Company Number: R0000568

NORTHERN BANK LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2019

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NORTHERN BANK LIMITED
Officers and Professional Advisers
For the year ended 31 December 2019

Directors	**Executive:**	Kevin Kingston	Chief Executive Officer
		Vicky Davies	Deputy Chief Executive Officer and Managing Director, Strategy and Corporate Development
		Stephen Matchett	Deputy Chief Executive Officer and Chief Financial Officer
	Non-executive:	Gerald Gregory*∞Ω	Chairman
		Berit Behring~ (Appointed 11 November 2019)	
		Michael Black*∞	
		Jim Ditmore~ (Resigned 5 September 2019)	
		Carsten Egeriis~	
		Astrid Grey*∞Ω (Appointed 28 February 2020)	
		Margaret Lesley Jones*∞Ω (Resigned 26 September 2019)	
		Paul Rooney∞Ω	
		Martin Stewart*∞Ω (Appointed 21 January 2020)	

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

Executive Committee	Kevin Kingston	Chief Executive Officer
	Vicky Davies	Deputy Chief Executive Officer and Managing Director, Strategy and Corporate Development
	Stephen Matchett	Deputy Chief Executive Officer and Chief Financial Officer
	Richard Caldwell	Managing Director, Personal Banking and Small Business
	Liam Curran	Chief Operating 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	
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 2019.

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 2019 Financial Statements have been prepared under International Financial Reporting Standards (IFRS).

Review of business

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.

Financial review

Key performance measures	**2019**	2018
Profit before tax - £m	**90.0**	88.8
Profit before loan impairments and tax as per the Income Statement - £m	**90.8**	91.7
Loan to deposit ratio* - %	**76%**	78%
Cost/income ratio** - %	**59%**	60%
Net interest margin*** - %	**2.15%**	2.23%

* *Customer loans divided by customer deposits*
** *Operating expenses divided by operating income*
*** *Net Interest income divided by average interest earning assets*

2019 financial performance

The Bank delivered a resilient performance during 2019. Profit before tax increased to £90.0m (2018: £88.8m) despite the ongoing low interest rate environment and continued uncertainty surrounding the UK's exit from the EU. The overall increase reflects a combination of lower costs and lower loan impairment charges. The profit attributable to the shareholders for the year ended 31 December 2019 amounted to £58.5m (2018: £64.7m).

Net interest income increased by 1% to £178.6m (2018: £177.4m), primarily driven by the positive impact of an increase in lending volume (3%) and deposit volume (7%). Such balance sheet growth and higher average UK interest rates (despite remaining low by historical standards) has resulted in the net interest margin staying broadly in line with the prior year at 2.2%. Retail customer activity levels remain satisfactory, supported by continued success of the Bank's mortgage finance proposition, although demand for new lending to businesses was subdued by Brexit uncertainty throughout 2019, with some larger customers delaying investment decisions.

Non interest income decreased by 5% to £56.8m (2018: £59.8m). Whilst trading income increased in 2019 to £10.4m (2018: £9.6m), fee and commission income decreased to £52.0m (2018: £56.5m) due to lower lending related fees. Operating expenses decreased by 2% to £139.7m (2018: £142.1m). The Bank continued to manage its cost base whilst investing in improved solutions and skills designed to ensure customers' expectations are fully met. Overall, the cost/income ratio decreased marginally to 59% (2018: 60%).

On 1 January 2019, the Bank adopted the accounting standard IFRS 16 'Leases'. The most significant impact of IFRS 16 to the Bank was the recognition of all material leases on balance sheet with a term greater than 12 months. On transition to IFRS 16, the Bank recognised a transitional adjustment for such right-of-use asset of £8.3m, with a corresponding amount recognised as financial lease liabilities. Consequently, the 2019 depreciation charge has increased to £4.9m (2018: £3.5m) as depreciation expenses are recognised on these assets, offset by a reduction in operating lease costs.

The continued improvement in collateral values and a stable trading performance during 2019 was reflected in impairments, with the recognition of a net loan impairment charge for the year ended 31 December 2019 of £0.8m (2018: £2.9m). The application of forward looking macro-economic scenarios and assumptions at 31 December 2019 within the Bank's 'expected credit loss' model continues to reflect a level of economic uncertainty following the UK's exit from the European Union (EU) on 31 January 2020 as the UK Government enters into negotiations with the EU around the terms of their future trading relationship. However, the downside macro economic scenario applied at 31 December 2019 pushes out the most significant negative economic impacts that would be associated with the UK not reaching a free trade agreement with the EU until after the transition period ends.

The Bank's effective tax rate for the year ended 31 December 2019 was 28.8% (2018: 21.0%). The primary drivers for the increased effective tax rate was the de-recognition in the level of the deferred tax asset relating to tax losses brought forward from previous years and a change in the treatment of interest deduction for certain capital instruments. Excluding these, the adjusted effective tax rate for the year ended 31 December 2019 would have been 24.4% (2018: 24.5%).

Review of business (continued)

2019 financial position

Both customer lending and deposit volumes increased during 2019. Overall customer lending increased by 3% to £6.1bn (2018: £5.9bn) and customer deposits increased by 7% to £8.1bn (2018: £7.6bn). The loan-to-deposit ratio decreased marginally to 76% (2018: 78%). We remain well positioned for any increased demand for credit.

The Bank continued to increase its portfolio of investment securities held during 2019 with £1.3bn held at 31 December 2019 (2018: £1.2bn). Cash and balances at central bank increased to £2.2bn at 31 December 2019 (2018: 2.0bn). Consequently the Bank continues to report a strong liquidity position.

The funded status of the defined benefit pension scheme was a surplus of £195.9m at 31 December 2019 (2018: £150.3m). The scheme surplus increased during the year primarily due to the increase in the value of the pension assets, partly offset by an increase in the value of the pension liabilities as a result of the fall in the discount rate applied.

A property revaluation at 30 June 2019 was undertaken by external valuers and this increased the carrying value of properties by £0.3m. The previous property valuation was at 30 June 2018. During 2019 the Bank disposed of one property (2018: one property) and has two properties held for sale at 31 December 2019 (2018: two properties).

A net deferred tax liability of £20.1m was recognised at 31 December 2019 (2018: net deferred tax asset of £3.2m). The increase in the deferred tax liabilities for 2019 was primarily driven by the increase in the defined benefit pension scheme surplus at 31 December 2019 (as outlined above) and a reduction in the level of deferred tax asset relating to tax losses brought forward from previous years. The key driver of the decrease in the deferred tax assets in 2019 was a de-recognition in the level of deferred tax asset relating to tax losses brought forward from previous years.

The Bank remains well capitalised and this is reflected in its solvency ratio of 18.0% (2018: 19.0%). During the year interim dividends of £100m (2018: £128.0m) were paid to the Bank's ultimate parent undertaking Danske Bank A/S.

General review

2019 was, overall, a successful year against increasingly challenging external conditions. The pace of change in financial services continued to increase against a backdrop of Brexit and political uncertainty.

By maintaining our focus on ‘Making More Possible’ for our customers, our colleagues, our partners and society, we achieved core business growth, delivered material customer experience improvements and were named Northern Ireland’s Responsible Company of the Year.

Making more possible for our customers

Personal Banking & Small Business

Mortgages were the key driver of our overall increase in lending in 2019. We have firmly established ourselves as a leading lender to homebuyers and owners in Northern Ireland, providing lending to one in five home buyers in Northern Ireland and helping more than 2,000 people buy their first home.

We continued to improve our mortgage offering with new product development as well as investment to improve the mortgage journey for customers. This has reduced the time to offer for our customers, particularly through our broker channel. Together with competitive pricing, this has helped us continue to be the leading mortgage provider in Northern Ireland.

We continued to respond to the changes in how consumers want to do their banking and to focus on enhancing the customer experience through all of our channels.

While this meant making the difficult decision to close two more branches, we also invested in five more branch refurbishments and increased assisted self-service technologies.

The high quality service provided through our contact centre was recognised when we were named Northern Ireland’s Contact Centre of the Year for the second year in a row.

We increased our focus on supporting customers in vulnerable circumstances by establishing a network of Vulnerability Champions across our business, working with a range of partners to provide more training and investing in our systems to ensure these customers are getting the highest levels of service.

Ensuring our services are inclusive and accessible to everyone, we trained more of our colleagues to be ‘dementia friendly’ and one of our branch managers was named the Alzheimer's Society’s Dementia Friend Champion of the Year. We were also the first bank to sign up to the Equality Commission Northern Ireland’s, 'Every Customer Counts' initiative, a public commitment to making our services accessible to customers who have a disability.

Review of business (continued)

General review (continued)

Start-ups and small business

We continued to help Northern Ireland's businesses by providing access to funding, expertise and advice.

We marked the first anniversary of the Catalyst Belfast Fintech Hub, a co-working space for early-stage technology entrepreneurs on the ground floor of our head office, that is run in partnership with the not-for-profit entrepreneurial eco-system, Catalyst. At the end of the year there are 78 Catalyst members using the space and more than 6,000 people have attended over 300 events.

TheHub.io, our free-of-charge online platform for growth start-ups, grew significantly. By the end of 2019, 188 start-ups had profiles on the site, 773 jobs had been advertised on it and there were 2,600 job applications through it. TheHub.io is a strategic partnership between Danske Bank, Catalyst and Rainmaking, a global cooperative of entrepreneurs.

Our network of 17 branch-based Small Business Advisers continues to provide a high quality service with fast, local decision making, something our customers tell us they value.

Corporate & Business Banking

We continue to grow our share of the top 100 companies in Northern Ireland and to attract high-growth international businesses. Whilst our capacity to support new business lending remains strong, demand for lending continues to be subdued as a result of uncertainty around the prolonged Brexit process.

Our focus is on strong relationship management, sectoral expertise and providing added value for our customers. This includes our series of Danske Advantage thought leadership events, bringing together business leaders and experts on a range of topics during 2019 including; corporate governance, innovation and three regional events on preparing for Brexit.

In 2019 we migrated the first tranche of businesses to our new online banking platform, 'District'. We also launched digital signing functionality which means business customers can now digitally sign their overdraft facility letter and lending requests can be completed in hours rather than days.

We streamlined the account opening process for trading businesses and expanded our digital credit application proposition to agriculture and business centre customers, significantly reducing the application timescales and accelerating customers' time to funds.

Investment in digital

The pace of change continues to accelerate, led by consumer behaviour and how customers want to bank with us. Customers have adopted our digital offerings at rapid speed, with digital touchpoints far outnumbering other interactions with the Bank.

With the continued investment in improving our digital proposition, we saw further adoption of our digital channels, with 75 million digital logons and a 33% increase in digital transactions year-on-year. Increased wearable payments contributed to this growth in 2019.

To successfully compete and be relevant in the future we must embrace and drive change, but we must do so in a responsible way. Our 'digital with a human touch' approach is about helping our customers manage this transition. This responsible approach to digital transformation was recognised externally by Business in the Community who awarded us the Responsible Digital Innovation award in 2019.

A key milestone in 2019 was the successful migration of our customers to our new mobile banking app. At the same time we launched a new security app, Danske ID, which has replaced the physical authorisation card and removed a key pain point for customers.

We further developed our Open Banking services; customers can now view their account information from six UK banks through our online and mobile banking services. In addition, we launched online meeting booking, enabling customers to book appointments directly in customer advisers' diaries.

Review of business (continued)

General review (continued)

Making more possible for our colleagues

2019 was a year of significant progress in our ambition to become the best bank to work for. We delivered an enhanced employee experience, invested in leadership capabilities, sharpened our performance management, modernised our approach to employee benefits and established a People Board.

Specific focus turned to employee resilience and wellbeing, investing in training and in deployment of innovative digital tools.

We entered into new partnerships and were awarded external charter marks by Legal Island, Diversity Chartermark NI, HM Treasury Women in Finance and Stonewall.

In 2019 we received several awards for our diversity and inclusion strategy - the CIPD Northern Ireland award for Best Diversity & Inclusion initiative, the Business in the Community NI award for Diversity and Inclusion and the Women in Business award for Advancing Diversity in the Workplace.

These awards recognise the public commitments the Bank has made to diversity and inclusion and significant, colleague-led, growth in our diversity networks – the Gender Diversity Network, Rainbow Network and Enable, the Danske Disability Network.

It was another record year for learning and development, with 40,000 hours of training delivered and a particular focus on Customer Experience (CX) initiatives. This investment was recognised externally when we won the CIPD Learning and Development Award 2019.

Competition for the best local talent continues to increase. We created more entry points with early careers programmes, took on our third round of graduate recruits and launched a second round of Danske Futures, our unique apprenticeship programme in partnership with Ulster University.

In the autumn we announced the creation of 30 new customer service adviser roles in Portadown, supplementing the work of our existing contact centre.

Making more possible for our partners and society

We play a significant role in driving Northern Ireland's economic growth; ensuring we deliver our services responsibly is key to who we are.
It was a year of many highlights, including being named Business in the Community Northern Ireland's Responsible Company of the Year.

We published our first annual Responsible Business report and achieved the highest level in Business in the Community's responsible business benchmarking survey, CORE.

A successful three-year partnership with Action Mental Health came to a close. During this time we raised more than £200,000 to support children's mental health, enabling 5,000 more primary school children to benefit from the charity's 'Healthy Me' mental health and resilience sessions in schools.

Through our Danske 'Time to Give' volunteering programme we facilitated our employees to volunteer over 1,500 hours in local communities. In addition, colleagues also helped teach more than 5,500 children and young people about money and budgeting.

Fraud and cyber-crime poses a growing threat to consumers and businesses and can have a devastating effect on victims. A dedicated Fraud and Cyber Crime team was established, bringing together expertise in card, ATM, cheque and payment fraud and further strengthening our customer education and outreach programmes.

Managing our impact on the environment was another key priority area in 2019 and we retained our Platinum position in the NI Environmental Benchmarking survey, leading the way in Northern Ireland's financial services sector. A change in waste management supplier means that from 2019 no waste will be sent to landfill. New initiatives included the development of a biodiversity strategy, embedding the Business in the Community Business & Biodiversity Charter, actions to help reduce the use of single-use plastic in our business and events to educate our employees and promote behavioural change.

Developments in 2020

During the course of 2020 there will be continuing developments in the Brexit process that will have impacts for the Bank and its customers.

Additionally, the coronavirus outbreak (COVID-19) is a recent emerging risk with impacts for customers, for colleagues, for the Bank and for wider society.

The Bank has arrangements in place to respond to both of these developments with a focus on ensuring that customers can continue to access banking services and that the Bank appropriately discharges its role in society whilst balancing the needs and expectations of customers, colleagues and partners.

Section 172(1) Statement

The members of the Board of Directors of Northern Bank Limited consider, both individually and collectively, that they have acted to promote the success of the Bank taking into account the needs of customers, colleagues, members and other stakeholders and the Bank's wider role in society. In doing so they have taken into account the following matters set out in s172(1) (a) to (f) of the Companies Act 2006:

(a) the likely consequences of any decision in the long term,
(b) the interests of the company's employees,
(c) the need to foster the company's business relationships with suppliers, customers and others,
(d) the impact of the company's operations on the community and the environment,
(e) the desirability of the company maintaining a reputation for high standards of business conduct, and
(f) the need to act fairly as between members of the company.

The Board is mindful that the long term success of the Bank is critically dependent on the way we work with a large number of notable stakeholders. The table below sets out our focus on the key relationships and shows how engagement with them is addressed by the Board of Directors (or Board committees) to help inform the Bank's decision making. It is important for all members of the Board to gain sufficient understanding of the issues relating to every stakeholder so that their views are taken into account in Board discussions.

A robust corporate governance framework is in place to ensure that stakeholder considerations are captured and enhancements made to strengthen the views of our stakeholders in the boardroom. Further information is set out in the Bank's Corporate Governance Statement.

Stakeholder Group	**Form of engagement**	**How this stakeholder group influenced the Board agenda and long term decision-making (s172(1)(a))**
Our people- s172(1)(b)(e) We create an environment in which our people can make a positive contribution, develop their careers and reach their potential. At the end of December we had c.1400 employees.	*At Board level:* Colleagues are a core pillar in the Bank's strategy and form a fundamental part of the Board-approved Corporate Plan. The Board receive regular updates on progress against the Bank's Colleague-focused strategic objectives and KPIs in addition to an annual update on our People Plan agenda provided by the HR Director. To facilitate engagement we have established a People Board including Executive Committee members. *At Business level:* Our people are a fundamental asset of our business and play a key role in the success of the Bank. Their views are taken into account throughout the Bank's Corporate Planning process, in which the HR Director plays a key role as a member of the Executive Committee. Engagement with our people takes many forms with regular and ongoing discussions, both at 1-2-1 and team level, divisional 2-way update sessions, CEO and ExCo roadshows and Employee Engagement surveys.	During 2019 the Bank has delivered Board approved colleague initiatives to motivate, engage and support high performance and retain key talent. **Early Careers** In 2019 we increased the number of entry points to our organisation as the first bank in Northern Ireland to launch a school leaver to degree apprenticeship programme through our Danske Futures initiative and we continue to run an annual Graduate Programme. **Continuous development** We invested more than ever before in both face to face and digital training - over 20% of colleagues are currently studying for professional qualifications, while c.40,000 hours were completed across digital and face to face channels. **Leadership Development** A suite of Leadership development programmes and interventions are in place to support all key milestones in a leadership journey. **Diversity and Wellbeing** In 2019 we launched 'Danske Belong' to connect our various Equality, Diversity and Inclusion (EDI) networks and to enhance our cohesive and consistent strategy. In 2019 the Bank won the Business in the Community's and the CIPD's Diversity & Inclusion awards. We entered into partnerships and were awarded external charter marks by Legal Island, Diversity Chartermark NI, HM Treasury Women in Finance and Stonewall. Our commitment to helping our employees manage their physical and mental wellbeing was reflected in our decision to work closely with Action Mental Health as our charity partner. New third-party partnerships provide colleagues with convenient access to services, new policies and training, providing additional support. As a result of this focus the Bank won Business in the Community's Wellbeing award.

Section 172(1) Statement (continued)

Stakeholder Group	Form of engagement	How this stakeholder group influenced the Board agenda and long term decision-making (s172(1)(a))
Our Customers - s172(1)(c)(d)(e) The users of our financial products and services. We have c.470k personal customers and c.40k business customers. We are enhancing our customer experience to attract new and retain loyal customers.	*At Board level:* The Bank has a number of dedicated teams that focus on delivering positive customer outcomes. This includes our Conduct and Customer Experience (CX) team that reports to the Executive Committee on a monthly basis, and updates are provided to Board on a regular basis in relation to Conduct and managing our Customer Satisfaction Key Performance Indicator (KPI). *At Business level*: The Bank uses customer feedback and insights as a core input to help shape strategic investment decisions utilising independent customer research, satisfaction surveys, mystery shopping and impact assessments. We have also established cross-functional Customer Journey Squads to drive enhancements across key journeys. Additionally, the Bank's Data Team provide key insights and analytics on customer behaviour to shape decisions and take action. One particular focus for the Bank is supporting customers in vulnerable circumstances. External partnerships and stakeholder engagement with vulnerable customer representative groups are key facets of this work to ensure our services are accessible to all our customers.	Customer satisfaction scores and feedback received influences decision-making at Board level. This has been reflected with customers as one of the Bank's four Making More Possible strategic pillars and core values which are a fundamental part of the Bank's Corporate Plan. We aim to be the first choice for helping our customers and businesses to achieve their financial goals in Northern Ireland. Every employee of the Bank has improving customer satisfaction as a core, and significant, element of their KPIs. As part of an ongoing multi-year programme, we remain committed to delivering a distribution network which meets the varying needs of our customer base. The growth of digital banking supports our investment plans in these areas, but we continue to recognise the importance of branch services to the communities we serve and the resulting benefits to the Bank of providing a network that covers all of the major towns across the province with at least one branch in each county. In 2019 the Bank decided to focus on supporting customers in vulnerable circumstances and became the first bank to sign up to the Northern Ireland Equality Commission's Every Customer Counts initiative.
Our Suppliers - s172(1)(c)(e) Provide our goods and services which we rely on to deliver for our customers.	*At Board level:* Reports are submitted to the Board on matters of importance regarding the supply of goods and services. They are also advised when adverse incidents that affect the Bank's ongoing operations are live and have been resolved. *At Business level*: The Bank has robust procurement policies (including sustainability, responsible sourcing and supply chain resilience) and manages its obligations under outsourcing in accordance with EBA guidelines. Supplier/Stakeholder meetings are conducted on a regular basis in accordance with Bank policy on outsourcing. The Bank maintains service level agreements with its parent Danske Bank A/S for the provision of key services to the Bank such as IT.	The Board approves the Modern Slavery Statement annually and we expect all our suppliers to be compliant with the Modern Slavery Act. We work closely with our suppliers and peers to build on our knowledge and promote best practice particularly in relation to anti-bribery and corruption.
Our Regulators- s172(1)(c) The Financial Conduct Authority (FCA) and the Bank of England (including its subsidiary, the Prudential Regulation Authority (PRA)), regulate our business.	*At Board level*: It is the Bank's policy to interact with the Regulators in an open and cooperative way. Members of the Board meet with the FCA and PRA on a regular basis. The Regulatory Reporting Committee meets bi-monthly and is attended by two members of the Board. The FCA and PRA also receive copies of Board papers. *At Business level*: We submit an extensive range of returns to the Regulators on all areas of the business as and when required. Senior management regularly engage with the Regulators to ensure all submitted returns are complete, accurate, consistent, timely and in compliance with the Regulators' requirements. Regulators also undertake onsite visits and reviews covering specific topics of interest.	Feedback received from the Regulators influences decision making at Board level including areas of critical importance such as the review and approval of risk appetite. We aim to maintain our positive relationship with the Regulators by following an approach of early and regular engagement regarding such decisions.

Section 172(1) Statement (continued)

Stakeholder Group	Form of engagement	How this stakeholder group influenced the Board agenda and long term decision-making (s172(1)(a))
Our Community and the environment - S172(1)(d)(e) We recognise our role supporting the community in Northern Ireland. We are conscious of the impact of our operations and the need to manage our impact on the environment.	*At Board level:* Society is a core pillar of the Bank's Making More Possible strategy and firmly embedded in the culture of the Bank. It is a key pillar in the Bank's strategy and forms a core part of the Board-approved Corporate Plan. The Board is regularly updated on progress against the Bank's Society-focused strategic objectives and KPIs in addition to receiving an annual update on our Society agenda. *At Business level*: The Bank's Responsible Business Board meets quarterly, and is chaired by our Chief Executive Officer. The Bank's impact on the environment, both direct and indirect, has become a factor in decision making. We recognise both the UK's recent policy announcements in addition to the EU's guidance in relation to the Non-Financial Reporting Directive, which encourages reporting in this area using the recommendations of the Climate Change Taskforce on Climate-related Financial Disclosures (TCFD). We are committed to supporting local communities and do so through our charity initiatives, volunteering, sponsorships and financial education programmes.	The Bank's Corporate Plan recognises this focus by including strategic objectives and selected Key Performance Indicators aimed at supporting our local community within the Board-level Balanced Scorecard that is reviewed at each Board meeting. The Board recognises that climate change must take greater prominence both at senior management and Board levels in 2020. Positive outcomes resulting from our community programmes include: - Named Business in the Community's (BITC) Responsible Business of the Year 2019; - Achieved Gold (the highest) level in BITC's CORE responsible business standard; - Achieved Platinum level in BITC's NI Environmental Benchmarking Survey for the second year; - Our three year partnership with Action Mental Health raised over £200k helping to support children's mental health education in schools; - Our employees volunteered over 1,600 hours in local communities during 2019; - Our SMART financial education programme in schools helped to educate 5,500 children and young people in 2019; - Development of our first biodiversity policy and achieved BITC's Business & Biodiversity Charter at Platinum level.
Business Relationships and Conduct- s172(1)(e) The Bank conducts its business responsibly, protecting customer interests resulting in appropriate customer outcomes, ensuring regulatory compliance and high standards of professional conduct.	*At Board level*: The Bank's Corporate Governance framework allows the Board and management to assess and monitor culture. The Board has oversight of the culture and the standards of business culture promulgated throughout the Bank. *At Business level:* Acting responsibly and ethically, our Responsibility Policy governs and outlines our approach to conducting our business in a responsible and transparent manner and is integrated in daily decision-making through strategies, policies, targets, business procedures and processes. Corporate Responsibility is integrated in our core business through our vision and strategy. This provides the strategic framework including KPIs and reporting. High standards of professional conduct are communicated via our Code of Conduct and also workforce training in anti-bribery and corruption, anti-money laundering and ethics. The Bank has a dedicated Conduct and Customer Experience team led by a Senior Manager that reports into the Bank's Conduct Committee which is attended by Executive Committee members.	The Board is committed to embedding the section 172(1) factors in the culture of the business and decision making at all levels of management. This is evidenced by the empowerment of sub committees and management teams for each key stakeholder group. The Bank's focus on conducting its business responsibly was also externally recognised by being named Business in the Community's (BITC) Responsible Business of the Year 2019. Further information is available in the Bank's Responsible Business Report on our website www.danskebank.co.uk.

Section 172(1) Statement (continued)

Stakeholder Group	Form of engagement	How this stakeholder group influenced the Board agenda and long term decision-making (s172(1)(a))
Our Company and its Parent s172(1)(f) As a strong, stable and predictable bank, we seek to create long-term value through the delivery of sustainable returns. Through the delivery of our Corporate Plan, the Bank aims to optimise returns, support our Parent, and invest in the business in an efficient and cost-conscious way.	*At Board level:* The Bank, its Executive Management and Board are closely engaged with our Parent. The Bank's Board includes two Group Directors (both of whom are members of the Group's Executive Leadership Team). Group updates are also provided by these two Directors to the Bank's Board. The Bank's Executive Committee is closely aligned to Group counterparts and through regular Board updates provides insight into Group interactions. At senior decision-making level we share with Group a strategic vision to promote the success of the Bank for the benefit of all its Stakeholders. Our Corporate Plan is developed in conjunction with senior Group colleagues and has received endorsement from both the Group Executive, Leadership Team and Group Board. The Bank has an annual Board Meeting at its parent site in Copenhagen, at which senior Group employees present updates to the Board on specific areas of interest. The Bank's three Executive Directors also attended the Group Leaders Conference in September 2019. In addition to Bank employees, the Board regularly receives updates from Group stakeholders across areas including Finance, IT, Risk, Business Development and Strategy. These stakeholders also provide inputs to the Bank's Corporate Planning process and are integral parts of delivering developments for the Bank.	The Board in its decision making process takes into account the impacts of the decision on the return to the Group on its capital investment in the company. The Board also considers annually whether a dividend should be paid from surplus capital.

Principal risks and uncertainties

Economic overview

UK GDP was flat in the last quarter of 2019, following growth of 0.5% in the third quarter of the year. In annual terms, the UK economy grew by 1.4% in 2019, slightly above the 1.3% observed in 2018.

In its Northern Ireland Quarterly Sectoral Forecasts 2019 Q4 report, Danske Bank estimated that economic growth in Northern Ireland was 0.8% in 2019, a recovery from the fall in output recorded for 2018.

The CPI inflation rate in the UK fell from 1.5% in November 2019 to 1.3% in December 2019. In annual average terms, UK inflation was 1.8% in 2019, down from 2.5% in 2018.

At the end of 2019, Bank Rate was 0.75%. In annual average terms, interest rates in the UK were 0.75% in 2019, up from 0.60% in 2018. This remains low by historical standards, and with interest rates likely to remain relatively low for a protracted period of time, the monetary policy environment could continue to pose an income challenge for the Bank.

The Northern Ireland labour market data for October – December 2019 showed that, over the quarter, the employment rate increased to 72.4%, the unemployment rate decreased to 2.4% and the economic inactivity rate was unchanged at 25.8%. In annual average terms, the unemployment rate in 2019 was 2.7%, the employment rate was 72.1% and the economic inactivity rate was 25.9%. The strong labour market in Northern Ireland led to relatively high rates of wage growth, which in turn supported consumer spending.

House prices in Northern Ireland increased by 2.5% over the year to the fourth quarter of 2019, lower than the 3.9% rise in 2019 Q3. The standardised house price in 2019 Q4 was £140,190. In annual average terms, house prices in Northern Ireland increased by 3.5% in 2019. The reasonably strong performance of the local housing market was a supportive factor behind the increase in the Bank's mortgage lending in 2019.

Looking forward, the economy is expected to continue relying on consumer spending to drive growth as uncertainty around the future trading relationship between the UK and the EU weighs on business investment and modest global growth constrains exports.

Principal risks and uncertainties (continued)

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 (ICAAP), Individual Liquidity Adequacy Assessment Process (ILAAP) 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

Business risk is the risk that income unexpectedly will not be able to cover losses inherent in the chosen business model not related to other risk types i.e. credit risk, market risk, operational risk, pension risk etc. Consequently, business risk is considered a residual risk that reflects possible changes in general business conditions such as market environment, customer behaviour, the Bank's reputation and technological progress to which the Bank may not be able to adjust sufficiently quickly. 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 business risk outlook is seen as increasing due to the competition in the banking arena from non traditional banks with Open Banking, together with the significant level of regulatory change such as High Cost of Credit Review and Alternative Dispute Resolution.

Operational risk (Outlook: Increasing)

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 as ineffective management of operational risk can damage the credibility, reputation and finances of the Bank. The Bank recognises that operational risk exists as an inherent part of doing business. 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.

- Internal 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 IT 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.

- Climate change
  The Bank has made a long-term commitment to protecting and enhancing the environment. It will continue to give consideration to its impact on the climate and has designed environment objectives which aim to minimise negative impacts, while also looking at ways to enhance the opportunities arising from the transition to a low carbon economy. Climate Change is a major focus area for the Bank and is a significant risk category. This is reinforced by the expectations inherent within the Prudential Regulation Authority (PRA) Supervisory Statement (SS3/19) on 'Enhancing Bank's and Insurer's approaches to managing the financial risk from climate change'. The Bank is also working closely with the Danske Bank Group in exploring adoption of the Task Force on Climate-Related Financial Disclosures (TCFD) recommendations and the development of high quality, consistent and comparable climate-related financial disclosures.

Principal risks and uncertainties (continued)

Operational risk (Outlook: Increasing) (continued)

- Climate change (continued)

A Board-approved climate change implementation strategy is in place to continually assess and address the ongoing impact of Climate Change on both the Bank and its customers. The Board is kept appraised of significant physical and transitional risks, along with related policies on climate change via the appropriate risk committees. The role of the Board is to understand and assess the financial risks from climate change and oversee those risks within business strategy and risk appetite. At Bank Management level, regular identification, control and management of climate change risks will continue to mature within existing processes and infrastructure. In addition, the Bank has an Environmental Social and Governance (ESG) Risks policy in place. To manage these climate related strands, the Bank established a Climate Change Working Group which comprises senior stakeholders from across the Bank

Consideration will be given to the physical and transitional risks to the Bank, its relationships and partners, along with other climate-impacted exposures. It is the Bank's objective, through sectoral risk analysis in a climate change context, to mitigate the societal and financial impact of climate change on its customers and the local environment. The benefits to the Bank of incorporating increased awareness and understanding of climate related risks and opportunities include better risk management, more informed decision making, informed strategic planning and a more diverse investor base.

Each business area will support the Bank's approach to managing climate change impacts. Business Units will be responsible for the risks in their area, and a centralised register will be maintained to capture climate related risks across the Bank. There will also be focus on societal impact and sustainability by incorporating responsible banking principles in to a sustainable lending strategy. These processes will evolve over time. Transitionary and physical risks will be considered on a sectoral basis and as part of ongoing due diligence of the Bank's relationships. This will give consideration to evolving governmental policies and the Bank's own ESG and Credit Risk policies.

As part of the Danske Bank Group, the Bank has been carbon neutral since 2009. The Group has limited its C02 emissions by purchasing renewable electricity and C02 credits. It has also signed up to RE100, a global initiative uniting businesses who are committed to 100% renewable energy. Group have given their commitment to the Paris Pledge for Action and is also a signatory to the Carbon Disclosure Project (CDP) and the Montreal Carbon Pledge. The Bank has set a target of achieving a 15% reduction in energy consumption from 2015 to 2020. This reduction was achieved by 2018 and the target was increased to 25%. It has also retained its platinum level position in the 2019 Northern Ireland Environmental Benchmarking Survey. During the current financial year, the Bank purchased a Climate Awareness Bond (CAB) as part of its liquid asset buffer holding. The Bond focuses on investment in renewable energy, efficiency and other activities contributing to climate change mitigation, where that activity substantially contributes to stabilisation of greenhouse gas concentrations in the atmosphere at a level which prevents dangerous anthropogenic interference with the climate system.

The Bank is aware that this is also an area of opportunity as climate change understanding evolves with institutions and consumers transitioning to a low carbon environment. The Bank endeavours to develop these opportunities in a proactive way, by setting appropriate policies and procedures aligned with climate related considerations within the Bank risk appetite.

- Other operational risk matters

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 is 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. The Bank aims to continue to improve IT system stability and has made significant investment in strengthening our Group-wide IT change management arrangements.

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).

Although the Bank is firmly focused on operational risk performance improvement, it acknowledges that the key drivers of operational risk have become increasingly complex. These include automation and digitalisation, regulatory focus on customers as victims, reputational impact and fines from operational events and cyber risk, the embedding of the General Data Protection Regulation (GDPR) and its strict new guidelines that must be adhered to. In addition, the Bank is exposed to risks arising out of widespread public health crises, including the recent coronavirus outbreak. For this reason, the Bank sees the operational risk outlook as increasing for the considerable future.

- Coronavirus (COVID-19) outbreak

The coronavirus outbreak (COVID-19) is a recent emerging risk. The Bank has invoked contingency planning to manage the operational impacts with a view to ensuring that customers can continue to access banking services and that the level of disruption is minimised. It is likely that the outbreak will impact market sectors to which the Bank is exposed and that there could be a negative impact on the Bank's future performance. The Bank is continually monitoring and assessing the range of potential impacts and will continue to respond to the situation as it evolves. The final impact will be dependent on a wide range of future developments which are highly uncertain and cannot be predicted.

Regulatory risk (Outlook: Increasing)

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.

Significant uncertainty exists as to the respective legal and regulatory arrangements under which the Bank will operate when the UK is no longer a member of the European Union.

Principal risks and uncertainties (continued)

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

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 parameters 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 via both manual and automated channels, 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 aiming to become the core or preferred banking choice for our customers. To maintain such relationships, the Bank must always be able to offer competitive financial solutions that meet the needs of its customer base. 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 and support customers through challenging situations. Consequently, when extending and monitoring credits, the Bank makes detailed assessments of individual customers and their financial positions.

The Bank continues to monitor closely the credit standing of customers in the light of Brexit, particularly those customers and industry sectors considered vulnerable to Brexit related risks. It will also endeavour to react quickly in implementing suitable credit related policies to counteract risks arising under the present fluid environment, as the need arises.

The uncertainties around Brexit and the future trading relationship with the European Union will have an impact upon future impairment levels. The underlying stress scenarios which underpin the impairment calculation under IFRS 9 can be adjusted to encapsulate forecast macroeconomic conditions dependent upon the likelihood of occurrence of various Brexit related outcomes. These macroeconomic conditions are reviewed through the course of the year to ensure they remain relevant to the latest political and economic situations.

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;
- use of automated decision models and statistical scorecards;
- 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:
- delegated authorities for the approving of credit;
- effective employee management to maintain and develop staff expertise; 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.

Principal risks and uncertainties (continued)

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

- 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, Board Risk Committee 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 as considered appropriate.

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.

- 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.

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 both; and
- LCR regulatory stresses, ensuring that the Bank has sufficient liquidity to survive for a 30 day period.

Principal risks and uncertainties (continued)

Liquidity risk (Outlook: Stable) (continued)

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.

The Board has approved 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 the Financial Services Compensation 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, 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 or for hedging.

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 objective of asset and liability management is 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).

Impact of LIBOR reform

The interest rate benchmark LIBOR is expected to cease after the end of 2021 and firms must transition to alternative rates before this date. The London Interbank Offered Rate (LIBOR) is currently across five currencies and is based on submissions provided by a panel of twenty banks. These submissions are intended to reflect the interest rate at which banks could borrow money on unsecured terms in wholesale markets. However, it had become increasingly apparent that the absence of active underlying markets and the scarcity of term unsecured deposit transactions raised serious questions about the future sustainability of the LIBOR benchmarks.

In order to enable time for the market to transition away from LIBOR, a voluntary agreement was received from the LIBOR panel banks to continue to submit to LIBOR until the end of 2021. All banks and other market participants need to have removed dependencies on LIBOR by this date if they are to avoid disruption when publication of LIBOR ceases.

The Bank currently has various Business and Corporate Banking products that are priced with LIBOR, and to a smaller extent other IBOR's as a reference rate. This reference rate needs to be removed and, where relevant, replaced with an alternative Risk Free Reference Rate (RFR). The Bank also, from a ris management perspective, uses LIBOR for fixed rate swaps and holds LIBOR linked bonds in its Liquid Asset Buffer, all of which will require changes in reference rates.

In February 2019, the Bank formally established a LIBOR programme to ensure a coordinated and timely approach to the transition to new and amended reference rates ensuring a harmonised implementation approach across all asset classes and different types of contacts.

There still remains uncertainty on the alternative RFR's to be used, and thus, how conversion of instruments to these new reference rates will be effected and the timescales for conversion which is an industry-wide issue. Until more certainty exists, through market-wide agreement, the impact of the LIBOR reform cannot be reliably determined.

Principal risks and uncertainties (continued)

Pension risk (Outlook: Stable)

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 administration costs 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 cessation of 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 analysis 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.

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 exposures and multilateral development bank bonds. The investment portfolio fluctuates according to the Bank's liquidity and interest 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 9.6% (2018: 9.8%) for the year ended 31 December 2019. Furthermore, its capital position remained strong with a Common Equity Tier 1 ratio of 17.3% (2018: 17.0%) at 31 December 2019.

The Bank (as a Group) is still responding to justified criticism of its management of AML issues in Estonia, particularly in the areas of stronger governance controls and Group oversight. This issue had limited impact locally.

Capital adequacy risk (Outlook: Stable)

This is the risk that the Bank holds insufficient capital to absorb extreme and unexpected losses arising from the Bank's chosen business strategy which could eventually result in insolvency.

Capital adequacy risk is central to the strategic planning process. The purpose of the Bank's capital management is to support its strategy and to ensure that it is sufficiently capitalised to withstand even severe downturns without breaching regulatory requirements. There is regular senior management reporting presented and reviewed at Asset and Liability Committee (ALCO) and at scheduled Board meetings 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.

Principal risks and uncertainties (continued)

Capital position (unaudited)

In June 2018, the Bank of England outlined its approach to setting a Minimum Requirement for own funds and Eligible Liabilities (MREL) for UK banks, building societies and large investment firms. MREL is the minimum amount of equity and subordinated debt a firm must maintain to support an effective resolution. This is separate to the capital requirements set by the Prudential Regulatory Authority (PRA). The PRA has determined that the Bank meets the criteria for holding MREL resources due to its current provision of critical services in the Northern Ireland economy.

From 1 January 2020, the Bank is required to hold internal MREL equivalent to 18% of total Risk Exposure Amount (REA), with a PRA prescribed scaling factor applied. This is expected to hold, subject to annual review, until 1 January 2022, when the Bank will be required to hold internal MREL equivalent to two times its Pillar 1 and Pillar 2A (excluding capital buffers), with a PRA prescribed scaling factor applied. In order to meet its MREL requirement, the Bank will issue MREL eligible liabilities during 2020.

The Bank's Common Equity Tier 1 ratio (on a UK PRA basis) decreased from 13.8% in December 2018 to 13.4% in December 2019.

Regulatory capital

	31 December 2019 £'000	31 December 2018 £'000
Common Equity Tier 1 capital		
Permanent share capital	**218,170**	218,170
Retained earnings	**165,194**	180,288
Profit yet to be verified for inclusion in regulatory capital	**(13,658)**	(20,708)
Share premium account	**306,590**	306,590
Revaluation reserve	**35,906**	35,602
Reserve for Investment securities - Hold to collect and sell	**1,594**	(2,977)
IFRS 9 transitional adjustment	**15,503**	14,174
Less : pension fund asset (net of tax)	**(148,258)**	(115,465)
Less : deferred tax asset ineligible for Common Equity Tier 1 capital	**(18,060)**	(23,830)
Less : prudent valuation adjustment	**(434)**	(334)
Less : intangible asset	**(212)**	(415)
Total Common Equity Tier 1 capital after deductions	**562,335**	591,095
Additional Tier 1 capital		
AT1 capital instrument	**97,069**	97,101
AT1 regulatory restriction*	**(12,902)**	-
CRD IV compliant instrument	**84,167**	97,101
Tier 2 capital		
Subordinated loan debt	**126,000**	126,000
Subordinated loan regulatory restriction*	**(15,254)**	-
Dated CRD IV compliant subordinated loan instruments	**110,746**	126,000
Total capital after deductions	**757,248**	814,196

*The PRA expects the Bank's Total Capital Requirement (Pillar 1 and Pillar 2A) to be met with at least 56% CET1 capital, no more than 44% Additional Tier 1 capital and no more than 25% Tier 2 capital. As a result of the reduction in the Bank's Pillar 2A capital requirement during 2019, a portion of the Bank's Additional Tier 1 capital and Tier 2 capital is no longer eligible to be included in the Bank's regulatory total capital as it falls above the capital restrictions.

Principal risks and uncertainties (continued)

Capital position (continued)

Risk-weighted exposure amounts (REA) (standardised approach)

	31 December 2019 £'000	31 December 2018 £'000
Credit risk	**3,802,081**	3,902,542
Operational risk	**396,090**	379,629
Market risk	**-**	1
Credit value adjustment	**736**	44
	4,198,907	4,282,216

Capital ratios

	31 December 2019	31 December 2018
Common Equity Tier 1 ratio	**13.4%**	13.8%
Tier 1 ratio	**15.4%**	16.1%
Total capital ratio	**18.0%**	19.0%
Total Capital Requirement (TCR)	**10.6%**	12.0%
Leverage ratio	**6.3%**	7.0%

Regulatory capital to statutory total equity reconciliation

	31 December 2019 £'000	31 December 2018 £'000
Regulatory Common Equity Tier 1 capital	**562,335**	591,095
Add back:		
- Pension fund asset (net of tax)	**148,258**	115,465
- Deferred tax asset relying on future profitability	**18,060**	23,830
- Profit to be verified for inclusion in regulatory reporting	**13,658**	20,708
- Intangible assets	**212**	415
- Cash flow hedge reserve	**2,132**	148
Additional tier 1 capital	**97,069**	97,101
IFRS 9 transitional adjustment	**(15,503)**	(14,174)
Prudent valuation adjustment	**434**	334
Statutory total equity	**826,655**	834,922

Minimum Pillar 1 capital requirements

	31 December 2019 £'000	31 December 2018 £'000
Credit risk	**304,166**	312,203
Operational risk	**31,687**	30,370
Market risk	**-**	-
Credit value adjustment	**59**	4
Pillar 1 regulatory capital	**335,912**	342,577

Principal risks and uncertainties (continued)

Regulatory capital flow of funds

	31 December 2019 £'000	31 December 2018 £'000
Common Equity Tier 1 capital		
Common Equity Tier 1 capital at 1 January	**591,095**	544,452
Profit for the year	**64,104**	70,173
Adjustment for profit yet to be verified for inclusion in regulatory capital	**7,050**	98,957
Property revaluation (net of tax)	**767**	339
Investment securities: Hold to collect and sell (net of tax)	**4,571**	(1,858)
Additional Tier 1 interest (net of tax)	**(5,560)**	(5,429)
Pension surplus adjustment (net of tax)	**(19,724)**	(259)
Dividend	**(100,000)**	(128,000)
Deferred tax asset movement	**18,600**	10,932
Prudent valuation adjustment movement	**(98)**	3
Intangible asset movement	**202**	(141)
IFRS 9 transitional adjustment	**1,328**	1,926
Total Common Equity Tier 1 capital after deductions at 31 December	**562,335**	591,095
Additional Tier 1 capital		
Additional Tier 1 capital at 1 January	**97,101**	97,020
AT1 regulatory restriction	**(12,902)**	-
Movement in interest accrual	**(32)**	81
Additional Tier 1 capital at 31 December	**84,167**	97,101
Tier 2 Capital		
Tier 2 capital at 1 January	**126,000**	126,000
Subordinated loan regulatory restriction	**(15,254)**	-
Total Tier 2 capital after deductions at 31 December	**110,746**	126,000
Total capital after deductions at 31 December	**757,248**	814,196

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

As at 31 December 2019

	Capital required £'000	**REA £'000**	**Exposure £'000**
Corporate	**182,023**	**2,275,283**	**3,856,898**
Retail	**100,851**	**1,260,643**	**3,766,955**
Institutions	**3,844**	**48,049**	**120,238**
Sovereign	**-**	**-**	**4,535,615**
Other	**17,448**	**218,106**	**397,088**
	304,166	**3,802,081**	**12,676,794**

As at 31 December 2018

	Capital required £'000	REA £'000	Exposure £'000
Corporate	191,926	2,399,074	3,756,683
Retail	94,420	1,180,247	3,683,803
Institutions	3,019	37,739	85,633
Sovereign	-	-	4,193,627
Other	22,839	285,482	438,951
	312,204	3,902,542	12,158,697

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

Fiona Sturgess
Company Secretary
19 March 2020

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 2019.

The Bank's profits, strategic highlights, business developments and management of risk are set out in the Strategic Report on pages 3 to 19 and notes 1 to 45 of the Financial Statements.

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 £100,000,000 (2018: £128,000,000). The Directors do not recommend the payment of a final dividend in respect of this financial year (2018: £Nil).

Directors and Directors' interests

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

Berit Behring (Appointed 11 November 2019)
Michael Black
Vicky Davies
Jim Ditmore (Resigned 5 September 2019)
Carsten Egeriis
Gerald Gregory
Astrid Grey (Appointed 28 February 2020)
Kevin Kingston
Margaret Lesley Jones (Resigned 26 September 2019)
Stephen Matchett
Paul Rooney
Martin Stewart (Appointed 21 January 2020)

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 Bank itself to the extent that it is obligated to indemnify Directors and officers for such liability.

Employee engagement

The Bank carries out an information programme to keep colleagues 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 Bank colleagues are considered in making decisions which are likely to affect their interests.

The results of the Bank's consultation with its employees on principal decisions made are set out in the s172(1) statement contained in the Strategic Report.

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 (2018: £Nil).

Business relationships

The Directors understand the need to foster the Bank’s business relationships with suppliers, customers and others, and have set out the effect of that regard, including on the principal decisions taken by the Bank during the financial year, in the s172(1) statement in the Strategic Report.

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 2019 the portfolio of liquid assets was £2.2bn and significantly in excess of that required to meet the most stressful liquidity scenario. The Bank's loan book is fully funded by customer deposits and the Bank has a low loan-to-deposit ratio of 76%; 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 2019 to the shareholders.

Auditor

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

19 March 2020

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

19 March 2020

For the year ended 31 December 2019, under The Companies (Miscellaneous Reporting) Regulations 2018, the Bank has adopted the Wates principles for large private companies as an appropriate framework when making a disclosure about its corporate governance arrangements.

Each of the 6 Wates Principles has been considered individually within the context of the Bank's specific circumstances and a short supporting statement is set out below to explain how each principle has been applied to achieve better outcomes.

Purpose and Leadership

An effective Board develops and promotes the purpose of a company, and ensures that its values, strategy and culture align with that purpose.

As Northern Ireland's biggest bank, we have been helping people and businesses achieve their ambitions for over 200 years. We support financial stability by running a profitable business, conducting our activities in a responsible manner and making our time and expertise available for the benefit of the communities that we serve.

The Bank's purpose, and ultimately its vision, is to be the best bank in Northern Ireland by "Making More Possible" for our customers, colleagues, partners and society. These four focus areas form the framework of our Corporate Plan which is developed on an annual basis by management, in conjunction with the Board/under the Board's direction.

The Board is committed to a culture of strong ethical behaviour as embodied in our five core values – expertise, integrity, value, agility and collaboration which together are central to the Bank's vision of "Making More Possible".

Our Culture Wheel articulates the behaviours that are critical for the future success of our business. The wellbeing of our colleagues, customers and wider society lies at the heart of what we do and ensures alignment of our wellbeing strategy with our people strategy and overall Corporate Responsibility agenda.

Board composition

Effective Board composition requires an effective chair and a balance of skills, backgrounds, experience and knowledge, with individual Directors having sufficient capacity to make a valuable contribution. The size of a Board should be guided by the scale and complexity of the company.

The Bank has a separate Chairman and Chief Executive to ensure that the balance of responsibilities, accountabilities and decision making across the Bank is effectively maintained. The Chairman plays a pivotal role in creating the conditions for overall Board and individual Director effectiveness and ensuring that the Board is effective in its task of setting and implementing the Bank's direction and strategy.

The Board comprises a Chairman, Chief Executive Officer, two Deputy Chief Executive Officers, two Group Non-Executive Directors and four Independent Non-Executive Directors. The size and composition of the Board is appropriate to the Bank's size, nature and complexity of the business.

The combination of skills of the Directors is considered suitable for the nature of the organisation; Independent Non-Executive Directors bring experience in banking and finance, audit, insolvency and business recovery, and technology, in addition to perspectives and challenge from outside the banking industry. There is an appropriate mix of local, national and international Directors and the Board continues to improve its gender balance noting that by quarter three 2019, gender diversity on the Board had increased to 30%.

The Directors have equal voting rights when making decisions, except the Chairman, who has the casting vote. All Directors have access to the advice and services of the Company Secretary and may, if they wish, take professional advice at the Bank's expense.

There is open debate and constructive challenge at meetings, with Board members demonstrating good engagement with the business and a sound understanding of the Bank's strategy and associated risks and challenges.

The duties of the Board are executed partially through committees. The Independent Non-Executive Directors are members of and act as chairs to relevant committees so that they are able to challenge and influence a broad range of areas across the Bank.

Directors update their skills, knowledge and familiarity with the Bank by meeting with senior management, visiting operations and by attending appropriate internal and external seminars and training courses. There is an induction programme for all new Directors which is tailored to their specific experience and knowledge and which provides access to all parts of the business, including access to the Bank's sole shareholder, Danske Bank A/S (the 'Group').

Director responsibilities

The Board and individual Directors should have a clear understanding of their accountability and responsibilities. The Board's policies and procedures should support effective decision-making and independent challenge.

Each Board member has a clear understanding of their accountability and responsibilities. The Board has a programme of at least seven principal meetings every year, plus two additional days for strategic planning with key Group stakeholders. Whilst Board oversight is always maintained, key decisions are made by the individuals and committees with the most appropriate knowledge and industry experience.

At each Board meeting, all Directors are asked to declare any potential conflicts of interest. These declarations are collated by the Company Secretary and where there are potential conflicts, appropriate safeguards are implemented.

In addition, certain governance responsibilities are delegated to other Board committees (Audit, Risk and Remuneration). Membership of these committees is comprised entirely of Independent Non-Executive Directors who support effective decision making and independent challenge.

The Independent Non-Executive Directors are wholly independent in that they have no material business or relationships with the Bank that might influence their independence or judgement.

Director responsibilities (continued)

There is a process in place for regular Board effectiveness reviews to seek independent, objective advice on the effectiveness of the Board's decision-making, its structure, its people and its processes. The Board undertook a formal effectiveness review facilitated by an independent external adviser in 2017 and has scheduled the next independent review for early 2020. Between externally facilitated assessments, the Board has conducted informal self assessments which the Board considers important in the identification of key areas for future improvements, focus and for strengthening its overall performance.

Opportunity and risk

A Board should promote the long-term sustainable success of the company by identifying opportunities to create and preserve value, and establishing oversight for the identification and mitigation of risks.

The promotion of the long-term sustainable success of the Bank is fundamental to the Bank's 5 year Corporate Plan which is updated each year, under Board direction. It is the view of the Board that the long term future of banking will, in part, be about strategic partnerships and this is a theme that underpins the Bank's purpose and vision. As such, 2019 was a year of strengthening existing relationships and embarking on strategic new partnerships in the technology, higher education, not-for-profit and social enterprise sectors.

At Board level, oversight of risk is delegated to the Board Risk Committee, which meets at least six times per year, the membership of which is comprised entirely of Independent Non-Executive Directors, ensuring there is appropriate accountability to stakeholders. There is also a well-established Corporate Governance Framework which establishes oversight for the identification and mitigation of risks across the Bank.

Remuneration

A Board should promote executive remuneration structures aligned to the long-term sustainable success of the company, taking into account pay and conditions elsewhere in the company.

The Board of the Bank has an established Remuneration Committee (RemCo), which is chaired by the Chairman of the Board. The RemCo is instrumental in the Board's fulfilment of its governance responsibilities relating to the remuneration of employees and in particular the alignment of performance related pay with the long-term interests of the Bank and its policy on risk and stakeholders in the Bank.

The Board is committed to creating an environment at all levels in the Bank which enables people to perform and develop their abilities and potential.

A diverse workplace which does not attach specific importance to; age, community background or country of origin, disability, gender, nationality, political opinion, religious belief, or sexuality, ensures that we are able to attract talented employees who will contribute to the Bank's success.

Annually, the RemCo prepares a Remuneration Report which is published on our website www.danskebank.co.uk.

Stakeholder relationships and engagement

Directors should foster effective shareholder relationships aligned to the company's purpose. The Board is responsible for overseeing meaningful engagement with stakeholders, including the workforce, and having regard to their views when taking decisions.

The Board has strong relationships with Danske Bank A/S, its sole shareholder, with two Executives of Danske Bank A/S appointed as Directors of Northern Bank Limited. At each Board meeting, the Board is provided with an update in relation to Danske Bank A/S and, on an annual basis, the Board visits the offices of the Group for a series of presentations from key stakeholders across the Danske Bank Group, for strategic planning purposes and to hold an offsite meeting of the Board. Furthermore, the Board regularly receives updates from Group stakeholders across areas including Finance, IT, Risk, Business Development and Strategy. These stakeholders also provide inputs to the Bank's Corporate Planning process and are integral parts of delivering developments for the Bank.

Close dialogue with stakeholders is an integral and natural part of the Bank's operations. Senior leaders welcome dialogue with all external stakeholders, representatives of government and other leading figures within Northern Ireland and beyond and want to engage in a constructive manner, and from a long-term perspective. This approach is driven by an ambition to create value, commitment to transparency and the core values of integrity and collaboration.

Listening to, and empowering employees is critical to achieving the Bank's vision. Formally, employees have a voice through regular 'Pulse' and 'Team Talk' Surveys. The outputs from these employee surveys inform the People Board (a group of senior employees who are responsible for shaping and delivering the people strategy in collaboration with HR) and business unit action plans. In addition, regular employee 'Roadshows' are delivered in locations across Northern Ireland and provide a briefing on the Bank's performance and allow individuals to raise questions and provide feedback.

Northern Bank Pension Trust Limited is the corporate Trustee of the Northern Bank Pension Scheme. Although a wholly-owned subsidiary, the Trustee operates independently of the Bank and in accordance with pension regulations. The Bank, as sponsor of the Scheme, maintains a constructive and open relationship with the Trustee (usually through the Chairman of the Trustee Board). The Trustee Directors comprise individuals nominated by either pension scheme members or by the Bank. This support, provided by the Bank, ensures diversity of knowledge and skills on the Trustee Board, thereby facilitating good governance and decision-making (which is in the interests of all Scheme stakeholders).

The Bank's website, intranet and social media channels provide extensive and up-to-date news on recent developments impacting our customers, colleagues, partners and the society.

We advocate the benefits of running a responsible business and encourage others to follow. In January 2019 the Bank published our first annual Responsible Business Report, which highlights our contribution to the wider society that we serve and the local communities we are a part of, in areas such as diversity and inclusion, sustainability and climate change.

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

Report on the Audit of the Financial Statements

In our opinion the financial statements of Northern Bank Limited (the 'Bank'):
- give a true and fair view of the state of the Bank's affairs as at 31 December 2019 and of the profit for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements which comprise:
- the Income Statement;
- the Statement of Comprehensive Income;
- the Balance Sheet;
- the Statement of Changes in Equity;
- the Cash Flow Statement;
- the Statement of Accounting Policies; and
- the related notes 1 to 45.

The financial reporting framework that has been applied in their preparation is applicable law and IFRSs adopted by the European Union.

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 Financial Reporting Council's (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: - Expected credit losses on loans and advances to customers; - Valuation and recoverability of deferred tax asset; and - Valuation of defined benefit pension scheme obligations. Within this report, key audit matters are identified as follows: Newly identified Increased level of risk Similar level of risk Decreased level of risk
Materiality	The materiality that we used in the current year was £5,000,000 which was determined on the basis of profit before tax.
Scoping	We determined the scope of our audit 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 being audited by a separate audit team in Copenhagen, Denmark.
Significant changes in our approach	There have been no significant changes in our approach when compared to the financial audit for the year ended 31 December 2018.

Conclusions relating to going concern

We are required by ISAs (UK) to report in respect of the following matters 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.

We have nothing to report in respect of these matters.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matters (continued)

Expected credit losses on loans and advances to customers	
Key audit matter description	Under IFRS 9, losses on financial assets which are recognised at amortised cost, are recognised on an expected credit loss basis. Expected credit losses (ECLs) are required to incorporate forward-looking information, reflecting management's view of potential future economic environments. The complexity involved required management to develop new methodologies involving the use of significant judgements. This includes the risk that an inappropriate valuation of collateral used and other significant cash flows used in the individually assessed provision calculations, as well as the risk that significant increases in credit risk are not identified resulting in inaccurate staging classification under IFRS 9. At 31 December 2019, the expected credit loss allowance on loans and advances to customers was £79.4 million (2018: £92.1 million), representing a coverage level of 1.3% on a total portfolio of £6,188 million (2018: 1.5% on a total portfolio of £6,018 million). Measurement of the ECL allowances on loans and advances to customers is a key audit matter as the determination of assumptions for ECLs is highly subjective due to the level of judgement applied by Management. The most significant judgements include: - Determining the criteria for a significant increase in credit risk and for being classified as credit impaired; - Choosing the appropriate models and assumptions for measuring ECL (being probability of default, loss given default, and exposure at default); and - Key assumptions, including collateral valuation and cashflow timings, used in discounted cashflows (DCFs) of individually assessed Stage 3 loans. 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 understood and tested key controls supporting the calculation of ECLs on loan and advances to customers focusing on; - model development, validation and approval to ensure compliance with IFRS 9 requirements; - review and approval of key assumptions, judgements and forward looking information used in the models; and - front line credit monitoring and assessment controls. Our testing of key controls included an evaluation of IT system controls, management review controls and governance controls. We understood and critically assessed the ECL models developed by the Bank. Our team in Denmark used credit-modelling specialists to challenge the judgements and assumptions supporting the ECL requirements. These included assumptions used in the ECL models applied in stage allocation, calculation of lifetime probability of default and methods applied to derive loss given default rates. We assessed the reasonableness of the forward looking information incorporated into the impairment calculations including assessing management's experts. We also challenged the multiple economic scenarios chosen and the weightings applied. This included benchmarking the economic data used to recognised external data sources. We tested a risk based sample of manually rated stage 1 and stage 2 loans (focusing our significant risk on those stage 2 loans closest to default) to ensure that they have been included in the correct stage in accordance with the Bank's methodology and IFRS 9. In examining a sample of DCF individually assessed Stage 3 loans cases, we challenged management on the judgments made regarding the application of default policy, collateral valuation and realisation time frames; and examined the credit risk functions analysis of data at a portfolio level. Where appropriate, this work involved assessing third party valuations of collateral, internal valuation guidelines, and external expert reports on borrowers' business plans. This allowed us to determine whether appropriate valuation methodologies were employed and assess 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 ECL allowances and the sensitivity of the allowance 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)

Valuation and recoverability of deferred tax asset	
Key audit matter description	The risk that projection of profitability over a long time period presents inherent uncertainty, involving significant management judgements and therefore inappropriate valuation of deferred tax assets. The Bank has recognised a deferred tax liability of £20.1 million (2018: asset of £3.2 million) at 31 December 2019 in respect of brought forward tax losses and other timing differences. This comprises a gross deferred tax asset of £31.3 million (2018: £40.5 million) and a gross deferred tax liability of £51.4 million (2018: £37.3 million). The gross deferred tax asset of £18.1 million (2018: £23.1 million) in respect of brought forward losses is based on the Bank's forecast profitability over a period of 5 years ending 31 December 2024 (2018: 5 years ending 31 December 2023) but has not recognised an asset in respect of these losses where utilisation is uncertain after this date. 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(d) to the financial statements. The key sources of estimate uncertainty in relation to deferred tax are disclosed in note 1(b) and further disclosures are presented in note 19 to the financial statements.
How the scope of our audit responded to the key audit matter	We have audited management's analysis supporting the recoverability and valuation of the deferred tax asset. We assessed the policy, process and governance in place over the recognition of the deferred tax asset. This included testing the design and implementation of controls over the completeness and accuracy of the year-end tax calculations and the forecast financial information. We challenged the key assumptions, both positive and negative, included in the calculation of the asset recognised, including the recovery period selected. We have challenged the adjustments recorded by management relating to non-taxable expenditure, made to the accounting profit to determine the taxable profit for accuracy. We assessed the ability of the Bank to recover the asset by auditing future approved profit forecasts, including discussing them with management. We recalculated the deferred tax asset based on future profit forecasts and challenging whether the recovery period selected is appropriate and independently benchmarked the recognition policy against peer Banks and industry norms. We agreed the accounting profit used in the model to the approved strategic plan for the years ending 31 December 2020 to 31 December 2024, and reviewed the adjustments to derive taxable profit for reasonableness. 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	Based on evidence obtained, we found that the assumptions used by management in the recognition of deferred tax assets are within a range we consider to be reasonable.

Key audit matters (continued)

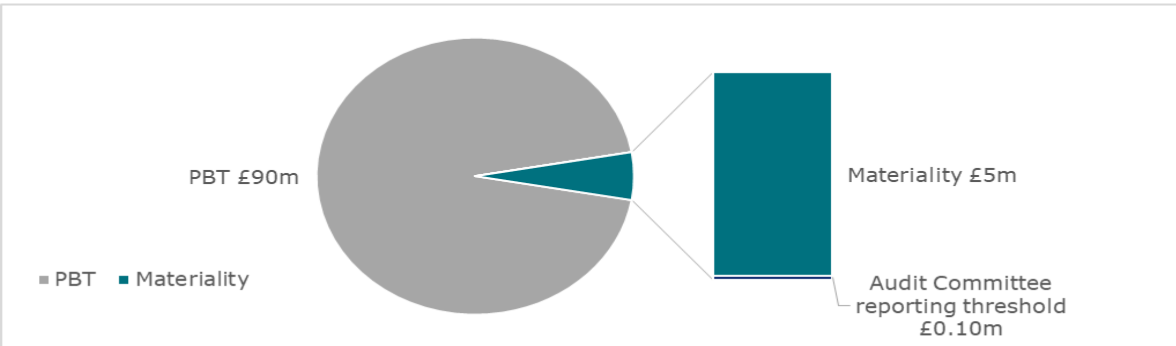
Valuation of defined benefit pension obligations	
Key audit matter description	Determining the key assumptions used to calculate the present value of defined benefit pension scheme obligations of £1,171 million (2018: £1,130 million) included in the pension surplus requires significant management judgement 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. We note that the selection of the discount, mortality 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 evaluated the design and determined the implementation of controls over the completeness and accuracy of the valuation of the pension obligation. We utilised Deloitte actuarial specialists as part of our team to assist us in evaluating the appropriateness of actuarial assumptions with particular focus on discount rates, mortality rates and inflation rates. Our work included inquiries with Management and the Bank's external actuaries to understand the processes and assumptions used in calculating defined benefit pension obligations. We benchmarked and audited the key assumptions that underpin the pension scheme liability, being discount rate, inflation rate and mortality rate, to ensure that they are reasonable and supportable. We evaluated and assessed the adequacy of disclosures made in the financial statements, including disclosures of the assumptions and sensitivity of the defined benefit obligation to changes in the underlying assumptions.
Key observations	Based on the evidence obtained, we concluded that the data and assumptions used by Management in the actuarial valuations for defined benefit obligations are within a range we consider to be reasonable.

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 (2018: £5,000,000)
Basis for determining materiality	5.6% (2018: 5.6%) of profit before tax. We maintained materiality at £5,000,000 consistent with the financial year ended 31 December 2018 as the balance sheet of Northern Bank Limited had not changed significantly. The percentage applied to profit before tax 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 (2018: £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

Scoping
We determined the scope of our audit 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 being audited by a separate audit team in Copenhagen, Denmark.

Due to the centralised structure of certain Danske A/S financial responsibilities, certain areas of audit testing are performed by the Group audit team in Copenhagen.

Audit testing is performed by the group audit team using materiality advised by Deloitte (NI) Limited and not that of the Danske A/S Group audit. Testing is supervised by the Northern Bank Limited audit team and additional review procedures are performed by the team based in Belfast. Regular meetings take place throughout the year to discuss procedures and review outputs.

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 respect of these matters.

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.

Details of the extent to which the audit was considered capable of detecting irregularities, including fraud and non-compliance with laws and regulations are set out below.

As part of an audit in accordance with ISAs (UK), we exercise 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).

The auditor communicates 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.

Auditor's responsibilities for the audit of the financial statements (continued)

For listed entities and public interest entities, the auditor also provides those charged with governance with a statement that the auditor has complied with relevant ethical requirements regarding independence, including the FRC's Ethical Standard, and communicates with them all relationships and other matters that may reasonably be thought to bear on the auditor's independence, and where applicable, related safeguards.

Where the auditor is required to report on key audit matters, from the matters communicated with those charged with governance, the auditor determines those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. The auditor describes these matters in the auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, the auditor determines that a matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Extent to which the audit was considered capable of detecting irregularities, including fraud

We identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and then design and perform audit procedures responsive to those risks, including obtaining audit evidence that is sufficient and appropriate to provide a basis for our opinion.

Identifying and assessing potential risks related to irregularities

In identifying and assessing risks of material misstatement in respect of irregularities, including fraud and non-compliance with laws and regulations, we considered the following:

- the nature of the industry and sector, control environment and business performance including the design of the Bank's remuneration policies, key drivers for Directors' remuneration, bonus levels and performance targets;
- the Bank's own assessment of the risk that irregularities may occur either as a result of fraud or error;
- results of our enquiries of management, internal audit, legal counsel and the audit committee about their own identification and assessment of the risks of irregularities;
- any matters we identified having obtained and reviewed the Bank's documentation of their policies and procedures relating to:
    - identifying, evaluating and complying with laws and regulations and whether they were aware of any instances of non-compliance;
    - detecting and responding to the risks of fraud and whether they have knowledge of any actual, suspected or alleged fraud;
    - the internal controls established to mitigate risks related to fraud or non-compliance with laws and regulations;
- discussing among the engagement team and involving relevant internal specialists, including tax, pensions and IT specialists regarding how and where fraud might occur in the financial statements and any potential indicators of fraud; and
- obtaining an understanding of the legal and regulatory framework that the Bank operates in, focusing on those laws and regulations that had a direct effect on the financial statements or that had a fundamental effect on the operations of the Bank. The key laws and regulations we considered in this context included the UK Companies Act, pensions legislation, tax legislation, as well as FCA/PRA guidance.

In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override.

In addition, we considered provisions of other laws and regulations that do not have a direct effect on the financial statements but compliance with which may be fundamental to the Bank's ability to operate or to avoid a material penalty.

Audit response to risks identified

As a result of performing the above, we identified the valuation of loan loss provisions, valuation and recoverability of the deferred tax asset, and the valuation of defined benefit pension obligations as key audit matters. The key audit matters section of our report explains the matters in more detail and also describes the specific procedures we performed in response to those key audit matters.

Our procedures to respond to risks identified included the following:

- reviewing the financial statement disclosures and testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described as having a direct effect on the financial statements;
- enquiring of management, the audit committee and in-house legal counsel concerning actual and potential litigation and claims;
- performing analytical procedures to identify any unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- reading minutes of meetings of those charged with governance, reviewing internal audit reports and reviewing correspondence with the PRA/FCA; and
- in addressing the risk of fraud through management override of controls testing the appropriateness of journal entries and other adjustments; assessing whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluating the business rationale of any significant transactions that are unusual or outside the normal course of business.

We also communicated relevant identified laws and regulations and potential fraud risks to all engagement team members including internal specialists, and remained alert to any indications of fraud or non-compliance with laws and regulations throughout the audit.

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

Adequacy of explanations received and accounting records

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 this matter.

Other matters

Audit tenure

Following the recommendation of the 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 5 years, covering the years ending 31 December 2015 to 31 December 2019.

Consistency of the audit report with the additional report to the audit committee

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

Use of our report

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.

John McCarroll, FCA (Senior Statutory Auditor)
for and on behalf of Deloitte (NI) Limited
Chartered Accountants and Statutory Auditor
Belfast, Northern Ireland

19 March 2020

NORTHERN BANK LIMITED
Income Statement
for the year ended 31 December 2019

	Note	2019 £'000	2018 £'000
Interest and similar income		205,645	197,628
Interest expense		(27,074)	(20,185)
Net interest income	2	178,571	177,443
Fee and commission income	3	52,030	56,522
Fee and commission expense	3	(7,276)	(7,781)
Net trading income	2	10,417	9,562
Other operating income	4	1,652	1,484
Non interest income		56,823	59,787
Operating income		235,394	237,230
Operating expenses	5	(139,688)	(142,058)
Depreciation and amortisation expense	15,16,17	(4,879)	(3,486)
Profit before loan impairment charge		90,827	91,686
Loan impairment charge	13	(797)	(2,896)
Profit before tax		90,030	88,790
Tax expense	8	(25,926)	(18,618)
Profit for the year		64,104	70,172
Portion attributable to:			
Shareholders of Northern Bank Limited		58,544	64,742
Additional Tier 1 capital holders		5,560	5,430
		64,104	70,172

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

The notes on pages 37 to 92 form part of these Financial Statements.

NORTHERN BANK LIMITED
Statement of Comprehensive Income
for the year ended 31 December 2019

	Note	2019 £'000	2018 £'000
Profit for the year		64,104	70,172
Items that will not be reclassified to profit or loss			
Other comprehensive income/(loss):			
Actuarial gain/(loss)recognised in retirement benefit scheme	23	34,531	(6,435)
Tax on actuarial gain/(loss) recognised in retirement benefit scheme	19	(8,633)	1,609
Gain on property revaluation	16	865	248
Tax on property revaluation transferred to revaluation reserve	19	(88)	91
Items that may be reclassified subsequently to profit or loss			
Property write down taken to income statement in year		(9)	-
Change in reserve for investment securities at fair value			
Unrealised value adjustments of bonds at fair value (OCI)		6,094	(2,477)
Tax	19	(1,523)	619
Change in cash flow hedge reserve			
Gains during the year	11	2,646	192
Tax	19	(662)	(48)
Total other comprehensive income/(loss)		33,221	(6,201)
Total comprehensive income for the year		97,325	63,971
Portion attributable to:			
Shareholders of Northern Bank Limited		91,765	58,541
Additional Tier 1 capital holders		5,560	5,430
Total comprehensive income for the year		97,325	63,971

The notes on pages 37 to 92 form part of these Financial Statements.

NORTHERN BANK LIMITED
Balance Sheet as at 31 December 2019

	Note	31 December 2019 £'000	31 December 2018 £'000
Assets			
Cash and balances at central bank	9	2,179,160	2,041,923
Items in the course of collection from other banks		30,804	40,137
Due from other banks	10	44,198	41,543
Derivative financial instruments	11	11,473	9,857
Investment securities	12	1,326,229	1,165,654
Loans and advances to customers	13	6,108,412	5,926,360
Investment in subsidiaries	14	250	250
Intangible assets	15	212	415
Property, plant and equipment	16	44,242	44,955
Right-of-use asset	17	6,899	-
Assets held for sale	18	485	526
Deferred tax assets	19	-	3,232
Defined benefit pension asset	23	195,883	150,260
Other assets	20	31,789	31,491
Total assets		9,980,036	9,456,603
Liabilities			
Due to other banks	21	373,024	372,624
Items in course of transmission to other banks		11,731	17,854
Derivative financial instruments	11	14,705	11,992
Deposits from customers	22	8,091,540	7,565,139
Notes in circulation		471,968	489,091
Deferred tax liabilities	19	20,106	-
Other liabilities	24	39,269	34,859
Provisions	25	5,038	4,122
Subordinated debt	26	126,000	126,000
Total liabilities		9,153,381	8,621,681
Equity			
Share capital	31	218,170	218,170
Share premium account		306,590	306,590
Revaluation reserve		35,906	35,602
Reserve for investment securities at fair value	32	1,594	(2,977)
Cash flow hedge reserve	33	2,132	148
Retained earnings		165,194	180,288
Shareholders of Northern Bank Limited		729,586	737,821
Additional Tier 1 capital holders	34	97,069	97,101
Total equity		826,655	834,922
Total liabilities and equity		9,980,036	9,456,603

The notes on pages 37 to 92 form part of these Financial Statements.

These Financial Statements were approved by the Board of Directors on 19 March 2020 and were signed on its behalf by:

Kevin Kingston
Director and Chief Executive Officer

Stephen Matchett
Deputy Chief Executive Officer and Chief Financial Officer

Company Number R0000568

NORTHERN BANK LIMITED
Statement of Changes in Equity
for the year ended 31 December 2019

	Note	Attributable to equity holders of the parent Share capital	Share premium	Revaluation reserve	Cash flow hedge reserve	Reserve for investment securities at fair value	Retained earnings	Total	Additional Tier 1 capital	Total
		£,000	£,000	£,000	£,000	£,000	£'000	£'000	£'000	£'000
At 1 January 2018		218,170	306,590	35,364	4	(1,119)	248,271	807,280	97,020	904,300
Profit for the year		-	-	-	-	-	64,742	64,742	5,430	70,172
Other comprehensive income/(loss):										
Actuarial loss recognised in retirement benefit scheme	23	-	-	-	-	-	(6,435)	(6,435)	-	(6,435)
Change in cash flow hedge reserve	11	-	-	(101)	-	-	101	-	-	-
Property revaluation	16	-	-	248	-	-	-	248	-	248
Property write down taken to income statement	16	-	-	-	-	(2,477)	-	(2,477)	-	(2,477)
Investment securities at fair value		-	-	-	192	-	-	192	-	192
Tax	19	-	-	91	(48)	619	1,609	2,271	-	2,271
Total other comprehensive income/(loss)		-	-	238	144	(1,858)	(4,725)	(6,201)	-	(6,201)
Total comprehensive income for the year		-	-	238	144	(1,858)	60,017	58,541	5,430	63,971
Transactions with owners:										
Dividends paid		-	-	-	-	-	(128,000)	(128,000)	-	(128,000)
Paid interest on Additional Tier 1 capital		-	-	-	-	-	-	-	(5,349)	(5,349)
		-	-	-	-	-	(128,000)	(128,000)	(5,349)	(133,349)
At 31 December 2018		218,170	306,590	35,602	148	(2,977)	180,288	737,821	97,101	834,922
Profit for the year		-	-	-	-	-	58,544	58,544	5,560	64,104
Other comprehensive income/(loss):										
Actuarial gain recognised in retirement benefit scheme	23	-	-	-	-	-	34,531	34,531	-	34,531
Transfer re property disposals		-	-	(464)	-	-	464	-	-	-
Property revaluation	16	-	-	856	-	-	-	856	-	856
Investment securities at fair value		-	-	-	-	6,094	-	6,094	-	6,094
Change in cash flow hedge reserve	11	-	-	-	2,646	-	-	2,646	-	2,646
Tax	19	-	-	(88)	(662)	(1,523)	(8,633)	(10,906)	-	(10,906)
Total other comprehensive income		-	-	304	1,984	4,571	26,362	33,221	-	33,221
Total comprehensive income for the year		-	-	304	1,984	4,571	84,906	91,765	5,560	97,325
Transactions with owners:										
Dividends paid		-	-	-	-	-	(100,000)	(100,000)	-	(100,000)
Paid interest on Additional Tier 1 capital		-	-	-	-	-	-	-	(5,592)	(5,592)
		-	-	-	-	-	(100,000)	(100,000)	(5,592)	(105,592)
At 31 December 2019		**218,170**	**306,590**	**35,906**	**2,132**	**1,594**	**165,194**	**729,586**	**97,069**	**826,655**

NORTHERN BANK LIMITED
Cash Flow Statement
for the year ended 31 December 2019

	Note	2019 £'000	2018 £'000
Cash flow from operating activities			
Profit before tax		90,030	88,790
Adjustments for:			
Tax paid		(12,264)	(18,821)
Adjustment for non-cash operating items:			
Amortisation of investment securities		4,429	6,982
Amortisation of intangible assets	15	203	108
Depreciation of property, plant and equipment	16	3,321	3,378
Depreciation of right-of-use asset	17	1,355	-
Loan impairment charges	40	797	2,896
Derivative financial instruments		1,097	(4,565)
Net defined benefit pension (credit)/expense	23	(3,066)	8,410
Other non-cash items		5,650	(3,850)
Total		91,552	83,328
Cash flow from operating capital			
Cash and balances at central bank - mandatory deposits	9	(246,796)	(62,945)
Items in transit		3,210	15,354
Loans and advances to customers		(182,849)	(523,352)
Due to other banks	21	400	(11,796)
Deposits		526,401	535,050
Notes in circulation		(17,123)	18,490
Defined benefit pension contributions	23	(8,026)	(10,844)
Other assets/liabilities		(267)	280
Cash flow from operations		166,502	43,565
Cash flow from investing activities			
Maturity of investments - hold to collect		100,000	151,000
Sale of investments - hold to collect		45,020	-
Sale of investments - hold to collect and sell		31,128	-
Purchase of investments - hold to collect		(230,791)	(38,754)
Purchase of investments - hold to collect and sell		(110,359)	(281,319)
Acquisition of intangible assets	15	-	(248)
Acquisition of tangible assets	16	(2,093)	(2,628)
Sale of tangible fixed assets		372	146
Cash flow from investing activities		(166,723)	(171,803)
Cash flow from financing activities			
Amounts drawn under the Term Funding Scheme		-	350,000
Dividends paid to parent		(100,000)	(128,000)
Payments of AT1 interest		(5,592)	(5,349)
Principal portion of lessee lease payments		(1,090)	-
Cash flow from financing activities		(106,682)	216,651
Cash and cash equivalents, beginning of year		1,114,257	1,025,844
Net change in cash and cash equivalents		(106,903)	88,413
Cash and cash equivalents, end of year		1,007,354	1,114,257
Cash in hand and demand deposits with central banks - non mandatory deposits	9	963,156	1,072,715
Deposits with credit institutions and central banks with terms shorter than 3 months	10	44,198	41,542
Total		1,007,354	1,114,257

1. Basis of preparation

(a) General

Northern Bank Limited is a private company limited by shares 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.

On 1 January 2019, the Bank implemented IFRS 16, Leases, and amendments to various standards (IFRS 9, Prepayment Features with Negative Compensation). The Bank has decided to early adopt the amendments to IFRS 9, IAS 39 and IFRS 7 included in the IASB's project 'Interest Rate Benchmark Reform'.

Further information on the implementation of IFRS 16 can be found in notes 1(c) and 17. Except for these changes, the Bank has not changed its significant accounting policies from those applied in 2018.

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 14).

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 sources of estimation uncertainty are set out below.

In preparing the Financial Statements, the Bank makes estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. As management judgement involves an estimate of the likelihood of future events, actual results could differ from those estimates, which could affect the future reported amounts of assets and liabilities. The estimates and judgements that have had the most significant effect on the amounts recognised in the Bank's Financial Statements are set out below.

Measurement of expected credit losses on loans measured at amortised cost

The three-stage expected credit loss impairment model in IFRS 9 depends on whether the credit risk has increased significantly since initial recognition. If the credit risk has not increased significantly, the impairment charge equals the expected credit losses resulting from default events that are possible within the next 12 months (stage 1). If the credit risk has increased significantly, the loan is more than 30 days past due, or the loan is in default or otherwise impaired, the impairment charge equals the lifetime expected credit losses (stage 2 and 3). In determining the impairment for expected credit losses, management exercises judgement and uses estimates and assumptions as explained below.

In determining the expected credit losses, management is required to exercise judgement in defining what is considered a significant increase in credit risk. The expected credit loss is calculated for all individual facilities as a function of probability of default (PD), exposure at default (EAD) and loss given default and incorporates forward-looking information. The estimation of expected credit losses involves forecasting future economic conditions over a number of years. Such forecasts are subject to management judgement and those judgements may be sources of measurement uncertainty that have a significant risk of resulting in a material adjustment to a carrying amount in future financial periods.

The incorporation of forward-looking elements reflects the expectations of the Bank's senior management and involves the creation of scenarios (base case, upside and downside), including an assessment of the probability for each scenario. The purpose of using multiple scenarios is to model the non-linear impact of assumptions about macroeconomic factors on the expected credit losses.

The base case scenario is the primary forward-looking economic information driving the calculation of expected credit loss. Expected credit loss is also estimated under an upside and a downside macroeconomic scenario. The base case scenario enters the calculation with a probability of 60%, the downside scenario with a probability of 30% and the upside scenario with a probability of 10%.

Under the base case, economic growth in Northern Ireland remains modest in the short-term, before rising later in the horizon period. Focusing on the short term there is solid growth in household spending power and consumer spending is the main driver of economic growth. Brexit-related uncertainty continues to act as a drag on business investment and the slower rate of global economic growth leads to adverse consequences for exports from Northern Ireland and the rest of the UK. The unemployment rate gradually picks up under the base case as the rate of jobs growth slows and house price growth remains positive throughout the horizon period. Monetary policy remains relatively accommodative throughout the horizon period.

Under the downside scenario, it is assumed that the UK Government does not take up the option to extend the transition period past the end of December 2020 and that the Government is not able to negotiate and ratify a new free trade agreement with the EU in such a short period of time, and so from the beginning of 2021, the UK finds itself out of the EU with no beneficial trading relationship i.e. effectively a 'no-deal' Brexit from a trade perspective. On top of the Brexit-related impacts included within this scenario, economic growth is also negatively impacted by rising trade protectionism and geopolitical uncertainty, both of which lead to lower global economic growth than under the base case which poses additional challenges to exporting businesses in Northern Ireland.

Under the upside scenario, the UK Government is very transparent on progress made during the talks on the post-Brexit, long-term UK-EU relationship and on many areas, pursues more business friendly policies. Global economic growth is also stronger than under the base case as some of the concerns about rising trade protectionism begin to dissipate.

The table below gives the average current year macroeconomic assumptions in the period 2020-2022 under the three scenarios considered.

Economic assumption	Measurement	Base Case	Upside scenario	Downside scenario
Northern Ireland GVA	Annual % change	1.4	1.7	(0.6)
Northern Ireland unemployment rate	Annual average	4.0	3.7	5.2
Northern Ireland house prices	Annual % change	3.6	4.0	(3.1)
UK CPI inflation rate	Annual average	2.0	2.0	2.6
Bank of England base rate	Annual average	0.8	0.9	0.2

1. Basis of preparation (continued)

(b) Significant accounting estimates (continued)

The table below gives the average prior year macroeconomic assumptions in the period 2019-2021 under the three scenarios considered.

Economic assumption	Measurement	Base Case	Upside scenario	Downside scenario
Northern Ireland GVA	Annual % change	1.5	1.3	(2.1)
Northern Ireland unemployment rate	Annual average	4.1	4.4	8.0
Northern Ireland house prices	Annual % change	4.2	3.9	(8.3)
UK CPI inflation rate	Annual average	2.0	2.1	3.8
Bank of England base rate	Annual average	1.2	1.1	0.0

Measurement of expected credit losses on loans measured at amortised cost

Based on these assessments, the allowance account at 31 December 2019 amounted to £83,281,000 (2018: £95,813,000). If the base case scenario was assigned a probability of 100%, the allowance account would decrease by £14,550,000 (2018: £7,575,000). The allowance account would increase by £34,961,000 (2018: £75,614,000) if the downside scenario was assigned a probability of 100%. If instead the upside scenario was assign a probability of 100%, the allowance account would decrease by £17,584,000 (2018: £9,364,000). Scenario sensitivities are primarily driven by both the changes in the macroeconomic assumptions applied at each year end (as outlined in the macroeconomic assumption tables) and the macroeconomic assumptions and probability weightings applied to each scenario in the assessment of the allowance account as at 31 December 2019. However, it shall be noted that the expected credit losses in the individual scenarios does not represent expected credit loss (ECL) forecasts.

Note 40 and the section on credit risk in the risk management notes provide more details on expected credit losses. At 31 December 2019, loans and advances to customers accounted for about 61.2% of total assets (2018: 62.7%).

Recognition of deferred tax asset

A deferred tax asset of £18,060,000 (2018: £23,830,000) is recognised for unused tax losses 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/decreased by 10% per annum, this would lead to an increase/decrease in the deferred tax asset of £2.0m.

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 five year period to 31 December 2024 i.e. the current corporate planning horizon. If the time period for expected profits was increased/decreased by one year this would lead to an increase/decrease in the deferred tax asset of £4.5m.

Defined benefit pension scheme

As disclosed in note 23 the Bank operates a defined benefit pension scheme with a surplus at 31 December 2019 of £195,883,000 (2018:£150,260,000). 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 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

At 1 January 2019, the Bank implemented IFRS 16, Leases and amendments to various standards (IFRS 9, Prepayment Features with Negative Compensation. The Bank has decided to early adopt the amendments to IFRS 9, IAS 39 and IFRS 7 included in IASB's project 'Interest Rate Benchmark Reform'.

The sections below explain the key impacts of the changes in accounting policies implemented.

IFRS 16, Leases

IFRS 16 provides revised principles for lessees, and requires lessees to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of a low value. The lease payments associated with short-term leases and leases for which the underlying asset is of low value is recognised in profit and loss as an expense. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, there are no changes to the Bank's accounting policy for lessor accounting.

As allowed under the transitional provisions of IFRS 16, the Bank uses the cumulative catch up approach. Accordingly, the Bank has not restated comparative information. The implementation of IFRS 16 had an impact on the balance sheet at 1 January 2019. A right-of-use asset for £8.3m was recognised and corresponding liabilities of £7.4m and £0.9m recognised in Other Liabilities and Provisions respectively. The Bank has excluded initial direct costs from the measurement of the right-of-use lease asset at the date of initial application, and the Bank has relied on the Bank's assessment of whether leases are onerous, applying IAS 37 immediately before the date of initial application. There has been no implementation impact on shareholders' equity and an immaterial effect on the Bank's capital ratios. The Bank has used hindsight in determining the lease tem at initial application. At 1 January 2019, the Bank's weighted average incremental borrowing rate applied to the lease liabilities was 1.5 % for right-of-use assets.

In the income statement, expenses related to leases are presented as depreciation expenses and interest expenses. As the interest expenses are calculated on the reducing balance of the lease liabilities while the depreciation is charged on a straight-line basis, the costs under IFRS 16 are front loaded compared to under IAS 17. The impact of this front loading has had an immaterial impact in the income statement.

Amendment to IFRS 9, Financial Instruments

The amendment to IFRS 9, Financial Instruments, relates to the SPPI test, and the requirement that a prepayment option will only be consistent with 'basic lending features' if the prepayment amount represents the principal amount outstanding plus accrued interest and may include a reasonable additional compensation for early termination (i.e. the party exercising the right cannot receive a compensation for the early termination). The word 'additional' has now been removed. After the implementation of the amendment, compensation that reflects changes in the relevant benchmark interest rate will be consistent with the SPPI test, regardless of whether the compensation is positive or negative. The implementation of the amendment had no impact on the classification of financial instruments between fair value measurement and amortised cost.

Amendment to IFRS 9/ IAS 39, Financial Instruments, and IFRS 7, Financial Instruments: Disclosures

The amendments to IFRS 9/IAS 39 and IFRS 7 cover issues related to the pre-replacement issues following the ongoing Interest Rate Benchmark Reform that could result in discontinuation of hedge accounting relationships. The effective date of the amendments is 1 January 2020 with earlier application permitted. In the fourth quarter of 2019, the Bank has early adopted the amendments. The Bank uses the option in IFRS 9 to continue to apply hedge accounting using the requirements in IAS 39 and so the amendments to IAS 39 have been early adopted.. The amendments to IAS 39 implies, that for the purpose of the assessment of the prospective hedge effectiveness it shall be assumed that the benchmark reform uncertainty will not alter the cash flows and that a hedging relationship is not required to be discontinued if the actual results of the effectiveness exceeds the 80%-125% limit.

Standards and interpretations not yet in force

The International Accounting Standards Board (IASB) has issued amendments to existing international accounting standards (IFRS 3, IFRS 7, IFRS 9, IAS 1, IAS 8, IAS 39) that have not yet come into force. Further, several standards were amended to incorporate reference to the revised Conceptual Framework for Financial Reporting that has not yet come into force. The Bank has early adopted the changes in IASB's Interest Rate Benchmark Reform, which included amendments IFRS 9, IAS 39 and IFRS 7, see further in the above section. The Bank has not early adopted any of the other changes and no significant impact 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.

Classification and measurement of financial assets and financial liabilities under IFRS 9

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, if any) into one of the following measurement categories:
- Amortised cost (AMC)
- Fair value through other comprehensive income (FVOCI)
- Fair value through profit or loss (FVPL)

Financial assets are measured at AMC if they are held within a business model for the purpose of collecting contractual cash flows (hold 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 for the purpose of both collecting contractual cash flows and selling (hold 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 are reclassified to the income statement.

1. Basis of preparation (continued)

(d) Accounting policies (continued)

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.

Generally, financial liabilities are measured at amortised cost with bifurcation of embedded derivatives not closely related to the host contract. Financial assets 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 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 "hold to collect" and "hold to 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 less any subsequent repayment. The interest must 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 is not consistent with basic lending features, the financial asset is mandatorily recognised at FVPL.

In general, the SPPI test of the Bank's portfolios of financial assets, that are "hold to collect" or "hold to collect and sell", have contractual cash flows that are consistent with the SPPI test, i.e. they have basic lending features.

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 that are an integral part of the effective interest rate on loans. 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 for expected credit losses. The difference between the value at initial recognition and the redemption value is amortised over the term to maturity as part of the effective interest and recognised under Interest income. If fixed-rate loans and

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 charge 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 loan is transferred to stage 2 and an impairment charge equal to the lifetime expected credit losses is recognised;
- Stage 3: If the loan is in default or otherwise credit impaired, it is transferred to stage 3, for which the impairment charge continues to equal the lifetime expected credit losses but with interest income being recognised on the net carrying amount.

The expected credit loss is calculated for all individual facilities as a function of the probability of default (PD), the exposure at default (EAD) and the loss given default (LGD) and incorporates forwards looking elements. For facilities in stage 2 and 3, the lifetime expected credit losses cover the expected remaining lifetime of a facility. Expected credit loss impairments are booked in an allowance account and allocated to individual exposures.

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.

1. Basis of preparation (continued)

(d) Accounting policies (continued)

Investment securities - Financial assets measured at amortised cost (AMC)

The financial assets consist of bonds held within a business model for the purpose of collecting the contractual cash flows (hold to collect) and with cash flows that are solely payments of principal and interest on the principal amount outstanding (i.e. that passes the SPPI test in IFRS 9). 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. The bonds are subject to the expected credit loss model in IFRS 9 as described in note 40. The interest rate risk on fixed-rate bonds is not hedged.

Investment securities - Financial assets measured at fair value through other comprehensive income (FVOCI)

The financial assets comprise of bonds only, and primarily bonds listed in a liquid market. The bonds are held within a business model for the purpose of collecting contractual cash flows and selling (hold to collect and sell). The bonds have cash flows that are solely payments of principal and interest on the principal amount outstanding (i.e. that passes the SPPI test in IFRS 9). FVOCI results in the assets being recognised at fair value in the balance sheet and at amortised cost in the income statement, including the recognition of expected credit losses as described in note 40. Hence, gains and losses, except for expected credit losses and foreign exchanges gains and losses, are recognised in other comprehensive income until the bond is derecognised. When a fixed interest rate risk is hedged in a hedge that qualifies for fair value hedge accounting, the fair value changes of the hedged interest risk is further presented in the income statement under Net trading income. When bonds are sold unrealised value adjustments recognised under Other comprehensive income are reclassified to the income statement and presented under Net trading income. The Bank recognises interest income 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.

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 that were 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.

Right of use lease assets and lease liabilities

The Bank recognises a right-of-use asset and a lease liability at the commencement date, for all lease agreements, that the Bank has entered into as lessee, except short-term leases and leases of low value assets. The lease liability is initially measured as the present value of the future payments from lease components, discounted using the incremental borrowing rate for the individual lease. The lease liability is subsequently measured by increasing the carrying amount, to reflect interest and by reducing the carrying amount to reflect the lease payments made. Further, lease liabilities are changed when remeasurements are needed, with the corresponding adjustment to the related right-of-use asset. Gain or loss from a lease modification, not accounted for as a separate lease, is recognised in profit and loss. The initial right-of-use asset comprises the amount of the initial measurement of the lease liability, lease payments made at or before the commencement date, initial direct costs and costs to restore the underlying asset. The right-of-use asset is subsequently measured at cost less accumulated depreciation and impairment losses. The right-of-use assets are depreciated over the shorter period of the lease term and the useful life of the underlying asset.

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.

Loan commitments and guarantees

The Bank issues a number of loan commitments and guarantees. Such instruments are valued at the higher of the received premium amortised over the life of the individual obligation and the provision made, if any. 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. Loan commitments are discounted in accordance with the interest terms. Loan commitments and guarantees are subject to the expected credit loss impairment model in IFRS 9.

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 their likelihood of occurrence is considered remote.

Additional Tier 1 capital

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 IAS 32. 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.

1. Basis of preparation (continued)

(d) Accounting policies (continued)

Staff costs

This item includes salaries, performance-based pay, expenses for share-based payments, pension costs and other remuneration. Salaries and other remuneration the Bank expects to pay are expensed when the employees render the services. Performance-based remuneration is expensed as it is earned.

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 provided defined benefits based on years of service and career averaged revalued earnings up until 30 September 2018. 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.

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.

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.

1. Basis of preparation (continued)

(d) Accounting policies (continued)

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.

Interest income and expenses

Interest income and expenses arising from interest-bearing financial instruments measured at amortised cost and bonds at fair value through Other comprehensive income are recognised according to the effective interest rate 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 financial instruments included in stage 3 for the calculation of expected credit losses is recognised on the basis of the carrying amount (net of impairment charges). The interest rate risk on some fixed rate loans and advances to customers recognised at amortised cost is hedged by derivatives using fair value hedge accounting. Note 11 provides more information on hedge accounting. Interest income calculated using the effective interest method and presented as a separate line item in the income statement excludes the impact from hedge accounting.

Further, interest income and expenses includes interest on financial instruments measured at fair value through profit or loss.

Net trading income

Net trading income includes realised and unrealised capital gains and losses on financial assets and financial liabilities recognised at fair value through profit or loss.

For financial assets and liabilities subject to fair value hedge accounting, the fair value adjustments of the hedged financial instrument and the hedging instruments are recognised in Net trading income. Therefore, any hedge ineffectiveness is presented in Net trading income.

Fee income and expenses

Fee income is recognised to reflect the transfer of services to customers at an amount that reflects the consideration that is expected to be received in exchange for such services. The Bank identifies the performance obligation agreed with the customer and the consideration, and recognises income in line with the transfer of services, the performance obligation, agreed with the customer.

For each performance obligation identified, the Bank determines at contract inception whether it satisfies the performance obligation over time or at a point in time, whether the consideration is fixed or variable, including whether consideration is constrained due, for instance, to external factors outside the Bank's influence. Consideration is subsequently allocated to the identified performance obligation.

2. Net interest and net trading income

	2019 £'000	2018 £'000
Interest income		
Financial assets at amortised cost:		
Due from other banks and central bank	14,448	12,160
Investment securities - hold to collect	5,680	6,674
Investment securities - hold to collect and sell	4,230	2,474
Loans and advances to customers	179,282	173,974
Interest income on defined benefit pension scheme surplus (Note 23)	4,200	4,100
	207,840	199,382
Financial portfolios at fair value:		
Derivative financial instruments	(2,195)	(1,754)
Total interest income	205,645	197,628
Interest expense		
Due to other banks	4,103	3,155
Deposits from customers	19,410	13,800
Subordinated debt	3,403	3,230
Interest expense on lease liabilities	158	-
Total interest expense	27,074	20,185
Net interest income	178,571	177,443
Net trading income		
Net gain on financial instruments at fair value	1,150	318
Margin on foreign exchange brokerage	9,267	9,244
	10,417	9,562

Interest income includes £332,000 (2018: £601,000) received from Danske Bank A/S.

3. Fee and commission income/expense

	2019 £'000	2018 £'000
Fee income		
Financing (loans, advances and guarantees)	7,081	7,933
Investment (securities trading)	326	543
Services (payment services)	44,623	48,046
Total	52,030	56,522
Fee expenses		
Financing (loans, advances and guarantees)	748	797
Investment (securities trading)	89	107
Services (payment services)	6,439	6,877
Total	7,276	7,781

4. Other operating income

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

	2019 £'000	2018 £'000
Other income	1,652	1,484
Total	1,652	1,484

5. Operating expenses

	2019 £'000	2018 £'000
Staff costs		
- wages and salaries	45,496	43,289
- social security costs	4,589	4,514
- pension costs		
- defined benefit cost (Note 23)	-	9,168
- past service cost (Note 23)	147	2,527
- defined contribution	7,139	2,956
	57,372	62,454
Property related expenses	7,588	8,590
Information technology expenses	24,864	25,514
Administrative expenses	49,864	45,500
	139,688	142,058

Operating expenses include net recharges from Danske Bank A/S of £37,118,000 (2018: £33,969,000).

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

6. Operating profit

	2019 £'000	2018 £'000
This is stated after:		
Income		
Aggregate amounts receivable, including capital repayments under finance leases and hire purchase contracts (net of depreciation £132,798,000 (2018: £137,031,000))	8,900	9,109
Charges		
Depreciation of tangible fixed assets (Note 16)	3,321	3,378
Depreciation of right-of-use assets (Note 17)	1,355	-
Amortisation of intangible fixed assets (Note 15)	203	108
Loss on disposal of property, plant and equipment	11	4
Expenses relating to short term and low value leases*	378	2,035
Hire of computers and equipment	533	565
Auditor's remuneration		
Audit of these Financial Statements		
- Audit fee	138	138
- IFRS reporting requirements	40	40
Amounts receivable by the auditor and their associates in respect of:		
- Audit of the financial statements of subsidiary companies	28	28
- Other assurance services	75	75
	281	281

*On 1 January 2019 the Bank implemented IFRS 16, Leases, as set out in Note 1(c). Comparatives under IAS 17, Leases, have not been restated.

7. Directors' emoluments

	2019 £'000	2018 £'000
Aggregate emoluments	2,325	1,788
Bank pension contributions to money purchase pension schemes	18	28
	2,343	1,816

In addition to the amounts shown above, social security costs were payable in respect of emoluments to Directors amounting to £337,000 (2018: £252,000). This includes £144,000 in respect of the emoluments of the highest paid Director in the year ended 31 December 2019 (2018: £105,000).

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 (2018: three) and10,832 were exercised during the year (2018: 3,778 shares). Further details are disclosed in note 43 of the Financial Statements. For the year ended 31 December 2019 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 (2018: Two) accrued retirement benefits under a money purchase pension scheme and no Director (2018: 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 £1,015,000 (2018: £732,000). Of these emoluments, £354,000 (2018: £233,000) was in connection to services provided at the specific request of Danske Bank A/S and in respect of which the Bank was reimbursed. The Director is a member of the Northern Bank Defined Contribution Pension Scheme to which the Bank paid contributions of £Nil (2018: £Nil) on his behalf. The highest paid Director exercised conditional shares during the year.

8. Tax expense

	2019 £'000	2018 £'000
Current tax		
UK corporation tax		
Current year	10,333	10,315
Current year - corporation tax surcharge on Banking profits	3,801	4,191
Adjustment in respect of prior years	(640)	395
	13,494	14,901
Deferred tax note (Note 19)		
Current year	9,353	6,906
Adjustment in respect of prior years	599	(54)
Derecognition/(recognition) of tax losses in the year	2,480	(3,135)
	12,432	3,717
Tax charge	25,926	18,618

The effective taxation rate for the year ended 31 December 2019 is a charge of 28.8% (2018: 21.0%).

The tax assessed for the year differs from the standard rate of corporation tax in the UK (19.0%). A reconciliation from the expense implied by the standard rate to the actual tax expense is as follows:

	2019 £'000	2018 £'000
Profit on ordinary activities before tax	90,031	88,792
Tax charge based on the standard rate of Corporation Tax in the UK of 19.0% (2018: 19.0%)	17,106	16,870
Effects of:		
Additional Tier 1 payments	-	(1,016)
Expenses not deductible for tax purposes	903	250
Rate differences	(104)	(1,481)
Adjustments in respect of prior years	(41)	341
Derecognition/(recognition) of tax losses in the year	2,480	(3,135)
Effect of corporation tax surcharge on Banking profits	5,582	6,789
	25,926	18,618

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.

8. Tax expense (continued)

During the 2019 General Election campaign, the Conservative Party announced their intention to reverse the rate reduction, such that temporary differences unwinding after 1 April 2020 will do so at a rate of 19% instead of 17%. This has not been reflected in the disclosures as the change to 19% has not yet been substantively enacted.

The United Kingdom left the European Union on 31 January 2020, and has entered a transitional period until 31 December 2020. It is not expected that either of these events will have a material impact on tax balances included within the Financial Statements.

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 19, Deferred Tax.

9. Cash and balances at central bank

	2019 £'000	2018 £'000
Cash in hand	349,725	624,764
Balances at central bank	1,829,435	1,417,159
	2,179,160	2,041,923

Cash and balances at central bank include mandatory deposits of £1,216,004,000 (2018: £969,208,000) 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 held with the objective of collecting the contractual cash flows and therefore classified as "hold to collect" under IFRS 9. These amounts have basic lending features with the contractual cash flows solely representing the repayment of principal and interest on the principal amount outstanding i.e. the SPPI test. As a result these amounts are recognised at amortised cost.

Amounts due from other banks are stated at amortised cost.

	2019 £'000	2018 £'000
Other amounts due	44,198	41,543

	2019 £'000	2018 £'000
Analysed by remaining maturity:		
- on demand or at short notice	44,198	41,543

	2019 £'000	2018 £'000
Amounts include:		
Due from parent and fellow subsidiary undertakings	40,794	33,800

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

	2019 £'000	2018 £'000
Derivatives with positive fair value	11,473	9,857

(b) Trading portfolio liabilities

	2019 £'000	2018 £'000
Derivatives with negative fair value	14,705	11,992

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 2019				
Currency contracts				
Forwards	378,385	7,300	288,884	5,511
Interest rate contracts				
Swaps	425,293	4,168	691,122	9,189
Options	38,186	5	39,838	5
Total derivatives	841,864	11,473	1,019,844	14,705
Counterparty				
Ultimate parent and fellow subsidiary undertakings	706,996	8,756	877,044	10,092
Other	134,868	2,717	142,800	4,613
Total	841,864	11,473	1,019,844	14,705

	Positive Fair Value		Negative Fair Value	
	Notional amount £'000	Carrying amount £'000	Notional amount £'000	Carrying amount £'000
At 31 December 2018				
Currency contracts				
Forwards	396,088	7,885	356,075	6,513
Options	7,634	98	7,634	98
Interest rate contracts				
Swaps	354,259	1,815	387,395	5,321
Options	52,675	59	52,675	60
Total derivatives	810,656	9,857	803,779	11,992
Counterparty				
Ultimate parent and fellow subsidiary undertakings	620,983	4,597	702,270	9,384
Other	189,673	5,260	101,509	2,608
Total	810,656	9,857	803,779	11,992

11. Trading portfolio assets and liabilities (continued)

(d) Fair value hedge accounting

The Bank manages the fixed interest rate risk on financial assets and liabilities measured at amortised cost as a combination of economic hedges (matching of interest rate risk from assets and liabilities at amortised cost) and hedges using interest rate swaps. Treasury is responsible for the risk management of the interest rate risk (the so-called interest rate risk in the banking book). In the risk management process, economic hedges are established and/or identified. This includes the acquisition of 'hold to collect' fixed interest rate bonds in Treasury and the identification of fixed-rate loans extended by the Bank's banking units to hedge the fixed interest rate risk on liabilities (including core demand deposits). Interest rate risk on certain fixed-rate assets can be hedged using derivatives.

When the Bank uses swaps to hedge the fixed interest rate risk on financial instruments, the Bank applies fair value hedge accounting using the option in IFRS 9 to continue to apply the fair value hedge accounting provisions in IAS 39. Fair value hedge accounting can be applied if changes in the fair value of the hedging swaps are expected to be effective in offsetting changes in the fair value of the hedged fixed interest rate risk. This requires (1) a formal designation and documentation of the hedging relationship, including a risk management objective and strategy for the hedge, (2) that the hedge is expected to be highly effective in achieving offsetting changes in fair value of the hedged interest rate risk, (3) the effectiveness of the hedge can be reliably measured and (4) the hedge on an ongoing basis has proven to be effective in actually offsetting of changes in fair value. 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 on the hedged item and the hedging swaps are presented in the Income statement under Net trading income. Any ineffective portion of a hedge that lies within the range for effective hedging is therefore also included under Net trading income.

The interest rate is considered fixed if the interest rate resets to a reference rate with a term longer than three months. Once a financial instrument has been designated as a hedged item it will remain as a hedged item for the life of the instrument. For hedged assets to which a fixed rate of interest applies for a specified period of time starting at the commencement date of the agreement, future interest payments are split into basis interest and a customer margin and into periods of time. By entering into swaps or forwards with matching payment profiles in the same currencies and for the same periods, the Bank hedges the risk at portfolio level from the commencement date of the hedged items. 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. Portfolios of hedging derivatives are adjusted if necessary.

The primary reasons for changes in the fair value of fixed interest rate financial assets are changes in the interest rate risk and the credit risk.

Hedge ineffectiveness relates to the fact that the fair value change of the hedged items being measured based on the interest rate curve relevant for each hedged item while the fair value of the hedging fixed leg in the derivatives is measured based on a swap curve. Further, the adjustment of the portfolios of hedging two derivatives to changes in hedged position is not done instantly, and some hedge ineffectiveness can therefore exist.

The ongoing Interest Rate Benchmark Reform will replace existing benchmark inter-bank offered rates (IBORs) with alternative risk-free rates. There is currently uncertainty as to the timing and the methods of transition for the different IBORs and whether some existing benchmarks will continue to be supported in some way. The Bank's hedging activities are also exposed to interest benchmarks that are expected to be replaced by new risk-free rates, most notably, the replacement of LIBOR rates. Primarily for LIBOR benchmark rates, uncertainty relating to future development and transition still remains. In response to the Interest Rate Benchmark Reform, the Bank has established an IBOR change programme to address the impacts for both itself and its customers; as part of this, the Bank is examining how it will manage its current and future hedge accounting.

In the fourth quarter of 2019, the Bank has early adopted the amendments to IAS 39 issued by IASB in September 2019 (Interest Rate Benchmark Reform) which, for the assessment of effectiveness of such hedges, assumes that the benchmark reform will not alter the cash flows. Further, a hedge will not disqualify if the actual result of the hedge falls outside the band of 80-125%, if the other requirements for applying hedge accounting is fulfilled. The relief covers the period during which uncertainty on the timing and the amount of the amended or replaced reference rates exists. Based on this, the current uncertainty in relation to reference rates that have not yet been amended or replaced does not have an impact on the Bank's ability to use fair value hedge accounting on existing hedging relationships.

At 31 December 2019 the carrying amounts of effectively hedged fixed rate assets were £487,149,000 (2018: £449,753,000). 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.

	2019	2018
	£'000	£'000
Effect of interest rate asset hedging on profit		
Hedged loans and advances to customers	**5,157**	(3,329)
Hedging derivatives	**(5,084)**	3,307
Total	**73**	(22)

11. Trading portfolio assets and liabilities (continued)

(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	366,000	3,093	190,000	130

These hedges are included in the derivatives table above.

	2019 £'000	2018 £'000
Derivatives held as cash flow hedges	556,000	245,000

	2019 £'000	2018 £'000
Gains recognised in Other Comprehensive Income for the year	2,646	192

12. Investment securities

(a) Hold to collect (securities at amortised cost)

	2019 £'000	2018 £'000
Issued by public bodies		
Investment securities		
- listed	595,554	518,082
Unamortised premiums/(discounts)		
- on investment securities	9,554	17,082

(b) Hold to collect and sell (securities measured at FVOCI)

	2019 £'000	2018 £'000
Listed investments	730,675	647,572

The liquidity portfolio is part of the balance sheet management to optimise the balance sheet composition, to hedge the interest rate risk in the banking book and to manage the Bank's liquidity need. The management of the interest rate risk in the banking book is carried out through a combination of hedges with derivatives and partly through matching of the duration on the fixed interest rate deposits (the interest risk on core deposits) and with investment securities with a matching duration.

12. Investment securities (continued)

(b) Hold to collect and sell (securities measured at FVOCI) (continued)

Financial assets measured at amortised cost (AMC)
This portfolio includes the part of the liquidity bond portfolio that is held in a business model being 'hold to collect' the contractual cash flows, (i.e. with the purpose of generating a return until maturity). Further, the bonds included in the portfolio have contractual cash flows that pass the SPPI test.

The performance is measured based on the collection of the contractual cash flows. The fair value of the portfolio is monitored for liquidity purposes as the bonds can be used in repo transactions. Sales from the portfolio are infrequent. When sales are made they reflect:
- sales close to maturity (the proceeds from the sale approximate the collection of contractual cash flows);
- sales are managed to risk concentration; and
- sales due to increase in credit risk above a certain level (i.e. outside the investment policy)

The bonds are primarily UK government securities and highly rated covered, sovereign supernational and agency bonds.

Financial assets measured at fair value through other comprehensive income (FVOCI)
This portfolio includes the part of the liquidity bond portfolio where both the collection of the contractual cash flows and sales are an integrated part of achieving the objectives with the acquired bond portfolio. Further, the bonds included in the portfolio have contractual cash flows that pass the SPPI test.

The performance of the portfolio is measured on a combination of the collection of the contractual cash flows and sales proceeds. Sales typically occur when market opportunities arise, or when there is a need to adjust the portfolio to hedge part of the interest rate risk on the Bank's core deposits. There is no objective of short-term profit taking, and the performance reporting related to this portfolio reflects a combination of the collection of the contractual cash flows and realising fair value market changes. The business model is therefore 'hold to collect and sell'.

The portfolio comprises primarily highly rated covered, sovereign, supernational and agency bonds.

SPPI test applied for bonds at FVOCI or AMC
The SPPI test is applied for each bond to assess that the contractual cash flows represents repayment of principal amount and interest on the principal amount outstanding. Bonds that are included in the portfolios at FVOCI or AMC are generally plain 'vanilla' bonds that:
- have a fixed maturity, i.e. no perpetual bonds;
- do not have terms that introduce exposure to risk or volatility, e.g. by a yield that refers to changes in equity or commodity prices;
- are not subordinated or convertible bonds; and
- can be prepaid (e.g. at par plus accrued interest), with the fair value of the prepayment option being insignificant at initial recognition. In general, this will be the case if the premium/discount to the contractual par amount is insignificant at initial recognition.

13. Loans and advances to customers

Loans and advances to customers are held with the objective of collecting the contractual cash flows and therefore classified as "hold to collect" under IFRS 9. These loans and advances have basic lending features with the contractual cash flows solely representing the repayment of principal and interest on the principal amount outstanding i.e. the SPPI test. As a result these loans and advances are recognised at amortised cost.

Loans and advances to customers are stated at amortised cost.

	2019	2018
	£'000	£'000
Analysed by remaining maturity:		
- on demand or at short notice	1,162,819	1,180,433
- 3 months or less	336,007	348,396
- 1 year or less but over 3 months	360,288	468,855
- 5 years or less but over 1 year	1,482,341	1,449,781
- over 5 years	2,846,342	2,570,990
	6,187,797	6,018,455
Allowance account	(79,385)	(92,095)
	6,108,412	5,926,360

13. Loans and advances to customers

Reconciliation of loans and advances to customers

	Stage 1	Stage 2	Stage 3	Total
	£'000	£'000	£'000	£'000
Gross carrying amount at 1 January 2019	5,104,406	591,520	322,529	6,018,455
Transferred from Stage 1 to Stage 2	(185,703)	185,703	-	-
Transferred from Stage 2 to Stage 1	173,775	(173,775)	-	-
Transferred from Stage 3 to other stages	2,264	25,912	(28,176)	-
Transferred to Stage 3 from other stages	(67,492)	(33,000)	100,492	-
New assets*	1,201,637	123,365	11,007	1,336,009
Assets derecognised*	(722,129)	(55,574)	(28,354)	(806,057)
Assets written-off	-	-	(15,127)	(15,127)
Other changes in net exposure**	(141,508)	(49,405)	(154,570)	(345,483)
Gross carrying amount at 31 December 2019	5,365,249	614,747	207,801	6,187,797

	Stage 1	Stage 2	Stage 3	Total
	£'000	£'000	£'000	£'000
Gross carrying amount at 1 January 2018	4,712,770	440,338	359,482	5,512,590
Transferred from Stage 1 to Stage 2	(256,058)	256,058	-	-
Transferred from Stage 2 to Stage 1	126,668	(126,668)	-	-
Transferred from Stage 3 to other stages	3,643	46,557	(50,200)	-
Transferred to Stage 3 from other stages	(58,949)	(18,331)	77,280	-
New assets*	1,466,188	93,011	18,964	1,578,163
Assets derecognised*	(688,063)	(69,696)	(42,470)	(800,229)
Assets written-off	(3)	(8)	(17,452)	(17,463)
Other changes in net exposure**	(201,790)	(29,741)	(23,075)	(254,606)
Gross carrying amount at 31 December 2018	5,104,406	591,520	322,529	6,018,455

* Revolving credit facilities on renewal are included as new assets and assets derecognised in the above reconciliation.

** Other changes in net exposure include customer repayments, interest applied to lending and foreign exchange movements.

The transfer of the gross carrying amounts between ECL stages has been disclosed on an annual basis.

Classification and measurement – The SPPI test (solely payment of principal and interest on the principal amount outstanding)
Each loan is assessed to establish if the contractual cash flows are consistent with the SPPI test. The principal amount reflects the fair value at initial recognition less any subsequent changes, e.g. due to repayment. The interest shall represent consideration for the time value of money, credit risk, other basic lending risks and profit margin consistent with basic lending features, only. If the cash flows introduce more than de minimis exposure to risk or volatility that is not consistent with basic lending features, the loan is mandatorily recognised at fair value through profit or loss. Features that are not genuine do not affect the classification. A feature is not genuine if it affects the contractual cash flows only on the occurrence of an event that is extremely rare, highly abnormal and very unlikely to occur.

Classification and measurement – The SPPI test (solely payment of principal and interest on the principal amount outstanding) (continued)

In general, the SPPI test of the Bank's portfolios of loans covers, for instance, the following elements:
- Compensation for the time value of money. For some of the Bank's variable rate loans, the market standard for these loans is that the reset frequency and the tenor of the reference rate do 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, for instance, the development in share prices;
- Prepayment options are consistent with the SPPI test, if the prepayment amount represents the 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 represent cash flows that are solely payments of principal and interest on the principal amount outstanding.
- Compensation for credit risk and other basic lending risks. 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 agreements, for example by contractual terms that increase the credit margin if the customer's earnings increases;
- Non-recourse features. In general, the Bank does not grant loans that legally are non-recourse; and
- Non-payment is not a breach of contract. The Bank does not grant loans where non-payment would not constitute a breach of contract.

13. Loans and advances to customers (continued)

Financial instruments in scope of the expected credit loss impairment model in IFRS 9
Impairments for expected credit losses apply to all financial assets recognised at amortised cost or at fair value through Other comprehensive income, lease receivables and certain loan commitments and financial guarantee contracts. As a result, the Bank's expected credit loss model also applies to bond portfolios included in the line item Investment securities.

Significant increase in credit risk (transfer from stage 1 to stage 2)
The classification of facilities between stage 1 and 2 for the purpose of calculating expected credit losses depends on whether the credit risk has increased significantly since initial recognition. 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 facility and incorporates forward-looking information. A facility is transferred from stage 1 to stage 2 based on observed increases in the probability of default:
- For facilities originated below 1% in PD: An increase in the facility's 12-month PD of at least 0.5 percentage points and doubling up 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 or doubling up of the facility's lifetime PD since origination.

In addition, facilities that are more than 30 days past due are moved to 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 two-year probation period for performing forborne exposures.

Stage 3 (credit-impaired facilities)
A facility is transferred from stage 2 to stage 3 when it becomes credit-impaired. A facility becomes credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows have occurred. This includes observable data about (a) significant financial difficulty of the issuer or the borrower; (b) a breach of contract, such as a default or past due event; (c) the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, been granted a concession that would not otherwise have been considered; (d) it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; and (e) the purchase or origination of a financial asset at a high rate of discount that reflects the incurred credit loss. It may not be possible to identify a single individual event – instead, the combined effect of several events may cause the financial asset to become credit-impaired. Credit-impaired facilities are placed in rating category 10 or 11. For rating category 11 (default), all exposures are classified as stage 3.

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

Calculation of expected credit losses
The expected credit loss is calculated for all individual facilities 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 internal models in order to ensure alignment of models across the Bank. New models and calculations have been developed specifically for IFRS 9 purposes, including models for lifetime PD, prepayment and forward-looking LGD. All expected credit loss impairments are allocated to individual exposures. For significant loans in stage 3, the Bank determines the expected credit losses individually.

Expected remaining lifetime
For most facilities, the expected lifetime is limited to the remaining contractual maturity and is adjusted for expected prepayment. For exposures with weak credit quality, the likelihood of prepayment is not included. For exposures 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.

13. Loans and advances to customers (continued)

Incorporation of forward-looking information

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 of each scenario by the Bank's Chief Economist, the review and sign-off of the scenarios (through the Bank) and a process for adjusting scenarios given new information during the quarter. The purpose of using multiple scenarios is to model the non-linear impact of the assumptions about macroeconomic factors on the expected credit losses. 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 macroeconomists. The approved scenarios are used to calculate the impairment levels. Technically, the forward-looking information is used directly in the PDs through an estimate of general changes to the PDs and the LGDs in the expected credit loss calculation. However, for significant exposures in stage 3, an individual assessment of the scenarios, changes to expected credit losses and the related probabilities are performed by senior credit officers.

The forward-looking information is based on a three year forecast period converging to steady state in year seven.

Write-off policy

Loans that are considered uncollectible are written off. Write-offs are debited to the allowance account. Loans are written off once the usual collection procedure has been completed and the loss on the individual loan can be calculated. Full write-off of a loss is only recognised when the customer is formally notified that they no longer have a contractual obligation.

Modification

When a loan is modified the Bank assesses whether the modification results in derecognition. This depends on whether the changes to the contractual cash flows or other contractual terms are significant or not. If the changes are significant, the modification is accounted for as derecognition of the original loan and recognition of a new loan. If the changes are not significant, the modification is accounted for as a modification of the original loan. The assessment is based on the following considerations:

- The Bank differentiates between changes in the cash flows or other terms within the original contract and modifications of the contract, i.e. a new contract;
- In general, a significant modification is defined as a full credit process, a pricing decision and the signing of a new contract; and
- An assessment of whether the modification is caused as a forbearance measure or made on commercial terms.

If the financial asset is not derecognised, the original effective interest rate remains unchanged, and the net present value of the changed contractual cash flows represents the gross carrying amount of the financial asset after the modification. The difference between the net present value of the original contractual cash flows and the modified contractual cash flows is recognised in the Income statement as a modification gain or loss.

If the original financial asset is derecognised, a derecognition gain or loss is recognised in the Income statement. The derecognition gain or loss represents the difference between the carrying amount of the original financial asset and the initial carrying amount of the new financial asset plus/minus any cash payments between the parties in relation to the modification.

In terms of stage allocation, a modification that leads to derecognition of the initial loan and recognition of a new loan, the loan will (unless the new loan is credit-impaired at initial recognition) be recognised in stage 1 at initial recognition, i.e. the initial credit risk is reset. If the replacing loan is considered an amendment to the original loan, the initial credit risk is not reset. Loans modified as part of the Bank's forbearance policy, where the modification does not result in derecognition, the loss allowance on the forborne loans will generally only be measured based on 12-months expected credit losses when there is evidence of the borrower's improved repayment behaviour. When a loan in stage 3 is modified, and the modification results in derecognition, the Bank assesses if the new loan is originated credit impaired. The assessment includes factors such as whether the customer's repayment behaviour has improved significantly prior to the modification or not and whether the pricing on the new loan reflects the actual credit risk. New loans that are originated credit impaired remain under a lifetime ECL calculation for the remaining term of the exposure.

13. Loans and advances to customers (continued)

Reconciliation of total allowance account

The allowance account below is reconciled by measurement category. The allowance account for loans at amortised cost is credited against the related loans, whereas the allowance account related to loan commitments and guarantees is recognised as a liability and presented under Other liabilities. The transfer between ECL stages has been disclosed on a monthly basis.

Reconciliation of total allowance account

	Stage 1	**Stage 2**	**Stage 3**	**Total**
	£'000	**£'000**	**£'000**	**£'000**
ECL allowance account at 1 January 2019	**5,941**	**14,844**	**75,029**	**95,813**
				-
Charge for the year				
- transferred from Stage 1 during the year	**-**	**1,917**	**134**	**2,051**
- transferred from Stage 2 during the year	**1,693**	**-**	**2,705**	**4,398**
- transferred from Stage 3 during the year	**12**	**1,911**	**-**	**1,923**
- transferred to Stage 1 during the year	**-**	**(1,693)**	**(12)**	**(1,705)**
- transferred to Stage 2 during the year	**(1,917)**	**-**	**(1,911)**	**(3,828)**
- transferred to Stage 3 during the year	**(134)**	**(2,705)**	**-**	**(2,839)**
- ECL on new assets	**3,390**	**-**	**-**	**3,390**
- ECL on assets derecognised	**(3,309)**	**(6,003)**	**(14,266)**	**(23,578)**
Impact of net remeasurement of ECL (incl. changes in models)	**1,764**	**(243)**	**2,704**	**4,225**
Impact of net remeasurement of ECL (Stage Change)	**-**	**8,271**	**9,803**	**18,074**
Recovery of amounts written off in previous years	**-**	**-**	**(1,314)**	**(1,314)**
	1,499	**1,455**	**(2,157)**	**797**
Write-offs/recoveries applied to the allowance account				
- Write-offs debited to the allowance account	**-**	**-**	**(15,127)**	**(15,127)**
- Recoveries of amounts written off in previous years	**-**	**-**	**1,315**	**1,315**
Foreign exchange and other adjustments	**(4)**	**(8)**	**495**	**483**
As at 31 December 2019	**7,436**	**16,290**	**59,555**	**83,281**

	Stage 1	Stage 2	Stage 3	Total
	£'000	£'000	£'000	£'000
Collective and individual impairment charges under IAS 39 as at 31 December 2017	596	109	90,411	91,116
Transition effect (ECL at 1 January 2018)	4,606	11,908	(126)	16,388
Charge for the year				
- transferred from Stage 1 during the year	-	1,693	3,001	4,694
- transferred from Stage 2 during the year	7,723	-	4,437	12,160
- transferred from Stage 3 during the year	1,322	5,546	-	6,868
- transferred to Stage 1 during the year	-	(7,723)	(1,322)	(9,044)
- transferred to Stage 2 during the year	(1,693)	-	(5,546)	(7,239)
- transferred to Stage 3 during the year	(3,001)	(4,437)	-	(7,438)
- ECL on new assets	6,282	894	-	7,176
- ECL on assets derecognised	(3,273)	(5,891)	(20,481)	(29,644)
Impact of net remeasurement of ECL (incl. changes in models)	964	1,303	5,501	7,768
Impact of net remeasurement of ECL (Stage Change)	(7,583)	11,437	15,815	19,669
Recovery of amounts written off in previous years	-	-	(2,072)	(2,072)
	741	2,822	(667)	2,896
Write-offs/recoveries applied to the allowance account				
- Write-offs debited to the allowance account	(3)	(8)	(17,452)	(17,463)
- Recoveries of amounts written off in previous years	-	-	2,072	2,072
Foreign exchange and other adjustments	1	13	790	804
As at 31 December 2018	5,941	14,844	75,028	95,813

13. Loans and advances to customers (continued)

Allowance account broken down by balance sheet items

	2019 £'000	2018 £'000
Due from credit institutions and central banks	54	65
Loans at amortised cost	79,385	92,095
Loan commitments and guarantees	3,842	3,653
Total	83,281	95,813

Loan impairment charges include impairment charges for expected credit losses against loans, lease receivables, investment securities, certain loan commitments and financial guarantee contracts.

Significant accounting estimates related to expected credit losses

For information on significant accounting estimates related to expected credit losses, see note 1(b).

14. Investment in subsidiaries

	2019 £'000	2018 £'000
Ordinary shares in subsidiaries	250	250

There was no movement on shares and investments in subsidiary undertakings this year or in the previous year.

Investments in subsidiary undertakings are included at historical cost.

	2019 £'000	2018 £'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.

15. Intangible assets

	2019 £'000	2018 £'000
Cost at beginning of year	608	359
Additions	-	249
Cost at end of year	608	608
Accumulated amortisation at beginning of year	193	85
Amortisation charge for the year	203	108
Accumulated amortisation at end of year	396	193
Net book value at end of year	212	415

Intangible assets consist of acquired software.

16. Property, plant and equipment

	Freehold land and buildings £'000	Leases of 50 years and over unexpired £'000	Leases of under 50 years unexpired £'000	Motor vehicles, fixtures and equipment £'000	Total 2019 £'000
Cost at 1 January 2019	10,645	25,443	3,454	28,593	68,135
Additions	-	-	565	1,528	2,093
Transferred to assets held for sale	(360)	-	-	(124)	(484)
Revaluation	(434)	485	(2)	-	49
Cost at 31 December 2019	9,851	25,928	4,017	29,997	69,793
Accumulated depreciation at 1 January 2019	103	308	1,260	21,509	23,180
Depreciation charge for the year	206	610	408	2,097	3,321
Transferred to assets held for sale	-	-	-	(124)	(124)
Revaluation	(206)	(614)	(6)	-	(826)
Accumulated depreciation at 31 December 2019	103	304	1,662	23,482	25,551
Net book value at 31 December 2019	9,748	25,624	2,355	6,515	44,242

	Freehold land and buildings £'000	Leases of 50 years and over unexpired £'000	Leases of under 50 years unexpired £'000	Motor vehicles, fixtures and equipment £'000	Total 2018 £'000
Cost at 1 January 2018	11,349	25,873	3,378	26,297	66,897
Additions	-	-	76	2,552	2,628
Disposals	-	-	-	(135)	(135)
Transferred to assets held for sale	(530)	-	-	(121)	(651)
Revaluation	(174)	(430)	-	-	(604)
Cost at 31 December 2018	10,645	25,443	3,454	28,593	68,135
Accumulated depreciation at 1 January 2018	112	312	881	19,609	20,914
Depreciation charge for the year	219	618	385	2,156	3,378
Accumulated depreciation on disposals	-	-	-	(135)	(135)
Transferred to assets held for sale	(4)	-	-	(121)	(125)
Revaluation	(224)	(622)	(6)	-	(852)
Accumulated depreciation at 31 December 2018	103	308	1,260	21,509	23,180
Net book value at 31 December 2018	10,542	25,135	2,194	7,084	44,955

16. Property, plant and equipment (continued)

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 2019. 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

	2019 £'000	2018 £'000
Net book value	37,727	37,871

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

	2019 £'000	2018 £'000
Cost	20,449	20,054
Accumulated depreciation	(18,279)	(19,732)
Net book value	2,170	322

17. Right-of-use assets

	2019 £'000	2018 £'000
Net carrying amount	6,899	-

Right-of-use lease assets are in respect of buildings. The depreciation charge is £1,355,000. The interest expense on the corresponding lease liability is £158,000. There are no comparatives as the accounting standard IFRS 16 was implemented on 1 January 2019 and an asset of £8,256,000 was recognised. A description of the implementation of IFRS 16 is set out in Note 1. There were no additions and no significant impairment losses of the right-of-use lease assets . Expenses relating to leases of low value assets are set out in note 37.

18. Assets held for sale

	2019 £'000	2018 £'000
Assets held for sale	485	526

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 £18,000 (2018: £nil).

Properties held for sale consists of properties which have been closed as part of a review of the business. One property was sold during the year (2018: one.)

19. Deferred tax

Movement in net deferred tax (liability)/asset

	2019 £'000	2018 £'000
At 1 January	3,232	4,678
Recognised in the income statement (Note 8)	(12,432)	(3,717)
Recognised directly in equity:		
- Actuarial (gain)/loss	(8,633)	1,609
- Investment securities hold to collect and sell	(1,523)	619
- Cash flow hedge reserve	(662)	(48)
- Transfer to revaluation reserve	(88)	91
At 31 December	(20,106)	3,232

The Bank recognises deferred tax attributable to the following items:

	31 December 2019 £'000	31 December 2018 £'000
Deferred tax assets		
Tax losses carried forward	18,060	23,830
Investment securities - hold to collect and sell	-	992
Accelerated capital allowances	4,823	5,382
Other timing differences	8,438	10,344
	31,321	40,548
Deferred tax liabilities		
Defined benefit pension asset	47,625	34,795
Net gain on revaluation of properties	2,560	2,472
Investment securities - hold to collect and sell	531	-
Cash flow hedge reserve	711	49
	51,427	37,316
Net deferred tax (liability)/asset	(20,106)	3,232

At 31 December 2019 the Bank had an unrecognised deferred tax asset of £22,990,000 (2018: £20,510,000) representing trading losses with a gross value of £135,237,000 (2018: £120,650,000). 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. During the 2019 General Election campaign, the Conservative Party announced their intention to reverse the rate reduction from 1 April 2020, such that temporary differences unwinding after 1 April 2020 will do so at a rate of 19% instead of 17%. This has not been reflected in the disclosures as the change to 19% has not yet been substantively enacted.

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 deferred tax charge of £2,480,000, within a total deferred tax charge of £12,432,000.

20. Other assets

	2019 £'000	2018 £'000
Accrued interest	23,187	21,813
Prepayments and other amounts due	8,602	9,678
	31,789	31,491

21. Due to other banks

	2019 £'000	2018 £'000
Transaction balances with other banks	23,024	22,624
Term Funding Scheme (Bank of England)	350,000	350,000
	373,024	372,624

	2019 £'000	2018 £'000
Analysed by remaining maturity		
Repayable on demand	23,024	22,624
5 years or less but over 1 year	350,000	350,000
	373,024	372,624
Amounts include:		
Due to parent and fellow subsidiary undertakings	19,873	17,605

22. Deposits from customers

	2019 £'000	2018 £'000
Current accounts	4,694,545	4,395,663
Demand deposits	2,679,921	2,379,038
Time deposits	717,074	790,438
	8,091,540	7,565,139

	2019 £'000	2018 £'000
Analysed by remaining maturity		
Repayable on demand	7,374,466	6,774,701
- 3 months or less but not repayable on demand	502,843	501,355
- 1 year or less but over 3 months	201,704	268,541
- 5 years or less but over 1 year	12,527	20,542
	8,091,540	7,565,139

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 did not affect the pension arrangements of existing employees. The Scheme closed to future accrual on 30 September 2018. 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 2019 was £7,139,000 (2018: £2,956,000). 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.

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:

	2019	2018
	% p.a.	% p.a.
Inflation (RPI)	**2.95**	3.15
Inflation (CPI)	**2.05**	2.15
Rate of future increase in salaries	**N/A**	N/A
Rate of increase for pre-1997 pensions in payment	**1.60**	2.15
Rate of increase for 1997-2008 pensions in payment	**2.80**	2.95
Rate of increase for post-2008 pensions in payment	**1.90**	2.30
Discount rate	**2.05**	2.70
Post retirement mortality		
Current pensioners at 60 - males (years)	**28.70**	28.20
Current pensioners at 60 - females (years)	**30.40**	29.70
Future pensioners at 60 - males (years)	**30.20**	29.70
Future pensioners at 60 - females (years)	**31.80**	31.30

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 within the Danske Bank Group in the year ending 31 December 2020 is £1,000,000. Members no longer make contributions to the defined benefit scheme following Scheme closure on 30 September 2018.

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.

In previous years, the pension increase assumptions have been set in line with the relevant inflation measure with an approximate adjustment for the relevant caps and floors. At the 2019 year-end, the impact of the caps and floors were incorporated through the application of the Black Scholes model. The impact of using this approach was to decrease the value placed on the Scheme’s IAS19 liabilities as at 31 December 2019 by around £35m.

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.

	Market value 31 December 2019 £'000	Market value 31 December 2018 £'000
Equity securities	**83,578**	102,042
Debt securities	**541,494**	474,245
Real estate/property	**40,540**	61,810
Derivatives	**80,376**	60,220
Other	**1,322**	4,917
Buy-in annuity	**619,973**	577,326
Fair value of Scheme assets	**1,367,283**	1,280,560

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

23. Pension asset (continued)

Reconciliation to the Balance Sheet

	2019 £'000	2018 £'000
Analysis of defined benefit obligation by status		
- Active members	-	-
- Deferred pensioner members	476,000	542,300
- Pensioners	695,400	588,000
Present value of defined benefit obligation	1,171,400	1,130,300
Fair value of plan assets	1,367,283	1,280,560
Net defined benefit asset	195,883	150,260

	2019 £'000	2018 £'000
Net defined benefit asset at beginning of year	150,260	154,261
Service cost (including past service costs)		
- the Bank	(147)	(11,695)
- other participating employers	-	(32)
Administration costs incurred over the year	(987)	(816)
Net interest on net defined benefit asset	4,200	4,100
Employers' contributions		
- the Bank	8,026	10,845
- other participating employers	-	32
Remeasurement effects recognised in Other Comprehensive Income (OCI)	34,531	(6,435)
Net defined benefit asset at end of year	195,883	150,260

Movement in present value of defined benefit obligation

	2019 £'000	2018 £'000
Defined benefit obligation at beginning of year	1,130,300	1,194,100
Gross current service cost		
- the Bank	-	9,168
- other participating employers	-	32
- contributions paid by members	-	10
Past service costs		
- the Bank	147	2,527
Interest cost on the defined benefit obligation	29,800	27,800
Actuarial gain - experience	286	4,856
Actuarial gain - demographic assumptions	19,000	10,052
Actuarial gain/(loss) - financial assumptions	75,000	(67,860)
Benefits paid by the Scheme	(83,133)	(50,385)
Defined benefit pension obligation at end of year	1,171,400	1,130,300

Movement in fair value of Scheme assets

	2019 £'000	2018 £'000
Fair value of Scheme assets at beginning of year	1,280,560	1,348,361
Interest income on Scheme assets	34,000	31,900
Return on Scheme assets greater/(less) than discount rate	128,817	(59,387)
Employers' and employees' contributions paid into the Scheme		
- participating employers	8,026	10,845
- other participating employers	-	32
- member contributions	-	10
Benefits paid by the Scheme	(83,133)	(50,385)
Administration costs paid	(987)	(816)
Fair value of Scheme assets at end of year	1,367,283	1,280,560

23. Pension asset (continued)

Scheme expense recognised in the Income Statement

	2019 £'000	2018 £'000
Current service cost		
- the Bank included within operating expenses	-	9,168
- other participating employers	-	32
Past service cost and curtailments (including Guaranteed Minimum Pension)	147	2,527
	147	11,727
Net interest on net defined benefit asset	(4,200)	(4,100)
Administration costs incurred during the year	987	816
Scheme expense	(3,066)	8,443

Amount recognised in Other Comprehensive Income (OCI)

	2019 £'000	2018 £'000
Return on Scheme assets (greater)/less than discount rate	(128,817)	59,387
Actuarial loss due to liability experience	286	4,856
Actuarial loss/(gain) due to assumption changes	94,000	(57,808)
Remeasurement effects recognised in OCI - (gain)/loss	(34,531)	6,435

Actual return on Scheme assets

	2019 £'000	2018 £'000
Interest income on Scheme assets	34,000	31,900
Return on Scheme assets greater/(less) than discount rate	128,817	(59,387)
Actual return on Scheme assets	162,817	(27,487)

Plan characteristics and associated risks

	2019 £'000	2018 £'000
Maturity profile of Defined Benefit Obligation		
- Expected benefit payments during fiscal year ending 31 December 2020	53,100	51,500
- Expected benefit payments during fiscal year ending 31 December 2021	54,200	52,600
- Expected benefit payments during fiscal year ending 31 December 2022	55,300	53,700
- Expected benefit payments during fiscal year ending 31 December 2023	56,400	54,900
- Expected benefit payments during fiscal year ending 31 December 2024	57,500	56,100
- Expected benefit payments during fiscal year ending 31 December 2025 through 31 December 2029	305,000	299,100

	2019 Years	2018 Years
Weighted average duration of Defined Benefit Obligation (years)	18	20

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.

23. Pension asset (continued)

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

	2019 £'000
Discount rate	
Change in DBO at year end from a 50 basis points increase	(99,000)
Change in DBO at year end from a 50 basis points decrease	113,000
Price inflation (RPI measure)*	
Change in DBO at year end from a 50 basis points increase	60,000
Change in DBO at year end from a 50 basis points decrease	(55,000)
Pension increases**	
Change in DBO at year end from a 50 basis points increase	41,000
Change in DBO at year end from a 50 basis points decrease	(38,000)
Post retirement longevity	
Change in DBO at year end from a one year increase in longevity	41,000
Change in DBO at year end from a one year decrease in longevity	(41,000)

*Including consistent change to the pension increases, CPI related increases in deferment.
**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.

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 sufficient capital specifically in respect of pension risk.

24. Other liabilities

	2019	2018
	£'000	£'000
Accrued interest	3,341	3,457
Provision for off balance sheet financial guarantees and loan commitments	3,842	3,653
Accruals and sundry creditors	18,695	21,794
Lease liabilities	6,206	-
Corporation tax	7,185	5,955
	39,269	34,859

The Bank has issued a number of loan commitments and guarantee instruments. If an instrument is likely to result in a payment obligation, a liability is recognised corresponding to the present value of expected payments.

Lease liabilities broken down by expected due date:

	2019
	£'000
Lease liabilities due:	
- 1 year or less	1,248
- over 1 year	4,958
Total	6,206

There are no comparatives as the accounting standard IFRS 16 was implemented on 1 January 2019.

25. Provisions

	PPI	Other	Total
	£'000	£'000	£'000
At 1 January 2019	3,154	968	4,122
Charge to income statement	771	2,155	2,926
Provisions utilised	(1,196)	(814)	(2,010)
At 31 December 2019	2,729	2,309	5,038

Provisions broken down by expected due date:

	2019	2018
	£'000	£'000
Provisions due:		
- 1 year or less	4,153	4,122
- over 1 year	885	-
Total	5,038	4,122

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. With the FCA's deadline on PPI complaints having now passed, the level of uncertainty in determining the volume of complaints has reduced. However, due to the significant volumes received prior to the deadline, there continues to be uncertainties in relation to the assumptions and consequently the ultimate cost of redress. The assumptions underlying the provision calculation based upon experience and other relevant factors as matters develop include: (i) the number of those claims that ultimately will be upheld; (ii) the amount that will be paid in respect of those claims; and (iii) any additional amounts that may need to be paid in respect to previously handled claims.

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.

Other

This represents provisions 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 exit costs from property leases following the application of IFRS 16.

26. Subordinated debt

	2019 £'000	2018 £'000
Balance at 31 December	126,000	126,000

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 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).

	2019 < 1 year £'000	2019 > 1 year £'000	2018 < 1 year £'000	2018 > 1 year £'000
Assets				
Cash and balances at central bank	963,156	1,216,004	1,072,715	969,208
Items in the course of collection from other banks	30,804	-	40,137	-
Due from other banks	39,053	5,145	37,544	3,999
Derivative financial instruments	6,582	4,891	6,240	3,617
Investment securities - hold to collect	186,798	408,756	99,879	418,203
Investment securities - hold to collect and sell	125,019	605,656	6,004	641,569
Loans and advances to customers	2,546,426	3,561,986	2,440,640	3,485,720
Investment in subsidiaries	-	250	-	250
Intangible assets	-	212	-	415
Property, plant and equipment	-	44,242	-	44,955
Right-of-use asset	1,329	5,570	-	-
Assets held for sale	485	-	526	-
Deferred tax assets	-	-	-	3,232
Defined benefit pension asset	-	195,883	-	150,260
Other assets	29,706	2,083	28,797	2,694
Total assets	3,929,358	6,050,678	3,732,482	5,724,122
Liabilities				
Due to other banks	23,024	350,000	22,624	350,000
Items in course of transmission to other banks	11,731	-	17,854	-
Derivative financial instruments	4,965	9,740	5,487	6,505
Deposits from customers	5,317,989	2,773,551	5,126,446	2,438,693
Notes in circulation	-	471,968	-	489,091
Deferred tax liabilities	-	20,106	-	-
Provisions	4,153	885	4,122	-
Other liabilities	11,775	27,494	9,412	25,447
Subordinated debt	-	126,000	-	126,000
Total liabilities	5,373,637	3,779,744	5,185,945	3,435,736

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 (see note 39) 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 2019					
Liabilities					
Due to other banks	23,024	-	-	350,000	-
Deposits from customers	7,374,466	502,843	201,704	12,527	-
Derivative financial instruments	-	2,628	3,933	6,252	2,105
Subordinated debt	-	-	-	100,000	26,000
	7,397,490	505,471	205,637	468,779	28,105
Off balance sheet items					
Contingent liabilities	104,748	-	-	-	-
Commitments	932,172	-	-	-	-
	1,036,920	-	-	-	-
At 31 December 2018					
Liabilities					
Due to other banks	22,624	-	-	350,000	-
Deposits from customers	6,774,701	501,355	268,541	20,542	-
Derivative financial instruments	-	2,167	4,199	4,421	1,362
Subordinated debt	-	-	-	-	126,000
	6,797,325	503,522	272,740	374,963	127,362
Off balance sheet items					
Contingent liabilities	92,056	-	-	-	-
Commitments	926,244	-	-	-	-
	1,018,300	-	-	-	-

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, included within contingent liabilities, 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 2019					
Financial assets					
Cash and balances at central bank	**2,179,160**	**-**	**-**	**(471,968)**	**1,707,192**
Due from other banks	**44,198**	**-**	**(19,873)**	**(754)**	**23,571**
Derivatives with positive fair value	**11,473**	**-**	**(8,756)**	**-**	**2,717**
Loans and advances to customers	**6,108,412**	**(539,231)**	**-**	**-**	**5,569,181**
Financial liabilities					
Due to other banks	**373,024**	**-**	**(19,873)**	**-**	**353,151**
Derivatives with negative fair value	**14,705**	**-**	**(8,756)**	**(754)**	**5,195**
Deposits from customers	**8,091,540**	**(539,231)**	**-**		**7,552,309**
Notes in circulation	**471,968**	**-**	**-**	**(471,968)**	**-**
At 31 December 2018					
Financial assets					
Cash and balances at central bank	2,041,923	-	-	(489,091)	1,552,832
Due from other banks	41,543	-	(17,605)	-	23,938
Derivatives with positive fair value	9,857	-	(4,597)	(897)	4,363
Loans and advances to customers	5,926,360	(482,426)	-	-	5,443,934
Financial liabilities					
Due to other banks	372,624	-	(17,605)	-	355,019
Derivatives with negative fair value	11,992	-	(4,597)	(897)	6,498
Deposits from customers	7,565,139	(482,426)	-	-	7,082,713
Notes in circulation	489,091	-	-	(489,091)	-

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 investment securities - hold to collect and sell.

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 investment securities - hold to collect and sell 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 the initial margin into account. The valuation of derivatives thus includes amortisation of the value of initial margins over the remaining term to maturity. The initial margins cover such elements as future administrative expenses, capital consumption, funding costs and initial credit risk.

	2019 £'000	2018 £'000
Unamortised initial margins at 1 January	**363**	399
Amortised to the income statement during the year	**(1,029)**	(928)
Initial margins on new derivatives contracts	**971**	892
Terminated derivatives contracts	**(4)**	-
Unamortised initial margins at 31 December	**301**	363

30. Fair value information for financial instruments (continued)

	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
At 31 December 2019				
Financial assets				
Investment securities - hold to collect and sell	730,675	-	-	730,675
Interest rate and equity contracts	-	3,787	2	3,789
Currency contracts	-	7,684	-	7,684
Total	730,675	11,471	2	742,148
Financial liabilities				
Interest rate and equity contracts	-	5,511	-	5,511
Currency contracts	-	9,192	2	9,194
Total	-	14,703	2	14,705
At 31 December 2018				
Financial assets				
Investment securities - hold to collect and sell	647,572	-	-	647,572
Interest rate contracts	-	1,869	5	1,874
Currency contract	-	7,900	83	7,983
Total	647,572	9,769	88	657,429
Financial liabilities				
Interest rate contracts	-	5,376	5	5,381
Currency contracts	-	6,527	84	6,611
Total	-	11,903	89	11,992

Derivatives valued on the basis of non-observable input

	2019 £'000	2018 £'000
Fair value at 1 January	1	1
Acquisitions	-	2
Sale and redemption	(1)	(2)
Fair value at 31 December	-	1

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 - hold to collect and sell

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 set 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 investment securities to manage the remaining interest rate risk. Consequently, only 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.

It is assessed that the expected credit loss impairment model used for loans measured at amortised cost is a reasonable proxy for the fair value of the credit risk.

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					
Investment securities (Note 12)	**595,554**	**597,558**	**597,558**	**-**	**-**
Loans at amortised cost	**6,108,412**	**6,108,412**	**-**	**-**	**6,108,412**
At 31 December 2019	**6,703,966**	**6,705,970**	**597,558**	**-**	**6,108,412**
Financial assets					
Investment securities (Note 12)	518,082	520,950	520,950	-	-
Loans at amortised cost	5,926,360	5,926,360	-	-	5,926,360
At 31 December 2018	6,444,442	6,447,310	520,950	-	5,926,360

31. Share capital

	2019 £'000	2018 £'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. Reserve for investment securities at fair value

The reserve covers unrealised fair value adjustment, other than expected credit losses and foreign exchange gains and losses, of bonds measured at fair value through Other comprehensive income. Unrealised fair value adjustments of hedged interest rate risks that qualify for fair value hedge accounting are recognised in the Income statement and are not included in the reserve. When bonds are sold, the Bank reclassifies unreduced value adjustments from the reserve to the Income statement.

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 2019, the cash flow hedge reserve reflected a cumulative gain of £2,843,000 (2018: £197,000). This was offset by a deferred tax liability of £711,000 (2018: £49,000).

34. Additional Tier 1 capital

At the end of 2019, the total nominal value of issued Additional Tier 1 capital amounted to £96,000,000 (2018: £96,000,000). Capital notes of £16,000,000 were issued on 19 December 2017 and £80,000,000 issued on 12 January 2015.

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 2019 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.

35. 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.

	2019 £'000	2018 £'000
Contingent liabilities		
Guarantees and irrevocable letters of credit	**104,748**	92,056
Commitments		
Irrevocable loan commitments shorter than 1 year	**590,025**	608,604
Irrevocable loan commitments longer than 1 year	**342,147**	317,639
	932,172	926,243

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.

36. Capital commitments

The Bank had future capital expenditure which had been contracted but not provided for in the Financial Statements at 31 December 2019 of £560,000 (2018: £747,000).

37. 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 £8,240,000 (2018: £8,939,000) and £120,675,000 (2018: £116,167,000) respectively.

The total closing balances of finance leases and hire purchase contracts were £18,890,000 (2018: £19,580,000) and £206,006,000 (2018: £202,565,000) respectively.

Finance lease and hire purchase receivables

	2019	2018
	£'000	£'000
Gross investment in finance lease and hire purchase receivables		
Due within one year	**15,329**	16,642
Due within one to five years	**195,745**	191,225
Due after five years	**26,563**	26,284
Total gross investment in finance lease receivables	**237,637**	234,151
Unearned income	**(12,741)**	(12,006)
Net investment in finance lease and hire purchase receivables	**224,896**	222,145

Within the Bank, at 31 December 2019, there are impairment provisions of £Nil (2018: £694,000) in relation to finance lease receivables.

Operating leases

Operating leases consist of lease commitments with a term of less than twelve months together with lease commitments for low value assets.

	2019	2018
	£'000	£'000
Operating lease expiring		
- within 1 year	**243**	225
- in 1 - 5 years	**149**	976
- after 5 years	**-**	969
	392	2,169
Where the Bank is the lessee the future minimum lease payments under non-cancellable operating leases are:		
- within 1 year	**392**	2,169
- between 1 and 5 years	**247**	6,186
- over 5 years	**-**	2,678
	639	11,033

On 1 January 2019 the Bank implemented IFRS 16, Leases, as set out in Note 1(c). Consequently, property leases over twelve months that were previously disclosed as operating leases are now recognised as right-of-use assets. Comparatives have not been restated.

38. 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 2019	**97,101**	**126,000**
Movement in accrued interest	**(32)**	**-**
At 31 December 2019	**97,069**	**126,000**

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.

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".

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).

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 Risk Committee (BRC) 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 employs for the day to day running of the business.

The BRC 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 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 has 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.

Board Audit Committee (BAC)

The 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;
- 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.

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 and fair customer outcomes;
- 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.

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

a) Management of risk (continued)

Board Remuneration Committee (RemCo)

The Remuneration Committee of the Board of Directors is responsible for reviewing and recommending for the approval of the Board the overarching principles and governance framework of the Bank's remuneration policy, and for approving the remuneration outcomes for senior staff.

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.

Subsidiary 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. Layering on top of the activities of 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.

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, cyber-crime 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
Conduct Risk Committee	Conduct Risk
Pension Risk Committee	Pension obligation risk

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

a) Management of risk (continued)

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 it. The business should have sufficient controls in place to demonstrate a strong risk management framework in its own right;

- the Risk Management department is the second line of defence and is responsible for the independent oversight of risk, the provision of a suitable Bank-wide risk management framework (subject to the exclusions noted for specialist business units) and Senior Management Function responsibilities (SMF) 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 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 across all risk types 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 risk across all risk types;
- controlling risks within tolerances set to ensure that financial or non-financial exposures do not cause material damage to the Bank and manage risk based on realistic trade off decisions between the cost of mitigating a risk and the potential loss of accepting risk without mitigation ;
- 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.

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 strong control over discretionary costs and the delivery of lower cost to serve distribution channels and;
- Capital and liquidity management: maintaining strong capital and liquidity positions that are 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.

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

a) Management of risk (continued)

Risk Appetite Framework (RAF) (continued)

- *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, mortgages (with an ongoing focus on increasing mortgage growth through the switcher market and private banking). Any growth in the Bank's credit card portfolio, in addition to the planned growth in personal loan portfolio will continue to be on the basis of acceptable credit quality;
- Business customers: aiming to be the first choice for top business customers. The Bank will operate in Northern Ireland, supplemented by targeted lending activities in the rest of the UK. Lending acquisition will focus on small and medium sized entities and corporate acquisition, in addition to the provision of syndicated lending to investment-grade UK corporates with an NI footprint, with no appetite for other 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, ILAAP and Risk Management Framework.

Risk Assessment Methodology

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

The Risk Assessment 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 Risk Assessment is based on the likelihood of four parameters: regulatory, customer, reputational and financial impact.

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 risk

The Bank offers loans, credits, guarantees and other products as part of its business model and thus takes on credit risk.

Credit risk is the risk of losses because counterparties or debtors fail to meet all or part of their payment obligations to the Bank.

The Bank grants credits on the basis of information about customers' individual financial circumstances and monitors their financial situation with the aim of assessing whether the basis for granting credit facilities has changed. Facilities should adhere to the guidelines outlined in the Bank's Credit Policy, including the Principles of Responsible Lending. The Principles of Responsible Lending focus on customers' understanding of the consequences of borrowing, on an assessment of their needs and ability to repay, and on possible conflicts with the Bank's ethical guidelines. Facilities should match customers' financial situation, including their earnings, capital and assets, and business volume with the Bank to a reasonable degree, and customers must be able to substantiate their repayment ability.

In order to mitigate credit risk, the Bank uses collateral, guarantees and covenants.

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 2019	Lending activities	Counterparty risk derivatives	Inter group	Other	Total
	£'000	£'000	£'000	£'000	£'000
Balance sheet items					
Balances at central bank	**1,829,435**	-	-	-	**1,829,435**
Items in the course of collection from other banks	**30,804**	-	-	-	**30,804**
Due from other banks	**3,404**	-	**40,794**	-	**44,198**
Trading portfolio assets	-	**11,473**	-	-	**11,473**
Investment securities- hold to collect	-	-	-	**595,554**	**595,554**
Investment securities - hold to collect and sell	-	-	-	**730,675**	**730,675**
Loans and advances at amortised cost	**6,108,412**	-	-	-	**6,108,412**
Investment in subsidiaries	-	-	**250**	-	**250**
Off-balance sheet items					
Guarantees	**104,748**	-	-	-	**104,748**
Irrevocable loan commitments shorter than 1 year	**590,025**	-	-	-	**590,025**
Irrevocable loan commitments longer than 1 year	**342,147**	-	-	-	**342,147**
Total	9,008,975	11,473	41,044	1,326,229	10,387,721

At 31 December 2018	Lending activities	Counterparty risk derivatives	Inter group	Other	Total
	£'000	£'000	£'000	£'000	£'000
Balance sheet items					
Balances at central bank	1,417,159	-	-	-	1,417,159
Items in the course of collection from other banks	40,137	-	-	-	40,137
Due from other banks	7,743	-	33,800	-	41,543
Trading portfolio assets	-	9,857	-	-	9,857
Investment securities- hold to collect	-	-	-	518,082	518,082
Investment securities - hold to collect and sell	-	-	-	647,572	647,572
Loans and advances at amortised cost	5,926,360	-	-	-	5,926,360
Investment in subsidiaries	-	-	250	-	250
Off-balance sheet items					
Guarantees	92,056	-	-	-	92,056
Irrevocable loan commitments shorter than 1 year	608,604	-	-	-	608,604
Irrevocable loan commitments longer than 1 year	317,640	-	-	-	317,640
Total	8,409,699	9,857	34,050	1,165,654	9,619,260

40. Credit risk disclosures (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 expected credit losses and includes repo loans at amortised cost. 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. While rating all large customers, the Bank uses fully automated and statistically based scoring models for small customers such as personal customers and small businesses. Credit scores are updated monthly in a process subject to automated controls.

The Bank has developed a number of classification models to assess customer PD and to classify customers in various segments.

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.

The classification of facilities between stage 1 and 2 for the purpose of calculating expected credit loss impairments under IFRS 9 depends on whether the credit risk has increased significantly since initial recognition. The assessment of whether the 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 facility and incorporate forward-looking information. A facility is transferred from stage 1 to stage 2 based on observed increases in the probability of default:

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

In addition, facilities that are more than 30 days past due are moved to stage 2. 30 days past due is considered a backstop. Finally, customers subject to forbearance measures are placed in stage 2, if the Group, in the most likely outcome, expects no loss or the customers are in the two-year probation period for performing forborne exposures.

A facility is transferred from stage 2 to stage 3 when it becomes credit-impaired. A facility becomes credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows have occurred. This includes observable data about (a) significant financial difficulty of the issuer or the borrower; (b) a breach of contract, such as a default or past due event; (c) the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, been granted a concession that would not otherwise have been considered; and (d) it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation. It may not be possible to identify a single discrete event – instead, the combined effect of several events may have caused financial asset to become credit-impaired. Credit-impaired facilities are placed in rating category 10 or 11. For customers in rating category 10, the stage 3 classification only applies to customers where a loss is expected in the most likely scenario. For rating category 11 (default), all exposures are classified as stage 3.

Exposures which are considered to be in default for regulatory purposes will always be considered stage 3 under IFRS 9. This applies both to 90-days past-due considerations and unlikely-to-pay factors leading to regulatory default.

40. Credit risk disclosures (continued)

Expected credit losses

The expected credit loss is calculated for all individual facilities as a function of the probability of default (PD), the exposure at default (EaD) and the loss given default (LGD). For exposures in stage 1, 12 months expected credit losses are recognised. For exposures in stage 2-3, lifetime expected credit losses are recognised.

Credit portfolio broken down by rating category and stages

In the table below the rating categories 10 and 11 represent credit impaired assets.

	PD level		31 December 2019 Gross exposure				31 December 2018 Gross exposure			
	Upper	Lower	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
			£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Rating Category										
1	-	0.01	303,806	1,087	-	304,893	393,908	1,526	-	395,434
2	0.01	0.03	2,815,740	3,046	-	2,818,786	2,355,751	2,905	1,709	2,360,365
3	0.03	0.06	792,758	4,258	339	797,355	503,907	2,932	12	506,851
4	0.06	0.14	1,101,042	5,691	-	1,106,733	1,043,638	5,267	3	1,048,908
5	0.14	0.31	1,328,848	24,873	62	1,353,783	1,289,488	38,971	95	1,328,554
6	0.31	0.63	846,233	67,661	62	913,956	854,450	30,612	108	885,170
7	0.63	1.90	873,892	220,690	143	1,094,725	943,173	317,471	317	1,260,961
8	1.90	7.98	114,785	282,616	11,292	408,693	126,250	205,994	294	332,538
9	7.98	25.70	4,505	42,198	3,861	50,564	4,272	37,144	195	41,611
10	25.70	99.99	-	35,842	107,778	143,620	292	16,212	139,239	155,743
11	100.00	100.00	-	1,522	97,626	99,148	8	1,446	187,923	189,377
Total			8,181,609	689,484	221,163	9,092,256	7,515,137	660,480	329,895	8,505,512

	PD level		31 December 2019 Expected Credit Loss				31 December 2018 Expected Credit Loss			
	Upper	Lower	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
			£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Rating Category										
1	-	0.01	1	-	-	1	2	-	-	2
2	0.01	0.03	74	2	-	76	89	45	11	145
3	0.03	0.06	64	101	-	165	46	12	1	59
4	0.06	0.14	208	20	-	228	239	43	1	283
5	0.14	0.31	661	155	14	830	629	349	6	984
6	0.31	0.63	956	439	8	1,403	924	305	17	1,246
7	0.63	1.90	3,949	2,639	89	6,677	3,238	4,096	31	7,365
8	1.90	7.98	926	7,207	590	8,723	737	6,667	25	7,429
9	7.98	25.70	596	4,259	316	5,171	38	2,437	23	2,498
10	25.70	99.99	-	1,432	14,998	16,430	-	812	13,975	14,787
11	100.00	100.00	-	39	43,538	43,577	-	78	60,937	61,015
Total			7,435	16,293	59,553	83,281	5,942	14,844	75,027	95,813

40. Credit risk disclosures (continued)

Expected credit losses (continued)

Credit portfolio broken down by rating category and stages (continued)

	PD level		31 December 2019 Net exposure				31 December 2018 Net exposure			
	Upper	Lower	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000
Rating Category										
1	-	0.01	303,805	1,087	-	304,892	393,906	1,526	-	395,432
2	0.01	0.03	2,815,666	3,044	-	2,818,710	2,355,662	2,860	1,698	2,360,220
3	0.03	0.06	792,694	4,157	339	797,190	503,861	2,920	11	506,792
4	0.06	0.14	1,100,834	5,671	-	1,106,505	1,043,399	5,224	2	1,048,625
5	0.14	0.31	1,328,187	24,718	48	1,352,953	1,288,859	38,622	89	1,327,570
6	0.31	0.63	845,277	67,222	54	912,553	853,526	30,307	91	883,924
7	0.63	1.90	869,943	218,051	54	1,088,048	939,935	313,375	286	1,253,596
8	1.90	7.98	113,859	275,409	10,702	399,970	125,513	199,327	269	325,109
9	7.98	25.70	3,909	37,939	3,545	45,393	4,234	34,707	172	39,113
10	25.70	99.99	-	34,410	92,780	127,190	292	15,400	125,264	140,956
11	100.00	100.00	-	1,483	54,088	55,571	8	1,368	126,986	128,362
Total			8,174,174	673,191	161,610	9,008,975	7,509,195	645,636	254,868	8,409,699

	PD level		31 December 2019 Net exposure ex collateral				31 December 2018 Net exposure ex collateral			
	Upper	Lower	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000
Rating Category										
1	-	0.01	204,778	0	-	204,778	235,957	55	-	236,012
2	0.01	0.03	2,392,697	421	-	2,393,118	1,982,148	918	1,698	1,984,764
3	0.03	0.06	299,084	1,221	-	300,305	136,176	365	-	136,541
4	0.06	0.14	362,131	1,141	0	363,272	342,135	915	2	343,052
5	0.14	0.31	284,649	8,073	3	292,725	424,875	21,990	-	446,865
6	0.31	0.63	199,826	8,493	0	208,320	227,440	6,746	20	234,206
7	0.63	1.90	222,733	58,984	0	281,717	265,839	117,258	14	383,111
8	1.90	7.98	25,573	114,364	2,566	142,503	33,128	59,832	8	92,968
9	7.98	25.70	395	6,867	(0)	7,262	778	7,252	10	8,040
10	25.70	99.99	-	10,868	26,281	37,149	205	2,171	59,463	61,839
11	100.00	100.00	-	238	5,965	6,203	8	339	68,549	68,896
Total			3,991,866	210,671	34,815	4,237,352	3,648,689	217,841	129,764	3,996,294

Non performing loans

The net exposure from non-performing loans and advances to customers amounted to £161,610,000 at 31 December 2019 (2018: £254,868,000).

40. Credit risk disclosures (continued)

Breakdown of credit exposure (continued)

Credit exposure broken down by industry and stages

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 that has been adapted to the Bank's business risk approach used for the active management of the credit portfolio. The Bank has updated this segmentation in the first quarter of 2019 in order to better reflect current credit risk management areas.

	31 December 2019 Gross exposure				31 December 2018 Gross exposure			
	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000
Public institutions	2,328,370	300	-	2,328,670	1,854,603	1	-	1,854,604
Agriculture	405,212	102,601	31,648	539,461	417,539	117,107	21,155	555,801
Commercial property	436,886	98,474	72,142	607,502	506,033	112,908	68,311	687,252
Non-profit and associations	460,277	11,862	2,257	474,396	483,108	7,112	3,767	493,987
Personal customers	2,800,509	229,559	51,974	3,082,042	2,562,795	193,937	79,789	2,836,521
Business customers	1,719,355	245,550	63,142	2,028,048	1,663,109	229,375	156,873	2,049,357
Other	30,999	1,138	-	32,137	27,950	40	-	27,990
Total	8,181,609	689,484	221,163	9,092,256	7,515,137	660,480	329,895	8,505,512

	31 December 2019 Expected Credit Loss				31 December 2018 Expected Credit Loss			
	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000
Public institutions	49	0	-	49	45	-	-	45
Agriculture	901	1,458	7,355	9,714	542	1,700	2,375	4,617
Commercial property	1,567	3,331	9,390	14,289	1,158	3,411	16,845	21,414
Non-profit and associations	366	619	1,589	2,574	374	422	1,636	2,432
Personal customers	1,489	5,169	17,726	24,384	1,470	5,520	20,052	27,042
Business customers	2,324	5,624	23,493	31,440	2,349	3,791	34,119	40,259
Other	740	91	-	831	4	-	-	4
Total	7,436	16,292	59,553	83,281	5,942	14,844	75,027	95,813

	31 December 2019 Net exposure				31 December 2018 Net exposure			
	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000
Public institutions	2,328,322	300	-	2,328,621	1,854,558	1	-	1,854,559
Agriculture	404,311	101,143	24,293	529,747	416,997	115,407	18,780	551,184
Commercial property	435,319	95,143	62,752	593,213	504,875	109,497	51,466	665,838
Non-profit and associations	459,911	11,243	668	471,822	482,734	6,690	2,131	491,555
Personal customers	2,799,020	224,390	34,247	3,057,658	2,561,325	188,417	59,737	2,809,479
Business customers	1,717,032	239,926	39,649	1,996,608	1,660,760	225,584	122,754	2,009,098
Other	30,259	1,047	-	31,306	27,946	40	-	27,986
Total	8,174,173	673,193	161,610	9,008,975	7,509,195	645,636	254,868	8,409,699

40. Credit risk disclosures (continued)

Breakdown of credit exposure (continued)

Credit exposure broken down by industry and stages (continued)

	31 December 2019 Net exposure ex collateral				31 December 2018 Net exposure ex collateral			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Public institutions	2,328,264	300	-	2,328,564	1,854,493	1	-	1,854,494
Agriculture	90,232	10,644	12,563	113,439	124,909	16,934	1,574	143,417
Commercial property	93,364	16,661	10,450	120,475	103,778	14,230	27,486	145,494
Non-profit and associations	131,569	1,254	22	132,845	224,535	1,783	1,720	228,038
Personal customers	487,110	58,425	1,554	547,089	495,625	62,489	23,056	581,170
Business customers	831,068	122,341	10,226	963,635	817,422	122,364	75,928	1,015,714
Other	30,259	1,046	-	31,305	27,927	40	-	27,967
Total	3,991,866	210,671	34,814	4,237,352	3,648,689	217,841	129,764	3,996,294

For financial assets that are credit impaired (stage 3) at 31 December 2019, £126,796,000 of collateral is held as security against these exposures. (2018: £125,074,000)

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. 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)

	2019 £'000	2018 £'000
Real estate/property		
Personal	2,507,892	2,224,179
Commercial	1,409,119	1,277,944
Agricultural	379,809	390,784
Equipment	381,512	377,874
Guarantees	1,532	1,525
Deposits	31,939	44,226
Other assets	59,820	96,872
Total collateral	4,771,623	4,413,404
Total unsecured credit exposure	4,237,352	3,996,294
Unsecured portion of credit exposure (%)	47%	48%

Past due amounts (no evidence of credit impairment)

	Total past due amounts		Total due under loans	
	2019 £'000	2018 £'000	2019 £'000	2018 £'000
6-30 days	1,054	758	10,842	6,686
31-60 days	171	330	6,630	3,493
> 60 days	423	259	3,134	2,828
Total past due amounts	1,648	1,347		
Total due under loans			20,606	13,007

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 credit 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 a Stage 3 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 stage 3 impaired

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2019	2019	2019	2019	2019
	£'000	£'000	£'000	£'000	£'000
Good upper	1,899,254	65,505	741,964	1,081,627	3,788,350
Good lower	640,864	62,273	387,984	637,887	1,729,008
Marginal	122,430	16,484	40,747	184,469	364,130
Vulnerable	23,212	1,594	26,807	26,290	77,903
Total : Neither past due nor Stage 3 impaired	2,685,760	145,856	1,197,502	1,930,273	5,959,392

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2018	2018	2018	2018	2018
	£'000	£'000	£'000	£'000	£'000
Good upper	1,719,696	53,035	818,520	895,181	3,486,432
Good lower	623,502	30,126	385,734	806,353	1,845,715
Marginal	122,743	19,472	53,807	101,521	297,543
Vulnerable	24,481	1,169	12,817	15,877	54,344
Total : Neither past due nor specifically impaired	2,490,422	103,802	1,270,878	1,818,932	5,684,034

Six days plus past due not Stage 3 impaired

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2019	2019	2019	2019	2019
	£'000	£'000	£'000	£'000	£'000
Good upper	2,367	107	13	4,356	6,844
Good lower	3,174	248	1,077	847	5,346
Marginal	3,355	366	118	863	4,703
Vulnerable	1,635	198	645	1,237	3,713
Total : Days past due not stage 3 impaired	10,530	919	1,853	7,303	20,606

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2018	2018	2018	2018	2018
	£'000	£'000	£'000	£'000	£'000
Good upper	1600	140	10	39	1789
Good lower	2473	230	2011	12	4726
Marginal	1554	310	6	1167	3037
Vulnerable	2109	198	945	205	3457
Total : Days past due not specifically 3 impaired	7,736	878	2,972	1,423	13,009

40. Credit risk disclosures (continued)

Measurement of credit risk (continued)

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2019	2019	2019	2019	2019
	£'000	£'000	£'000	£'000	£'000
Stage 3 impaired	24,061	27,923	92,769	63,047	207,800

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2018	2018	2018	2018	2018
	£'000	£'000	£'000	£'000	£'000
Stage 3 impaired	37,152	42,507	130,780	110,973	321,412

Gross loans and receivables

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2019	2019	2019	2019	2019
	£'000	£'000	£'000	£'000	£'000
Good Upper	1,901,621	65,612	741,977	1,085,984	3,795,194
Good Lower	644,038	62,521	389,061	638,734	1,734,354
Marginal	125,785	16,851	40,865	185,332	368,833
Vulnerable	24,847	1,792	27,452	27,526	81,617
Impaired	24,061	27,923	92,769	63,047	207,800
Gross loans and receivables	2,720,352	174,698	1,292,124	2,000,623	6,187,797

Gross loans and receivables

	Mortgages	Other Personal	Property & Construction	Non Property Business	Total
	2018	2018	2018	2018	2018
	£'000	£'000	£'000	£'000	£'000
Good Upper	1,721,296	53,175	818,530	895,220	3,488,221
Good Lower	625,975	30,356	387,745	806,365	1,850,441
Marginal	124,297	19,782	53,813	102,688	300,580
Vulnerable	26,590	1,367	13,762	16,082	57,801
Impaired	37,152	42,507	130,780	110,973	321,412
Gross loans and receivables	2,535,310	147,187	1,404,630	1,931,328	6,018,455

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.

	Number of loans	Loan balance	% of total mortgage portfolio	Impairment allowance	Coverage
		£'000		£'000	%
At 31 December 2019					
Variation to the customer's existing contract with the Bank	**29**	**3,453**	**0.1%**	**134**	**3.9%**
Renegotiation	**3**	**573**	**0.0%**	**64**	**11.2%**
Post default mutual agreement	**6**	**1,156**	**0.0%**	**52**	**4.5%**
	38	**5,182**	**0.2%**	**250**	**4.8%**
At 31 December 2018					
Variation to the customer's existing contract with the Bank	27	3,711	0.1%	128	3.4%
Renegotiation	2	555	0.0%	79	14.2%
Post default mutual agreement	1	35	0.0%	2	5.7%
	30	4,301	0.1%	209	4.9%

In addition forbearance measures are provided to 19 business customers as at 31 December 2019, having associated facilities of £35,600,000.

40. Credit risk disclosures (continued)

Forbearance (continued)

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

	2019 £'000	2018 £'000
Counterparty risk		
Derivatives with positive fair value	11,473	9,857
Credit exposure from other trading and investing activities		
Investment securities - hold to collect	595,554	518,082
Investment securities - hold to collect and sell	730,675	647,572
Investment in subsidiaries	250	250
Total	1,337,952	1,175,761

Investment securities

Investment securities are made up of UK government gilts and highly rated covered, sovereign, supernational and agency bonds.

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 2019 Number	Amount 2019 £'000	Persons 2018 Number	Amount 2018 £'000
Loans - balance at 31 December				
Directors	4	17,039	4	18,615
Executive Committee	4	633	6	338
	8	17,672	10	18,953
Deposits - balance at 31 December				
Directors	5	4,403	5	2,901
Executive Committee	6	215	8	605
	11	4,617	13	3,506

No credit impairment has been identified in respect of loans provided to Executive Committee members. Furthermore no debts were written off or forgiven during the year ended 31 December 2019 (2018: £Nil).

Included in the above are seven loans (2018: seven) totalling £17,039,000 (2018: £18,615,000) made to Directors, their close family members and companies which they control. The maximum aggregate amount outstanding during the year in respect of these loans was £18,618,000 (2018: £19,236,000).

(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 £80,000 in the year ended 31 December 2019 (2018: £77,000).

42. Employees

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

	2019 Number	2018 Number
Managers	372	375
Clerical staff	947	907
	1,319	1,282

43. Share based payments

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.

	2019 Weighted average exercise price DKK	2019 Number of conditional shares	2018 Weighted average exercise price DKK	2018 Number of conditional shares
Outstanding at the beginning of the year	0.00	36,006	0.37	31,039
Granted during the year	0.00	38,537	0.00	23,715
Exercised during the year	0.00	(27,278)	0.00	(16,994)
Forfeited during the year	0.00	(3,185)	0.00	(1,754)
Expired during the year	0.00	-	0.00	-
Outstanding at the end of the year	0.00	44,080	0.00	36,006
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 92.05. The conditional shares at 31 December 2019 had a weighted average exercise price of DKK 0.00 and a weighted average remaining contractual life of 2.5 years. As at 31 December 2019 there were 44,080 conditional shares with an exercise price of DKK 0.00. In the year ended 31 December 2019, conditional shares were granted in April 2019. The estimated fair value of the conditional shares granted on this date was £546,000. The charge for the year in respect of share based payments was £578,000 (2018: £570,000).

44. Post balance sheet events

The coronavirus outbreak (COVID-19) is a recent emerging risk. The Bank has invoked contingency planning to manage the operational impacts with a view to ensuring that customers can continue to access banking services and that the level of disruption is minimised. It is likely that the outbreak will impact market sectors to which the Bank is exposed and that there could be a negative impact on the Bank's future performance. The Bank is continually monitoring and assessing the range of potential impacts and will continue to respond to the situation as it evolves. The final impact will be dependent on a wide range of future developments which are highly uncertain and cannot be predicted.

45. 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.