%**
Renegotiation	**5**	**322**	**0.0%**	**13**	**4.0%**
Post default mutual agreement	**23**	**877**	**0.0%**	**51**	**5.8%**
	68	**7,338**	**0.3%**	**243**	**3.3%**
At 31 December 2016					
Variation to the customer's existing contract with the Bank	54	10,860	0.5%	995	9.2%
Renegotiation	15	2,024	0.1%	158	7.8%
Post default mutual agreement	7	873	0.0%	103	11.8%
	76	13,757	0.6%	1,256	9.1%

40. Credit risk disclosures (continued)

Forbearance (continued)

Non performing loans

	2017 £'000	2016 £'000
Loans and advances to customers	173,055	208,116
Provisions	(85,860)	(95,490)
Total	87,195	112,626

Impairment provisions

Rating categories 10 (non default) and 11 (default) include customers with exposures for which objective evidence of impairment exists. Exposure to customers in the other rating categories is subject to collective impairment testing.

The allowance account comprises all impairment charges against loans and advances at amortised cost, amounts due from credit institutions and central banks, and loan commitments and guarantees.

Allowance account broken down by type of impairment

	Specific 2017 £'000	Collective 2017 £'000	Total Allowance 2017 £'000	Specific 2016 £'000	Collective 2016 £'000	Total Allowance 2016 £'000
Opening balance	134,894	11,573	146,467	261,279	17,045	278,324
Charge/(credit) for the year	(21,801)	(7,385)	(29,186)	(20,461)	(5,472)	(25,933)
Amounts written off	(27,050)	-	(27,050)	(104,730)	-	(104,730)
Recoveries of amounts written off in previous years	4,203	-	4,203	3,369	-	3,369
Foreign exchange and other movements	(3,318)	-	(3,318)	(4,563)	-	(4,563)
Closing balance	86,928	4,188	91,116	134,894	11,573	146,467

	2017 £'000	2016 £'000
Amounts included in		
Loans and advances to customers (Note 14)	90,297	145,173
Other liabilities (Note 24)	819	1,294
	91,116	146,467

Exposure to counterparty risk (derivatives) and credit exposure from other trading and investing activities

	2017 £'000	2016 £'000
Counterparty risk		
Derivatives with positive fair value	7,258	15,084
Credit exposure from other trading and investing activities		
Investments - held to maturity	637,310	817,434
Investments- available for sale	370,629	-
Investment in subsidiaries	250	250
Total	1,015,447	832,768

Bond portfolio

The investment portfolio is made up of European Union government securities on both a held to maturity and available for sale bases.

41. Related party transactions

(a) Transactions with Directors, Executive Committee members and their close family members

Directors, Executive Committee members, their close family members and companies which they control have undertaken the following transactions with the Bank in the normal course of business. The transactions were made on the same terms and conditions as applicable to other Bank employees, or on normal commercial terms.

	Persons 2017 Number	Amount 2017 £'000	Persons 2016 Number	Amount 2016 £'000
Loans - balance at 31 December				
Directors	3	7	3	10
Executive Committee	6	561	5	593
	9	568	8	603
Deposits - balance at 31 December				
Directors	5	965	5	968
Executive Committee	8	251	6	407
	13	1,216	11	1,375

No provisions have been recognised in respect of loans provided to Executive Committee members. Furthermore no debts were written off or forgiven during the year ended 31 December 2017 (2016: £Nil).

Included in the above are three loans (2016: three) totalling £7,000 (2016: £10,,000) made to Directors and companies which they control. The maximum aggregate amount outstanding during the year in respect of these loans was £14,000 (2016: £12,000).

(b) Interests

None of the Directors had any other disclosable interests in the shares or debentures of any UK group undertaking at the end of the year, or were granted or exercised any right to subscribe for shares in, or debentures of, any UK group undertaking during the year.

(c) Other related party transactions

In the normal course of business the Bank maintains accounts and conducts transactions with other members of the Danske Bank Group. This business is conducted at prevailing market rates and terms and includes deposits taken and placed, interest rate and foreign exchange swaps and the provision of technology and other services. The Bank has taken advantage of the exemption not to disclose full details of these transactions as the Bank is a wholly owned subsidiary of Danske Bank Group and the consolidated financial statements of the Danske Bank Group are publicly available.

The Bank has transactions with the Scheme detailed in Note 23. The Bank charges the Scheme with the cost of administration which amounted to £76,000 in the year ended 31 December 2017 (2016: £81,000).

42. Employees

The average number of full time equivalent UK employees of the Bank during the year was made up as follows:

	2017 Number	2016 Number
Managers	334	343
Clerical staff	959	924
	1,293	1,267

43. Share based payments

Until 2008 the Bank offered Executive Directors and senior managers incentive programmes that consist of Danske Bank A/S share options and conditional shares. During 2015, the last share options lapsed.

Effective from 2015, the Bank has granted rights to conditional shares - under the bonus structure for material risk takers - for part of their variable remuneration. Rights to Danske Bank A/S shares for material risk takers vest up to seven years after being granted, provided that the employee, with the exception of retirement, has not resigned from the Bank. In addition to this requirement and before pay-out of deferred shares, back testing is conducted to assess whether the initial criteria for granting the bonus are still considered fulfilled, whether the Danske Bank A/S' economic situation has deteriorated significantly and whether the individual has proven fit and proper. The fair value of the conditional shares is calculated as the share price at grant date less the payment made by the employee, if any.

	2017 Weighted average exercise price DKK	**2017 Number of conditional shares**	2016 Weighted average exercise price DKK	2016 Number of conditional shares
Outstanding at the beginning of the year	0.58	**19,582**	1.70	6,682
Granted during the year	0.00	**15,792**	0.00	24,533
Exercised during the year	0.00	**(4,335)**	0.00	(11,633)
Outstanding at the end of the year	0.37	**31,039**	0.58	19,582
Exercisable at the end of year	**-**	**-**	-	-

The weighted average share price at the date of exercise of the conditional shares during the year was DKK 248. The conditional shares at 31 December 2017 had a weighted average exercise price of DKK 0.37 and a weighted average remaining contractual life of 2.7 years. As at 31 December 2017 there were 31,039 conditional shares with an exercise price in the range of DKK Nil to DKK 1.7. In the year ended 31 December 2017, conditional shares were granted in April 2017. The estimated fair value of the conditional shares granted on this date was £445,000. The charge for the year in respect of share based payments was £850,000 (£291,000).

44. Ultimate parent undertaking

The ultimate parent undertaking, and ultimate controlling party, is Danske Bank A/S, a company incorporated in Denmark. This company also heads the smallest and the largest group in which the results of the Group are consolidated.

Copies of Danske Bank Group's financial statements may be obtained from Danske Bank A/S, Holmens Kanal 2-12, DK 1092, Copenhagen, Denmark.