# EBS LIMITED

## DIRECTORS' REPORT AND ANNUAL FINANCIAL STATEMENTS

## For the year ended 31 December 2013

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# Directors and other information

**DIRECTORS**

| | |
|---|---|
| Desmond Fitzgerald | Executive Director (Managing Director) |
| Bernard Byrne | Group Non-Executive Director |
| Fidelma Clarke | Group Non-Executive Director |
| Denis O'Callaghan | Group Non-Executive Director |
| Catherine Woods | Independent Non-Executive Director and Chairman |
| Tom Foley | Independent Non-Executive Director |
| James O'Hara | Independent Non-Executive Director |

| | |
|---|---|
| **SECRETARY** | Sarah McLaughlin |
| **REGISTERED OFFICE** | 2 Burlington Road<br>Dublin 4 |
| **REGISTERED NUMBER** | 500748 |
| **INDEPENDENT AUDITOR** | Deloitte & Touche<br>Chartered Accountants and Statutory Audit Firm<br>Hardwicke House<br>Hatch Street<br>Dublin 2 |
| **BANKER** | Allied Irish Banks, p.l.c.<br>7/12 Dame Street<br>Dublin 2 |

# DIRECTORS' REPORT

The Directors of EBS Limited present their Directors' report and annual financial statements of EBS Limited and its' subsidiaries (the 'Group') for the year ended 31 December 2013. A statement of Directors' responsibilities in relation to the financial statements appears on page 12.

## Activities of the Company

EBS Limited ('EBS' or 'the Bank'), a private company limited by shares, domiciled in Ireland, is a member of the EBS Group and is a wholly owned subsidiary of Allied Irish Banks p.l.c., ('AIB p.l.c.'), which is a member of AIB group. AIB p.l.c. operates EBS as a standalone, separately branded subsidiary with its own distribution network.

EBS operates in the Republic of Ireland and has a countrywide network of 74 offices and a direct telephone based distribution division (EBS Direct). EBS's network gives it a physical presence in communities across Ireland and this is important in allowing it to provide a high quality service to its customers. EBS also distributes mortgages through Haven Mortgages Limited, a wholly owned subsidiary, to independent mortgage intermediaries.

EBS is regulated by the Central Bank of Ireland ('CBI') and has an Irish banking licence under the Central Bank of Ireland Act 1971 (as amended).

EBS is a covered institution within the meaning of the Government Guarantee Scheme (the 'Scheme') and stood specified under the Credit Institutions (Financial Support) (Specification of Institutions) Order 2008 (Statutory Instrument No. 416 of 2008) ('CIFS') for the period 30 September 2008 to 29 September 2010.

EBS is a participating institution since 1 February 2010 under the Credit Institutions (Eligible Liabilities Guarantee) Scheme 2009 ('ELG') which came into effect on 9 December 2009. In December 2012, the European Commission further extended the ELG issuance to the 30 June 2013. On 26 February 2013, the Irish Government announced that the ELG would end at midnight on 28 March 2013. After that date any new liabilities were not covered by the Eligible Liabilities Guarantee Scheme. Liabilities incurred since January 2010 and before the scheme's end continue to be guaranteed until their maturity date.

## Business Review

During 2013, Ireland emerged from the European Union ('EU')/International Monetary Fund ('IMF') Programme against a background of increased market confidence. This has been a significant factor in an improvement in the market's assessment of Ireland's creditworthiness and is helping the sovereign and domestic banks to regain access to market funding at, increasingly, more favourable rates. Unemployment levels have declined consistently throughout the year and are 12.4% at December 2013 compared to 14.0% at December 2012 (Source: Central Statistics Office 'CSO').

As noted in the CSO house price index, average residential property prices increased by 6.4% in 2013 and have now decreased 46% from peak. This compares to a decline of 4.5% recorded in the twelve months to December 2012 and a peak to trough of 50% in 2012. In Dublin, the average residential property price increase was more pronounced and during 2013 average property prices increased by 15.7%. In Dublin, since the peak of the housing market, property prices have now decreased by 49% as at the end of 2013 compared to 56% as at the end of 2012. Outside Dublin, property prices have remained virtually unchanged when compared to 2012 and have declined 47% since the peak of market as at the end of 2013.

At 31 December 2013, the Group's Mortgage portfolio before impairments stood at €13.4bn (2012: €13.9bn) being Residential €13.1bn and Commercial €0.3bn (2012: Residential €13.6bn and Commercial €0.3bn). The decline in mortgage balances is due to customer repayments and redemptions exceeding new lending during the year, together with additional loan impairments.

# DIRECTORS' REPORT (CONTINUED)

## Business Review (continued)

EBS exited from the Commercial Lending market in 2008 and transferred all land and development and associated loans to the National Asset Management Agency ('NAMA') in 2010 and 2011 and sold a portfolio of commercial loans in 2012. This business has been discontinued.

The integration programme of EBS into the AIB Group was further progressed in 2013 with the completion of the following transactions with AIB P.L.C., to facilitate the implementation of more efficient Treasury management processes, (1) the sale of securities with a nominal value of €680m being the majority of its' Available for Sale ('AFS') investment portfolio, (2) the novation of the majority of EBS' portfolio of derivatives with counterparties outside the AIB Group and (3) the sale of EBS's holding of NAMA Senior Bonds. These transactions resulted in a net gain to EBS of €9m.

## Balance Sheet Assessment ('BSA')

The CBI concluded a BSA of the three credit institutions covered under the ELG, including AIB Group, in the fourth quarter of 2013. This review included an assessment of asset quality, risk weighted assets and point in time capital adequacy as at 30 June 2013. In early December 2013, AIB was advised of the findings of this review and has considered them in the preparation of the Group's year end December 2013 impairment provisions, capital position and financial statements. The BSA review process included a top down mortgage modelling exercise and a review of the classification of 670 mortgages. The review was conducted in line with the CBI impairment guidelines issued in May 2013. The Group determines impairment provisions on an ongoing basis in accordance with IFRS accounting standards, which takes into account impairment triggers, collateral valuations and the timing of realisation. In arriving at the 2013 total credit impairment provisions charge for EBS of €401m, consideration was given to the CBI BSA findings and impairment guidelines.

## Corporate Governance

AIB Group is subject to the provisions of the Central Banks' Corporate Governance Code for Credit Institutions and Insurance Undertakings ("CBI Code"), including compliance with requirements which specifically relate to 'major institutions', which imposes minimum core standards upon all credit institutions and insurance undertakings licensed or authorised by the Central Bank. AIB Groups' corporate governance practices also reflect Irish company law and, in relation to the UK businesses, UK company law, the Listing Rules of the Enterprise Securities Market of the Irish Stock Exchange, and certain provisions of the US Sarbanes Oxley Act of 2002. As a separately licensed credit institution, the Banks' corporate governance practices also reflect the relevant provisions of the CBI Code. The Bank has fully applied the principals of the UK Corporate Governance Code.

The AIB Group as a separately licensed credit institution, EBS' corporate governance practices also reflect the relevant provisions of the CBI Code. The Board's policy is to comply with the highest standards of corporate governance as set out in the CBI Code. EBS is required to submit a compliance statement to the CBI annually confirming compliance with the CBI Code. For 2013, the compliance statement will be submitted to the CBI along with a copy of the 2013 Annual Report and Accounts following approval by the Board.

Governance is exercised through the Board of Directors (the 'Board') and a senior management team. The conditions of EBS' Central Bank licence require that there should be a minimum of two Non-Executive Directors who are independent of the parent. Throughout 2013, there were three independent Non-Executive Directors on the Board. The Board also included one Executive Director, who was directly involved in the operation of EBS, and three other directors who, while also employees of AIB p.l.c. were deemed to be Non-Executive Director by virtue of the role they fulfilled in areas of AIB Group unrelated to the operations of EBS.

## DIRECTORS' REPORT (CONTINUED)

### Results for the year ended 31 December 2013
The Group reported a loss after taxation of €243m for the year, €481m less than the restated 2012 loss of €724m.

Net Interest Income
Net interest income for the year is €172m compared to €143m in 2012, up €29m or 20%.
The net interest margin (including charges under the ELG scheme) is 1.13% compared to 0.82% for 2012. The net increase of 31 basis points (bps) is due to:

- A decrease in the cost of interest on debt securities in issue, representing an increase of 0.20%.
- A decrease in retail funding costs including ELG, representing an increase of 0.05%.
- A decrease in wholesale funding costs, representing an increase of 0.6%.

Interest income on mortgage loans is €482m (2012: €554m). The decrease of €72m is mainly due to a decrease in the loan book, and lower average European Central Bank ('ECB') rates for 2013, and the full year impact of the sale of loans and advances with a carrying value of €1,513m during 2012.

Interest expense on customer accounts is €322m (2012: €377m). The decrease year on year is due to lower average balances as funding requirements reduce due to reduced mortgage assets and lower interest rates.

Other Income/(Loss)
Other income for the year is €31m compared to a loss of €654m in 2012.
The main drivers for the improvement are:

- Once off gain in 2013 of €16m from disposal of available for sale ('AFS') assets to AIB Group Treasury.
- Loss of €668m on sale of two portfolios of buy-to-let mortgage assets in 2012. There were no disposals in 2013.

Operating Expenses
Operating expenses are down €11m or a decrease of 13% from 2012.

Administrative expenses in 2013 are €65m compared to €75m in 2012. The decrease is due mainly to a defined benefit pension scheme curtailment gain of €15m in respect of the closure of the scheme to future accrual. The costs for 2013 also include €4m of voluntary severance payments to staff leaving EBS on the same terms as offered to employees of the AIB Group.

Excluding losses on disposal of loans, voluntary severance costs and pension adjustments, the cost to income ratio for 2013 is 42% compared to 54% in 2012 on a like for like basis. The improvement is due to increased income in 2013, mainly driven by increased net interest income and a gain on disposal of AFS assets to AIB p.l.c..

Loss before Taxation
Loss before tax of €272m is down by €556m from 31 December 2012 (2012: loss of €828m).
The reported loss before tax of €272m is attributable to the impairments incurred on loans and advances to customers of €401m.

Impairment Charge on Loans and Advances to Customers
The loan impairment provisions charge for loans and advances to customers for 2013 is €401m up from €229m in 2012. Total provisions held at December 2013 amount to €1,352m (2012: €934m). This total provision balance represents 10.1% of total loans and advances to customers (2012: 6.7%).

The impairment charge has increased principally due to:

- The adoption of a new Individually Insignificant ('II') provisioning model by EBS Group;
- An increase in impaired residential balances;
- An increase in the expected repossession rate; and
- An increase in the emergence period.

# DIRECTORS' REPORT (CONTINUED)

## Results for the year ended 31 December 2013 (continued)

The detailed breakdown of the impairment provisions stock together with impaired loans is set out below:

| Group 2013 | Loans & Advances | Impaired Loans & Advances | Impaired % of Loans | Total Impairment Provision | Provision % of Impaired Loans | Provision % of Loans |
|---|---|---|---|---|---|---|
| **Classification** | **€m** | **€m** | | **€m** | | |
| **Residential** | 13,116 | 3,217 | 24.5% | 1,272 | 39.5% | 9.7% |
| **Commercial** | 261 | 122 | 46.7% | 80 | 65.6% | 30.7% |
| **Total** | **13,377** | **3,339** | **25.0%** | **1,352** | **40.5%** | **10.1%** |

| Group 2012 | Loans & Advances | Impaired Loans & Advances | Impaired % of Loans | Total Impairment Provision | Provision % of Impaired Loans | Provision % of Loans |
|---|---|---|---|---|---|---|
| **Classification** | **€m** | **€m** | | **€m** | | |
| **Residential** | 13,625 | 2,904 | 21.3% | 869 | 29.9% | 6.4% |
| **Commercial** | 278 | 110 | 39.6% | 65 | 59.1% | 23.4% |
| **Total** | **13,903** | **3,014** | **21.7%** | **934** | **31.0%** | **6.7%** |

Residential Loan Book Asset Quality

Residential loans more than 90 days past due or impaired increased from 21.7% at December 2012 to 24.9% at December 2013. Impaired loans were 24.5% at December 2013, up from 21.3% at December 2012. This reflects the ongoing impact of unemployment, the impact of the sovereign requirements for an EU/IMF loan, and the associated fiscal policy measures causing financial stress for a greater number of borrowers.

The high level of unemployment, coupled with a general reduction in disposable income (including increased taxes and pay reductions) has had an adverse impact on borrowers' ability to repay loans which is evidenced by the increasing arrears on residential property mortgages.

Management remain focussed on arrears management and have taken timely action to minimise losses including additional resources in terms of staff and processes.

EBS is fully committed to supporting customers in financial difficulty and has implemented the CBIs' Code of Conduct on Mortgage Arrears to help support mortgage customers who are in arrears or are at risk of going into arrears. The protection of the Code applies to a property occupied as a family home by the borrower or a borrower's only residential property in the State.

Since 2011, a number of initiatives and regulations were introduced following the Inter-Departmental Working Group on Mortgage Arrears, including the publication of the 'Keane Report', the Code of Conduct on Mortgage Arrears, the Consumer Protection Code 2012 and the 2012 Code of Conduct for Business Lending to Small and Medium Enterprises, and the requirement for Mortgage Arrears Resolution Strategies. Collectively, these have led to a need for more sophisticated mortgage arrears management strategies, in particular, the application of forbearance measures which were introduced in 2012 and extended in 2013. The impact of these measures is resulting in an improvement in the trend of loan arrears, but it does increase the risk of potential loan losses which the Group would not otherwise incur as it may lead to a lack of willingness (as opposed to ability) to repay loans. Furthermore, there is a risk that the reforms of Irish bankruptcy law may result in more customers choosing this as a debt solution.

# DIRECTORS' REPORT (CONTINUED)

## Results for the year ended 31 December 2013 (continued)

Residential Loan Book Asset Quality (continued)
Where possible, arrangements are entered into with borrowers that are experiencing financial difficulty in order for them to manage their mortgage repayments. If an arrangement is agreed, the arrears are not adjusted other than where the borrower repays the outstanding arrears.

Hence all loans regardless of arrangements in place are included in the past due category. In certain circumstances (where the borrower has indicated an intent and capacity to repay) the loan terms may be modified by, for example, capitalising the arrears, switching to interest only for an agreed period or extending the loan term when it represents the best option for the customer to return the loan to a performing status and when the option does not result in a worse outcome for EBS than the possible alternatives.

Commercial Loan Book Asset Quality
Commercial loans more than 90 days past due or impaired increased from 47.5% at December 2012 to 51.7% at December 2013. Impaired loans were 46.7% at December 2013 up from 39.6% at December 2012. The deterioration in the underlying asset quality is due to continuing weakness in the commercial property market and economic environment generally. The level of provisions coverage on commercial loans increased marginally to 30.7% at December 2013 from 23.4% at December 2012.

Mortgage Market
The residential mortgage market in Ireland stabilised, albeit at a low level, with total advances of €2.5bn in 2013 compared to €2.6bn in 2012. New residential lending for the EBS Group is €107m in 2013 up from €27m in 2012 as EBS increased its market presence during the year. The overall mortgage market is much reduced, down 94% from its peak in 2006. EBS' share of new mortgage lending in 2013 is 4.4% (2012: 1.1%) and the EBS Groups' share of outstanding retail mortgage balances is approximately 10.5% (2012: 10.5%).

**Funding**
EBS Group is funded through a combination of retail and wholesale deposits. EBS is committed to maintaining an appropriate customer deposit base and reducing the dependence on wholesale funding, including funding from monetary authorities (including the ECB and CBI).

Customer Funding
EBS' strategy is to optimise funding requirements by matching its funding mix to the loan book portfolio, taking into account AIB Group funding policy and Basel III developments. EBS continues to have a strong franchise in the retail deposit market and at 31 December 2013 EBS has total customer accounts of €9,297m (2012: €10,117m). Customer funding is down by €820m due largely to taking a lead in the market to reduce funding costs.

Retail balances were €6,484m at 31 December 2013 (2012: €7,431m) and represent 70% (2012: 73%) of customer funding.

Wholesale Funding
Following the acquisition of EBS Limited by AIB Group in July 2011, EBS wholesale funding was limited to repo funding from market counterparties, the ECB and funding from AIB p.l.c. Over the course of 2013 EBS' wholesale funding balances were reduced by €1,239m. This was due to the reduction in repo funding secured on the AFS asset portfolio as these assets were sold to AIB p.l.c during the year. Debt securities in issue reduced by €181m to €2,001m primarily due to maturing securities not being replaced with new issues. Unsecured funding from AIB Group was increased by €649m to €665m by December 2013 and ECB funding was €1,485m lower at €975m representing 7% of total funding (2012: €2,460 and 16%).

## DIRECTORS' REPORT (CONTINUED)

### Results for the year ended 31 December 2013 (continued)

**Capital**

Regulatory Background

Following on from the CBI's 2011 Financial Measures Program ('FMP'), the regulatory capital requirements landscape has changed for EBS. The FMP which incorporated the Prudential Capital Assessment Review ('PCAR') and Prudential Liability Assessment Review ('PLAR') assessed the EBS's capital requirement at €1.5bn (being €1.2bn of a base requirement plus a buffer of €0.3bn for adverse deviations). Following the acquisition of EBS by AIB p.l.c. on 1 July 2011, the €1.5bn of capital was provided to AIB p.l.c. by the Irish Government in July 2011.

The required regulatory total capital ratio confirmed by the CBI is 8% for EBS. On September 2nd 2013 the CBI reduced the total capital ratio for EBS Mortgage Finance from 9% to 8%.

The primary driver of the €1.5bn capital requirement for EBS arose from loses expected to be incurred by EBS on the deleverage of €2.5bn of non-core assets by December 2013 via open market sales. To date EBS has sold €1.8bn in Non Core loans. As AIB Group. has achieved its deleveraging commitments no further loan sales are planned.

Capital Issue

In order to maintain adequate capital levels, EBS issued €330m of ordinary shares which were subscribed for in full by AIB p.l.c. for cash in December 2013. EBS is dependent on its parent AIB p.l.c. for on going funding and capital support.

The Group capital ratios at 31 December are as follows:

| | **2013 €m** | **2012 €m** |
|---|---|---|
| Core Tier 1 Capital | 789 | 706 |
| Non Core Tier 1 Capital | - | - |
| Tier 1 Capital | 789 | 706 |
| Tier 2 Capital | 99 | 111 |
| **Total Capital** | **888** | **817** |
| **Risk Weighted Assets** | 8,298 | 8,914 |
| Total Capital Ratio | 10.7% | 9.2% |
| Tier 1 Ratio | 9.5% | 7.9% |
| Core Tier 1 Ratio | 9.5% | 7.9% |

The total capital ratio at 31 December 2013 is 10.7% (2012: 9.2%); the increase in the capital ratio is due to additional capital drawn down in December 2013 offset by additional impairments changed in 2013.

### Risk Management

The risk management framework provides a firm-wide definition of risk and lays down the principles of how risk is to be identified, assessed, measured, monitored and controlled / mitigated, and the associated allocation of capital against same. The Group categorises risks under a number of headings namely, strategic, operational, compliance and financial (including credit, liquidity and market) risks. Together, these form the Group's Risk Universe. This helps the Group to assess and manage risk on an enterprise wide, holistic basis. The Risk Universe is continuously reviewed and updated reflecting the changing risk environment.

Further information in relation to the risk factors affecting the Group are set out in the Risk Management Report.

# DIRECTORS' REPORT (CONTINUED)

## Going Concern

The financial statements for the year ended 31 December 2013 have been prepared on a going concern basis as the Directors are satisfied, having considered the risks and uncertainties impacting the Bank, that it has the ability to continue in business for the period of assessment.

EBS is dependent on its parent, AIB, p.l.c. for continued funding and is therefore dependent on the going concern status of the Parent.

The financial statements of AIB p.l.c. have been prepared on a going concern basis as the Directors of AIB Group are satisfied, having considered the risks and uncertainties impacting the AIB Group, that it has the ability to continue in business for the foreseeable future. In making its assessment, the Group Directors have considered a wide range of information relating to present and future conditions. These have included financial plans prepared in November 2013 covering the period 2014 to 2016, the restructuring plan submitted to the European Commission in September 2012, liquidity and funding forecasts, and capital resources projections, all of which have been prepared under base and stress scenarios. In addition, the Directors have considered the commitment of support provided to AIB by the Irish Government. Furthermore, the Directors have considered the outlook for the Irish, the eurozone and UK economies.

**Conclusion**

On the basis of the continued availability of funding from AIB, p.l.c. to EBS Limited, the Directors of the Bank consider that it is appropriate to prepare the financial statements on a going concern basis at this time.

## Directors

The Directors at the date of this report are listed on page 2.

## Directors' and Secretary's Interest in Shares

The beneficial interests of the Directors and the Secretary in office at 31 December 2013, and of their spouses and minor children, in the shares of group companies are set out below. The shares referred to are €0.01 ordinary shares in AIB p.l.c. the holding company.

| **Ordinary shares** | **31 December 2013** | **1 January 2013*** |
|---|---|---|
| **Directors:** | | |
| Catherine Woods | Nil | Nil |
| Bernard Byrne | Nil | Nil |
| Fidelma Clarke | Nil | Nil |
| Tom Foley | 100 | 100 |
| Desmond Fitzgerald | Nil | Nil |
| Denis O'Callaghan | 13,749 | 13,749 |
| James O'Hara | Nil | Nil |
| **Secretary:** | | |
| Sarah McLaughlin | 377 | 377 |

**** or date of appointment, if later.***

# DIRECTORS' REPORT (CONTINUED)

## Share options

Details of the Directors' and the Secretary's options to subscribe for ordinary shares in AIB are given below. The vesting of these options to the individuals concerned is dependent on Earnings Per Share ('EPS') targets being met by AIB. Subject thereto, the options outstanding at 31 December 2013 are exercisable at various dates between 2013 and 2015. Details are shown in the Register of Directors' and Secretary's Interests, which may be inspected at AIB p.l.c.'s registered office, Bankcentre, Ballsbridge, Dublin 4, Ireland.

| | 31 December 2013 | 1 January 2013 | Options lapsed | Weighted average subscription price of options outstanding 31 December 2013 |
|---|---|---|---|---|
| **Directors:** | | | | € |
| Bernard Byrne | Nil | Nil | Nil | Nil |
| Fidelma Clarke | Nil | Nil | Nil | Nil |
| Desmond Fitzgerald | Nil | Nil | Nil | Nil |
| Tom Foley | Nil | Nil | Nil | Nil |
| Catherine Woods | Nil | Nil | Nil | Nil |
| Denis O'Callaghan | 10,500 | 20,500 | 10,000 | 14.3 |
| James O'Hara | Nil | Nil | Nil | Nil |
| | | | | |
| **Secretary** | | | | |
| Sarah McLaughlin | Nil | Nil | Nil | Nil |

Independent Non-Executive Directors do not participate in share option plans. No options were granted or exercised during the year.

## Long term incentive plans

There were no conditional grants of awards of ordinary shares outstanding to Group Non Executive Directors, Executive Director or the Company Secretary at 31 December 2013.

Independent Non-Executive Directors do not participate in long term incentive plans.

Apart from the interests set out above, the Directors and Secretary and their spouses and minor children have no other interests in the shares of AIB, p.l.c..

There were no changes in the Directors' and Secretary's interests between 31 December 2013 and 13 March 2014.

## Directors and Secretary

There were no changes to the Board of Directors during 2013.

## Events since the year end

In the directors' view, there have been no events since the year end that have had a material effect on the financial position of the Group.

# DIRECTORS' REPORT (CONTINUED)

## Books of account

The measures taken by the Directors to secure compliance with the EBS's obligation to keep proper books of account, are the use of appropriate systems and procedures and the employment of competent persons, which is performed under a master service agreement by Allied Irish Banks p.l.c. The books of account are kept at the Allied Irish Banks p.l.c.'s Registered Office, Bankcentre, Ballsbridge, Dublin 4, Ireland.

## Independent auditors

Deloitte & Touche, Chartered Accountants and Statutory Audit Firm, were appointed as auditors on the 30 July 2013. Deloitte & Touche have expressed their willingness to continue in office under Section 160(2) of the Companies Act, 1963.

## On behalf of the Board

Desmond Fitzgerald, Managing Director

Catherine Woods, Non-Executive Director

13 March 2014

## STATEMENT OF DIRECTORS' RESPONSIBILITIES

The following statement, which should be read in conjunction with the statement of Auditors' responsibilities set out with their Audit Report, is made with a view to distinguish for shareholders the respective responsibilities of the Directors and of the Auditor in relation to the financial statements.

The Directors are responsible for preparing the group and company financial statements, in accordance with applicable laws and regulations.

Company law requires the Directors to prepare group and company financial statements for each financial year. Under that law, the directors are required to prepare the financial statements in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the EU and as applied in accordance with the provisions of the Companies Acts, 1963 to 2013.

The Group and Company financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position and performance of the Group and Company; the Companies Acts, 1963 to 2013 provide in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing each of the financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state that the financial statements comply with IFRS's as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group and company will continue in business.

The Directors are responsible for keeping proper books of account that disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that its financial statements comply with the Companies Acts, 1963 to 2013. They are also responsible for taking such steps as are reasonably open to them to safeguard the assets of the group and company and to prevent and detect fraud and other irregularities.

The Directors are also responsible for preparing a Directors' report that complies with the requirements of the Companies Acts, 1963 to 2013.

The Directors that are listed on page 2 confirm, to the best of their knowledge and belief, that the financial statements, give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the company's affairs as at 31 December 2013 and of its loss for the year then ended.

On behalf of the board;

Desmond Fitzgerald, Managing Director

Catherine Woods, Non-Executive Director

# RISK MANAGEMENT REPORT

**1. Introduction**

The EBS Group assumes a variety of risks in undertaking its business activities. Risk is defined as any event that could damage the core earnings capacity of the Group, increase earnings or cash-flow volatility, reduce capital, threaten business reputation or viability, and/or breach regulatory or legal obligations.

EBS has a clearly defined Risk Governance structure and framework that is commensurate with the size, scale and complexity of the organisation. Over the course of 2013, the Group aligned and integrated its risk management structures and frameworks with the AIB Group.

The EBS Group's approach to identifying and monitoring the principal risks and uncertainties facing the Group is informed by risk factors. All of the EBS Group's activities involve, to varying degrees, the measurement, evaluation, acceptance and management of risks which are assessed on an AIB Group wide basis. Certain risks can be mitigated by the use of safeguards and appropriate systems and actions which form part of the AIB Group's risk management framework. The key risk factors to which the EBS Group is exposed and the governance and organisation framework through which the Group manages and seeks where possible to mitigate these risks are set out in section 5 below.

**2. Risk Management Framework**

EBS Group adopted an Enterprise Risk Management ('ERM') approach to identifying, assessing and managing risks, the core elements of which are set out in an Enterprise Risk Management Framework which was approved by the AIB Group Board during 2012.

This framework is in turn supported by a number of frameworks covering the management of specific risk categories (credit risk, operational risk, etc.) which were reviewed and approved by the AIB Group Board and adopted by EBS Group over the course of 2013.

The Board approved frameworks create clear ownership and accountability; ensure the EBS Group's most significant risk exposures are understood and managed in accordance with agreed risk appetite (for financial risks) and risk tolerances (for non-financial risks), and; ensures regular reporting of both risk exposures and the operating effectiveness of controls.

The EBS Group recognises that the effective management of risk and its system of internal control is essential to the minimisation of volatility against forecasted financial performance, the preservation of shareholder value and the achievement of the EBS Group's strategic objectives. The primary focus of the risk management framework is to ensure that the EBS Group achieves the optimal risk/reward return on any investment of people, time and resources. The core aspects of the EBS Group's risk management approach are described below.

The Group's risk identification and assessment framework described above is supported by a framework of stress testing, scenario and sensitivity analysis and reverse stress testing that seeks to ensure that risk assessment is dynamic and forward looking and considers not only existing risks but also potential and emerging threats. The Group undertakes a regular programme of stress testing across all its material risks to meet internal and regulatory requirements. In addition, ad-hoc stress tests are undertaken, as required, to inform strategic decision making.

**3. Risk Appetite Statement and Risk Policies**

The EBS Group's risk appetite is defined as the maximum amount of risk that the EBS Group is prepared to accept in order to deliver on its strategic and business objectives. The EBS Group maintains its own risk appetite statement ('RAS') which was last approved by the EBS Board in May 2013. The EBS Group RAS is aligned with the AIB Group RAS. The AIB Group RAS is currently in the process of being updated in line with its financial planning process and AIB Group strategy which will trigger a further review and update of the EBS Group RAS in Q1 2014. The RAS is a blend of qualitative and quantitative limits and triggers linked to the EBS Group's objectives covering areas such as credit risk, market risk, funding and liquidity risk and capital measures. The EBS Group's risk profile is measured against its risk appetite and adherence to the risk limits is monitored on an on going basis and reported monthly to the EBS Chief Risk Officer ('CRO') and at every Board meeting. Material breaches of risk appetite, if they occur, are escalated by the Board to the CBI.

Risk appetite limits and targets are cascaded where appropriate into more granular limits and targets across portfolios and business units. In turn, risk policies and procedures are updated, where appropriate, to reflect the limits of risk appetite across the EBS Group.

# RISK MANAGEMENT REPORT (continued)

**3. Risk Appetite Statement and Risk Policies (continued)**

These policies are closely managed on a day to day basis throughout EBS Group, and are monitored by specific business units with oversight by the relevant EBS Group risk committees. Material changes to these policies are assessed by the Management team on an annual basis and subsequently recommended to the Board for approval.

**4. Risk governance and risk management organisation**

Risk management in the EBS Group is aligned with a clearly defined risk governance structure at AIB Group level. The AIB Group ERM framework provides a robust and consistent approach to risk management across the EBS Group and is a core component of the EBS Group's Internal Governance framework.

Throughout 2013, the integrated governance, risk and control frameworks were further embedded continuing the use of a consistent approach to risk appetite, delegated authorities and governance committee structures.

The EBS Group has adopted a 'three lines of defence' framework in the delineation of accountabilities for risk governance. Under the three lines of defence model, primary responsibility for risk management lies with the business line management. The Risk Management Functions provide second line of defence, providing independent oversight and challenge to business line managers. The third line of defence is the AIB Group Internal Audit function which provides independent assurance to EBS on the effectiveness of the system of internal controls.

The Board was supported in 2013 by the work of the Board Audit Committee ('BAC'). The BAC supported the Board in reviewing existing internal control mechanisms to assess whether they are adequate and whether they are performing effectively, and in assessing adherence with laws and regulations in 2013. In addition it supported the work of the Board in relation to the EBS risk and control framework.

The EBS Management Team comprises the senior executive managers of the EBS Group who have responsibility for the management of the business as a whole. The key objective of the Management Team is to support the Managing Director in effective day-to-day running of the bank's business and in the delivery of the EBS Board approved strategy. It has responsibility for implementing the strategic business plan of the EBS Group, in line with AIB Group strategic objectives and monitoring actual and projected performance including profitability, impairments and capital ratios.

The risk management framework is supported by its underlying Risk Committees which during 2013 comprised of the Asset & Liability Committee ('ALCO'), the Risk Rating Approval Committee ('RRAC') and the Executive Risk Committee ('ERC'). Each of these committees, whose membership is approved by the Managing Director, was responsible for identifying actions to support robust risk management in line with the EBS Group risk appetite. Progress was monitored and reported regularly to the Board through the report of the Chief Risk Officer ('CRO'). Representatives from AIB Group Risk participated and attended each of the EBS Risk Committees as part of the alignment and oversight by AIB Group.

ALCO, which met monthly in 2013, monitors EBS Group's exposure to key market risks, i.e. liquidity risk, funding risk, interest rate risk in the banking book and, foreign exchange risk and its capital ratios. The Committee was responsible, in conjunction with AIB Group ALCO, for monitoring the adequacy of the liquidity framework and buffers, and for recommending the appropriate EBS Group funding and capital policies and plans to the Board for approval in line with AIB Group policies and planning. Responsibility for asset liability management has been outsourced to AIB Group ALCO.

During 2013, the roles and responsibilities of the ALCO have been subsumed into the EBS Management Team. On a monthly basis, the Management Team dedicate a meeting to its asset & liability management responsibilities.

Following a further review of risk governance in late 2012, the roles and responsibilities of a number of EBS Risk Committees, namely the Credit Risk Committee and the Operational Risk and Compliance Committee, which were in place during 2012, have been amalgamated to form one ERC. The main purpose of the ERC which was established in January 2013 and meets monthly, is to monitor, review and recommend an appropriate risk governance structure and risk appetite for EBS. In addition, the ERC is responsible for evaluating the adoption of AIB Group policies or alignment of EBS policies and providing recommendations to the Board in line with the overall risk appetite of the Group and AIB Group.

# RISK MANAGEMENT REPORT (continued)

**4. Risk governance and risk management organisation (continued)**

The Committee is also responsible for monitoring the make up and performance of the loan books and the adequacy of provisions for impaired loans. The evaluation of Counterparty Credit Risk and limit setting is performed at AIB Group level.

The RRAC, which met semi-annually in 2013, is responsible for the on-going validation and monitoring of risk rating systems, model performance and model output in terms of forecasting.

**5. Risk Factors**

EBS' approach to identifying and monitoring the principal risks and uncertainties it faces, is informed by risk factors. All of EBS' activities involve, to varying degrees, the measurement, evaluation, acceptance and management of risks which are assessed on a company wide basis. Certain risks can be mitigated by the use of safeguards and appropriate systems and actions which form part of EBS' risk management framework.

The principal risks and uncertainties facing EBS fall under the following broad categories:

- Macro-economic and geopolitical risk;
- Macro-prudential, regulatory and legal risks to our business model; and,
- Risks related to our business operations, governance and internal control systems.

The risks pertaining to each of these categories are set out in summary form and described in more detail in subsequent pages.

**Macro-economic and geopolitical risk**

- EBS' access to funding and liquidity is impacted by the financial instability within the Eurozone.
- Constraints on liquidity and market reaction to factors affecting Ireland and the Irish economy have created a challenging liquidity environment for the EBS Group.
- EBS' business may be adversely impacted by deterioration in economic and market conditions.
- Contagion risks could disrupt the markets and impact the EBS Group's financial condition.

**Macro-prudential, regulatory and legal risks to our business model**

- EBS Group is subject to Government supervision and oversight.
- The future of the EBS Group's business activities are subject to possible interventions by the Irish Government or the disposal of the Irish State's ownership interest in the AIB Group.
- EBS may be subject to the risk of having insufficient capital resources to meet increased minimum regulatory requirements.
- EBS Group's business activities must comply with increasing levels of regulation.
- EBS' participation in the NAMA Programme gives rise to certain residual financial risks.
- EBS may be adversely affected by further austerity and budget measures introduced by the Irish Government.
- The value of certain financial instruments recorded at fair value is determined using financial models incorporating assumptions, judgements and estimates that may change over time or may ultimately not turn out to be accurate and the value realised by EBS for its assets may be materially different from the current or estimated fair value.
- EBS Group's deferred tax assets are substantially dependent on the generation of future profits over an extended number of years.

**Risks related to business operations, governance and internal control systems**

- The EBS Group is subject to inherent credit risks in respect of customers and counterparties which could adversely affect the Group's results, financial condition and future prospects.
- EBS Group faces heightened operational risks.
- The Group's risk management strategies and techniques may be unsuccessful.
- There is a risk of litigation arising from the EBS Group's business activities.

These principal risks and uncertainties should not be considered as exhaustive and other factors not yet identified, or not currently considered material, may impact the EBS Group.

# RISK MANAGEMENT REPORT (continued)

## 5.1 Macro-economic and geopolitical risk

**1. EBS' access to funding and liquidity is adversely impacted by the financial instability within the Eurozone.**

While economic, monetary and political conditions have stabilised within the Eurozone in the last twelve months, there is still a risk that certain EU / Eurozone members may not be able to support their sovereign debt burdens and meet future financial obligations, which may result in a further downgrade of sovereign credit ratings. This could adversely affect the cost and availability of funding to EU Member States and European banks.

EBS Group is dependent on its parent the AIB Group for funding and liquidity management. The Irish sovereign rating has a direct impact on the AIB Group's rating, which is a key factor in attracting and retaining deposits. Any future downgrade of Ireland's sovereign rating or the Group's rating could threaten the Group's liquidity and funding including the AIB Group's deposit base and could also impede access to wholesale funding markets with consequent impacts on the EBS Group.

**2. Constraints on liquidity and market reaction to factors affecting Ireland and the Irish economy have created a challenging environment for the management of the Group liquidity.**

As noted above, the EBS Group is wholly dependent on its parent the AIB Group for funding and liquidity management. Until recently, the AIB Group has been operating in an exceptionally challenging environment where wholesale market conditions restricted the AIB Group's access to wholesale funding other than short duration and mainly secured funding. However, there has been recent improvement in market sentiment towards Irish issuers and the AIB Group has re-engaged in the wholesale funding market through the issuance of long dated secured and unsecured debt. However, any renewed stress or deterioration in credit market conditions could further restrict the AIB Group's access to wholesale funding.

The continuing availability of customer deposits to fund the AIB Group's loan portfolio is subject to factors outside the AIB Group's control, such as the loss of confidence of depositors in the Irish economy, the Irish financial services industry or the AIB Group. Any loss of confidence in the AIB Group, or in the financial services industry generally, could lead to losses of deposits over a short period of time.

To meet its funding requirements, the AIB Group has accessed a range of CBI liquidity facilities, including certain additional liquidity schemes introduced by the CBI for market participants during periods of dislocation in the funding markets. This included a switch from short term ECB drawings into two 3-year longer-term refinancing operations in December 2011 and March 2012. In accessing CBI and other secured lending facilities, the AIB Group has relied significantly on its qualifying liquid assets. The completion of the deleveraging programme combined with a stable customer deposits base has reduced the AIB Group's reliance on ECB funding and CBI liquidity facilities. The Credit Institutions Scheme 2009 (Statutory Instrument No. 490 of 2009), as amended (the 'ELG Scheme') was closed to covering further liabilities on 28 March 2013 and to date this event has had a negligible impact on deposit balances. However, in the unlikely event that the AIB Group exhausts its stock of available collateral for funding and unsecured funding is unavailable, it would be necessary to seek alternative sources of funding, including continued support by the Irish Government.

The Capital Requirements Regulation ('CRR') and the Capital Requirements Directive ('CRD'), published in the EU Official Journal on 27 June 2013, require banks to meet liquidity requirements including targets set for Basel III ratios, Net Stable Funding Ratio ('NSFR') and Liquidity Coverage Ratio ('LCR'). Meeting the phased implementation deadlines of these requirements could impose additional costs on the AIB Group.

# RISK MANAGEMENT REPORT (continued)

## 5.1 Macro-economic and geopolitical risk (continued)

**3. EBS' business may be adversely affected by deterioration in economic and market conditions.**
Deterioration in the performance of the Irish economy or other relevant economies has the potential to adversely affect the EBS Group's overall financial condition and performance. Such deterioration could result in reductions in business activity, lower demand for the EBS Group's products and services, reduced availability of credit, increased funding costs, decreased asset values and additional write downs and impairment charges.

While there are some signs of improvement and stabilisation in the Irish economy, any renewed stress or deterioration could impact the return of normalised markets for commercial and residential property. As the EBS Group remains heavily exposed to the Irish property market a prolonged delay in the recovery of the Irish market could have a negative impact on levels of arrears, the EBS Group's collateral values and consequently have a material impact on the EBS Group's future performance and results.

General economic conditions continue to be very challenging for customers. A continued high level of unemployment together with any further reduction in borrowers' disposable income (for example. current and future budgetary measures and reduction in salaries) has the potential to negatively impact customers' ability to repay existing loans. This could result in additional write downs and impairment charges for the Group and negatively impact the capital and earnings position of the Bank. Challenging economic conditions will also influence the demand for credit in the economy. A declining or continuing muted demand for credit has the potential to impact the EBS Group's financial position.

**4. Contagion risks could disrupt the markets and adversely affect the EBS Group's financial condition.**
The risk of contagion in the markets in which the EBS Group operates and dislocations caused by the interdependency of financial markets participants is an on-going material risk to the EBS Group's financial condition. Any reductions in the perceived creditworthiness of one or more corporate borrowers or financial institutions could lead to market-wide liquidity problems, losses and defaults, which could adversely affect the AIB Group's results, financial condition and future prospects. Another source of potential contagion risk relates to the Euro.

The risk of a Eurozone member withdrawing from the Eurozone has significantly reduced. However, if a Eurozone member exited from the Eurozone this would have a significant adverse effect on the financial stability of the Eurozone, the Irish financial system and Irish banks. In turn, this could result in a loss of customers' deposits, as well as creating immediate operational and business challenges for the EBS Group.

## 5.2 Macro-prudential, regulatory and legal risks to our business model

**1. EBS Group is subject to Government supervision and oversight.**
As a result of the recapitalisation of the AIB Group by the Irish Government, the AIB Group (including EBS Group) is subject to a set of obligations outlined under a number of Subscription and Placing Agreements impacting on the EBS Group's governance, remuneration, operations and lending activities. These obligations are in addition to certain commitments and restrictions to the operation of the AIB Group's business under the CIFS Scheme and the NAMA programme, all of which may serve to limit the EBS Group's operations and place significant demands on the reporting systems and resources of the EBS Group.

Extensive powers continue to be conferred on the Irish Minister for Finance. The Credit Institutions Stabilisation Act 2010 (the 'Stabilisation Act') conferred extensive powers on the Irish Minister for Finance to direct the affairs of and restructure credit institutions and reorganise their assets and liabilities.

# RISK MANAGEMENT REPORT (continued)

## 5.2 Macro-prudential, regulatory and legal risks to our business model (continued)

**1. EBS Group is subject to Government supervision and oversight. (continued)**
Pursuant to the Act, directors are required to act in a manner that is aligned to the interests of the State in the performance of their duties, having regard to public interest considerations specified in the Act. The Stabilisation Act will cease to have effect on 31 December 2014.

**2. The future of the EBS Group's business activities are subject to possible interventions by the Irish Government or the disposal of the Irish State's ownership interest in the AIB Group.**
The AIB Group is substantially owned by an agency of the Irish State and accordingly, subject to EU state aid rules, controlled by the Irish State. Such ownership or control may affect the EBS Group's operations, financial condition and future prospects.

In order to comply with contractual commitments imposed on the AIB Group in connection with its recapitalisation by the Irish State and with the requirements of EU state aid applicable in respect of that recapitalisation, a relationship framework was entered into between the Minister for Finance and the Group in March 2012. This provides the framework under which the relationship between the Minister and the Group is governed. Under the relationship framework, the authority and responsibility for strategy and commercial policies (including business plans and budgets) and conducting the Group's day-to-day operations rest with the Board of the AIB Group and its management team, but the appointment or removal of the chairman or chief executive officer of the AIB Group are reserved to the Minister, and in respect of which that Board may only engage with the prior consent of the Minister.

Nevertheless, for so long as ownership of the AIB Group remains within State control, there remains a risk of intervention by the Irish government in relation to the operations and policies of the AIB Group and its subsidiaries (including EBS Group). Such further interventions may have a negative impact on the operations of the AIB Group.

The Irish State may sell or otherwise dispose of its ownership interest in the AIB Group to any private or public entity, including any intergovernmental institution, such as the European Stability Mechanism. Any such sale or disposal, and any conditions attaching to it, could materially affect the Group's operations, financial condition and future prospects.

**3. EBS may be subject to the risk of having insufficient capital resources to meet increased minimum regulatory requirements.**
AIB Group's target capital requirements as determined by the CBI under the 2011 Prudential Capital Assessment Review are currently a core tier 1 ratio of 10.5% in the base scenario and 6% in a stressed scenario, (excluding a requirement for an additional protective buffer). EBS Group is dependent on its parent, AIB Group for capital management. EBS' minimum capital requirement, as part of the AIB Group, is currently a total capital ratio of 8%, not including an allowance for an additional protective buffer. As at December 2013 EBS achieved a total capital ratio of 10.7% which is significantly above the required level.

# RISK MANAGEMENT REPORT (continued)

## 5.2 Macro-prudential, regulatory and legal risks to our business model (continued)

**3. EBS may be subject to the risk of having insufficient capital resources to meet increased minimum regulatory requirements. (continued)**

AIB Group carries out extensive forward-looking stress tests on its capital position on a quarterly basis and, over the course of 2013, these have confirmed that the bank does not require additional capital within the defined stress level. However, given the levels of uncertainty in the current economic environment, there is a possibility that the economic outturn over the capital planning period may be materially worse than the stress scenario envisages and/or that losses on the AIB Group's (including EBS Group's) credit portfolio may be above forecast levels. Were such losses to be significantly greater than currently forecast, there is a risk that the AIB Group's capital position could be eroded to the extent that it would have insufficient capital to meet its regulatory requirements.

The CRR and the CRD, the EU's implementation of the Basel III reforms, were published in the EU Official Journal on 27 June 2013. As a result of these regulations, credit institutions may be required to increase the quantity and quality of their regulatory capital. Full details of requirements in this regard have yet to be confirmed by the competent authorities, and it is possible that the Group's target regulatory capital requirements may ultimately increase as a result.

The CBI conducted a balance sheet assessment of the three Irish credit institutions covered under the 'ELG' Scheme, including AIB Group, during the fourth quarter of 2013. This review included an assessment of asset quality, risk weighted assets and point in time capital as at 30 June 2013. AIB Group has been advised of the findings of this review and has considered them in the preparation of the AIB Group's year end December 2013 impairment provisions and financial statements.

In addition, the ECB announced during October 2013 that it will undertake a comprehensive assessment of the banking system, to be concluded in October 2014. This ECB exercise will entail a supervisory risk assessment, an Asset Quality Review and a Stress Test in order to provide a forward-looking view of banks' shock absorption capacity under stress. The assumptions under which these assessments take place (including use of Open Market Value or Economic Value basis for property valuations and provision assessment) have yet to be confirmed. The outcome of these assessments may lead to a range of follow-up actions for banks, possibly including requirements for changes in the AIB Group's capital requirements.

**4. EBS Group's business activities must comply with increasing levels of regulation.**

In 2013 a significant number of new regulations were issued by both by the CBI and the European Union. A particular focus in light of the mortgage forbearance issue has been the introduction of a revised Code of Conduct on Mortgage Arrears and the new personal insolvency legislation which had taken full effect by December 2013. A risk arises from potential changes in customer attitude to debt obligations given that the new legislation allows for the agreed settlement and/or of unsecured debt, and the settlement and or/restructuring of secured debts up to a maximum of €3 million. The inclusion of secured debt in the non-judicial process is unprecedented, and therefore, it is difficult to gauge its impact. The legal uncertainty with regard to the availability of certain remedies for the enforcement of mortgages over Irish land entered into prior to 1 December 2009 has been removed by the Land and Conveyancing Law Reform Act 2013 which was enacted on 24 July 2013.

The long anticipated revision to the EU Capital Requirements Directive and Regulation ('CRD IV') comes into force on 1st January 2014 and will be gradually implemented over 5 years. This omnibus legislation will, among other measures, increase capital buffers and introduce new liquidity and leverage ratios for greater transparency. It also provides for the introduction in November 2014 of a new banking supervisory system (a Single Supervisory Mechanism) which will see the Eurozone's largest banks, including AIB Group and its subsidiaries, coming under the direct supervision of the ECB. Other measures likely to impact on the business in 2014 include the Credit Reporting Bill creating a new centralised credit bureau and the revised Corporate Governance Code.

The delivery of this level of regulatory change will place strain on the organisation's resources, particularly during a period of significant restructuring and consolidation.

# RISK MANAGEMENT REPORT (continued)

## 5.2 Macro-prudential, regulatory and legal risks to our business model (continued)

**4. EBS Group's business activities must comply with increasing levels of regulation. (continued)**
The challenge of meeting tight implementation deadlines while balancing competing resource priorities and demands adds to the regulatory risk to the EBS Group. These may also impact significantly on the EBS Group's future product range, distribution channels, funding sources, capital requirements and consequently, reported results and financing requirements.

**5. EBS' participation in the NAMA Programme gives rise to certain residual financial risks.**
On 8 April 2009, the Minister for Finance announced that a NAMA would be established on a statutory basis for the purpose of strengthening the Irish financial system as a whole.

Legislation was enacted (the National Asset Management Agency Act 2009 ('NAMA Act')) in November 2009 which established NAMA, with the Group being designated in February 2010 as a participating institution under the NAMA Act.

In 2011, €77.0m in loans and advances were transferred to NAMA by the EBS Group. This was in addition to the €836.4m in 2010.

Section 93 of the NAMA Act (Clawback of overpayments) provides that where a participating institution receives an amount to which it was not entitled, that the participating institution will repay such amount to NAMA. Any payments to NAMA in relation to such 'Clawback' may have an adverse effect on the AIB Group. Section 135 of the NAMA Act [and Clause 9.2 of NAMA's Acquisition Terms and Conditions] directs the AIB Group to provide a series of indemnities to NAMA relating to the transferred assets. Any payment by the AIB Group to NAMA in respect of the indemnities may have an adverse effect on the Group.

Section 225 of the NAMA Act provides that, on the dissolution or restructuring of NAMA, the Minister for Finance may require that a report and accounts be prepared. In the event that NAMA shows that an aggregate loss has been incurred during the period since its establishment, the Irish Minister for Finance may impose a surcharge on AIB, as a participating institution (under additional legislation which would be enacted). No surcharge will become payable until either (a) 10 years after the passing of the NAMA Act; or (b) NAMA is dissolved or restructured, or there is a material alteration of NAMA's functions, whichever is last to occur.

In addition, credit exposure to NAMA arises from the senior and subordinated NAMA bonds acquired by the Group in consideration for the transfer of assets to NAMA.

Any of these events may serve to limit the EBS Group's operations and could have a material adverse effect on the EBS Group's results, financial condition and future prospects.

**6. EBS may be adversely affected by further austerity and budget measures introduced by the Irish Government.**
The current and future budgetary and taxation policy of Ireland and other measures adopted by Ireland may have an adverse impact on borrowers' ability to repay their loans and, as a result, the EBS Group's business. Furthermore, some measures may directly impact the financial performance of the group through the imposition of measures such as the recently imposed bank levy.

# RISK MANAGEMENT REPORT (continued)

## 5.2 Macro-prudential, regulatory and legal risks to our business model (continued)

**7. The value of certain financial instruments recorded at fair value is determined using financial models incorporating assumptions, judgements and estimates that may change over time or may ultimately not turn out to be accurate and the value realised by EBS for its assets may be materially different from the current or estimated fair value.**

Under IFRS, the EBS Group recognises at fair value: (i) derivative financial instruments; (ii) financial instruments at fair value through profit or loss; (iii) certain hedged financial assets and financial liabilities; and (iv) financial assets classified as available for sale ('AFS'). The best evidence of fair value is quoted prices in an active market. The absence of quoted prices due to the deterioration of the world's financial markets increases reliance on valuation techniques and requires the use of judgement in the estimation of fair value. This judgement includes but is not limited to: evaluating available market information; determining the cash flows for the instruments; identifying a risk free discount rate and applying an appropriate credit spread. Valuation techniques that rely to a greater extent on non-observable data require a higher level of management judgement to calculate fair value than those based on wholly observable credit spread.

The choice of contributors, the quality of market data used for pricing, and the valuation techniques used are all subject to internal review and approval procedures. Given the uncertainty and subjective nature of valuing financial instruments at fair value, any change in these variables could give rise to the financial instruments being carried at a different valuation, with a consequent impact on the shareholders' equity and, in the case of derivatives and contingent capital instruments, the statement of comprehensive income.

**8. EBS Group's deferred tax assets are substantially dependent on the generation of future profits over an extended number of years.**

The EBS Group's business performance may not reach the level assumed in the projections supporting the carrying value of the deferred tax assets. Lower than anticipated profitability within Ireland would lengthen the anticipated period over which the Group's Irish tax losses would be used. The value of the deferred tax assets relating to unused tax losses constitutes substantially all of the deferred tax assets recognised in the EBS Group's statement of financial position.

A significant reduction in anticipated profit, or changes in tax legislation, regulatory requirements, accounting standards or relevant practices, could adversely affect the basis for full recognition of the value of these losses, which would adversely affect the EBS Group's results and financial condition, including capital and future prospects.

New capital adequacy rules, consistent with Basel III principles, are within the EU Capital Requirements Regulation (part of the Capital Requirements Directive IV package). The new rules will, inter alia, require the EBS Group to deduct from its common equity capital, the value of most of the EBS Group's deferred tax assets, including all deferred tax assets arising from unused tax losses. The deduction from common equity capital is to be phased in evenly over 10 years.

## 5.3 Risks related to business operations, governance and internal control systems

**1. EBS Group is subject to inherent credit risks in respect of customers and counterparties which could adversely affect the Group's results, financial condition and future prospects.**

Risks arising from changes in credit quality and the recoverability of loans and other amounts due from customers and counterparties are inherent in a wide range of the EBS Group's businesses. In addition to the credit exposures arising from loans to individuals and Corporates, the Group also has an exposure to credit risk arising from loans to financial institutions, its trading portfolio, available-for-sale financial investments, derivatives and from off-balance sheet guarantees and commitments.

The EBS Group has been exposed to increased counterparty risk as a result of the risk of financial institution failures during the global economic crisis.

The Group is also exposed to credit risks relating to sovereign issuers. Concerns in respect of Ireland and other sovereign issuers, including other 'EU' Member States, have adversely affected and could continue to adversely affect the financial performance of the EBS Group.

# RISK MANAGEMENT REPORT (continued)

## 5.3 Risks related to business operations, governance and internal control systems (continued)

**2. EBS Group faces heightened operational risks.**
The EBS Group faces a heightened operational risk profile given the current economic environment and in the context of taking forward the significant organisational changes at EBS and AIB Group level, required to support the delivery of cost savings and the impact of an on-going organisational voluntary severance programme.

One of its key operational risks is people risk. The EBS Group's efforts to restore and sustain the stability of its business on a long-term basis depend, in part, on the availability of skilled management and the continued service of key members of staff both at its head office and at each of its business units.

Under the terms of the recapitalisation of the AIB Group by the Irish Government, the EBS Group is required to comply with certain executive pay and compensation arrangements. As a result of these restrictions, the EBS Group cannot guarantee that it will be able to attract, retain and remunerate highly skilled and qualified personnel in a highly competitive market. Failure by the EBS Group to staff its day-to-day operations appropriately or failure to attract and appropriately develop, motivate and retain highly skilled and qualified personnel could have an adverse effect on the EBS Group's results, financial condition and prospects.

Delivering the overall level of change has placed, and will continue to place, added risk on the organisation, including the challenge to meet tight delivery timelines in the face of competing priorities and resource demands. Negative public or industry opinion can result from the actual, or perceived, manner in which the EBS Group conducts its business activities or from the restructuring of the EBS Group. This could adversely affect the EBS Group's ability to keep and attract customers the loss of which would adversely affect the EBS Group's results, financial condition and prospects. Similarly, any weakness in the EBS Group's risk controls or loss mitigation actions in respect of operational risk could have a material adverse effect on the EBS Group's results, financial condition and operations.

**3. The Group's risk management strategies and techniques may be unsuccessful.**
The Group is exposed to a number of material risks. In order to minimise these risks, the Group has implemented a number of risk management strategies. Although the Group invests substantial time and effort in its risk management strategies and techniques, there is a risk that these may fail to fully mitigate the risks in some circumstances, particularly if confronted with risks that were not identified or anticipated.

Some of the Group's measures for managing risk are based upon observation of historical market behaviour. Where this is so, the Group applies statistical techniques to these observations to quantify its risk exposures. If circumstances arise that the Group in developing its models did not identify or anticipate, the losses could be greater than expected.

Furthermore, the Group's quantifications of risk do not take all risks into account. If the Group's measures to assess and mitigate risk prove insufficient, the Group may experience material unexpected losses.

**4. There is a risk of litigation arising from the EBS Group' business activities.**
The EBS Group operates in a legal and regulatory environment that exposes it to potentially significant litigation and regulatory risks. Disputes and legal proceedings in which the EBS Group may be involved are subject to many uncertainties, and their outcomes are often difficult to predict, particularly in the early stages of a case or investigation. Adverse regulatory action or adverse judgments in litigation could result in a monetary fine or penalty, adverse monetary judgement or settlement and/or restrictions or limitations on the EBS Group's operations or result in a material adverse effect on the EBS Group's reputation.

# RISK MANAGEMENT REPORT (continued)

## 6. Risk Disclosures

The EBS Group assumes a variety of risks in undertaking its business activities. Risk is defined as any event that could damage the core earnings capacity of the EBS Group, increase earnings or cash-flow volatility, reduce capital, threaten business reputation or viability, and/or breach regulatory or legal obligations. The EBS Group has adopted an Enterprise Risk Management approach to identifying, assessing and managing risks, the core elements of which are set out in a Board approved Enterprise Risk Management Framework.

The EBS Group categorises risks under a number of headings namely, business, credit, operational, regulatory compliance, people and culture, integration / managed services, commercial viability and financial (including capital, liquidity and market) risks. Together, these form the EBS Group's Risk Universe. This helps the EBS Group to assess and manage risk on an enterprise wide, holistic basis. The Risk Universe is regularly reviewed and updated reflecting the changing risk environment.

### 6.1 Business Risk

Business risk encompasses the internal and external factors that can impact on the Group's performance and comprises the EBS Group's values and beliefs, strategy and business planning risk, income and cost management risk, customer management framework risk, change management risk and modelling and scenario analysis risk change readiness, strategic plan management, remuneration, third party relationship management, brand management, distribution strategy, leadership and communication. Business risk also encompasses external trends which cannot be controlled but which could have a significant impact on the EBS Group's business such as the economic environment, market developments and technological innovation. Business risks are managed and monitored in the main by the senior management team and the Board. Significant developments are reported to the Board directly on a regular basis.

### 6.2 Operational Risk

Operational Risk is the risk arising from inadequate or failed internal processes, people and systems, or from external events. This category includes legal risk - the potential for loss arising from the uncertainty of legal proceedings and potential legal proceedings. It excludes financial crime and compliance risk which are covered in the Compliance Risk Framework. In essence, operational risk is a broad canvas of individual risk types which include information technology, business continuity, health and safety risks, and legal risk.

An overarching AIB Group Operational Risk Management ('ORM') framework is in place, designed to establish an effective and consistent approach to operational risk management across the enterprise. The AIB Group ORM framework is also supported by a range of specific policies addressing issues such as information security and business continuity management.

An important element of the AIB Group's ORM framework is the on-going monitoring through self-assessment of risks, control deficiencies and weaknesses, plus the tracking of incidents and loss events. Further actions are identified from the evaluation of losses and near misses which are recorded in each part of the organisation and monitored by the AIB Operational Risk function. These, and other actions arising from Internal Audit reviews, are monitored on an on-going basis and progress against actions is reported on a regular basis to the senior management team and the Board.

The role of Operational Risk is to review and coordinate operational risk management activities across the Group including setting policy and standards and promoting best practice disciplines augmented by an independent assurance process. Risk and Control Self-Assessment ('self-assessment') is a core process in the identification and assessment of operational risk across the AIB Group. The process serves to ensure that key operational risks are proactively identified, evaluated, monitored and reported, and that appropriate action is taken. This supports the business in identifying actions to improve the AIB Group's risk management capabilities.

### 6.3 Credit Risk Management

Credit risk management in the EBS Group is supported by an appropriate governance structure with separation of function between the sourcing and approval of business, the issuing of funds, loan management and independent review and monitoring.

# RISK MANAGEMENT REPORT (continued)

## 6.3 Credit Risk Management (continued)

Given the continued deterioration in credit quality throughout 2013 in the retail market, both credit management and credit risk management have continued to be a key area of focus during 2013. Resourcing, structures, policy and processes continue to be reviewed in order to ensure that the EBS is best placed to manage asset quality in this severe downturn.

The AIB Group ERC is responsible for reviewing appropriate credit risk management structures, forbearance strategies and policies in line with the credit risk appetite of the AIB Group and for monitoring the performance of the book.

The AIB Risk Analytics team is responsible for the development and on-going validation of credit risk rating models which are used to assess credit applications and to support a robust capital adequacy assessment process, and for independently monitoring the quality of the EBS loan assets.

The AIB Credit Review team assesses the application of credit policies, processes and procedures across all areas of the EBS Group.

The EBS Group in conjunction with AIB Group conducts both regular and ad-hoc credit risk stress testing to assess on an ongoing basis the ability of the Group to withstand various idiosyncratic and systemic stress scenarios. Credit contingency plans are developed and updated on a continual basis reflecting the results of the stress tests.

Given the economic environment, the AIB Group conducts a quarterly assessment of impairment provisions, assisted by the Risk Analytics and Credit divisions and evaluated by the AIB Group Credit Committee (‘GCC’).

**Credit risk on lending activities to customers and banks**

EBS Group lends to personal, retail customers and banks. Credit risk arises on the drawn amount of loans and advances, but also as a result of loan commitments, such as undrawn loans.

Credit risk also arises in EBS’ available-for-sale portfolio where counterparties are banks, sovereigns or structured debt. These credit risks are identified and managed in line with the credit management framework of the EBS Group.

**Country risk**

Credit risk is also influenced by country risk, where country risk is defined as the risk that circumstances arise in which customers and other counterparties within a given country may be unable to fulfil or are precluded from fulfilling their obligations to EBS Group due to economic or political circumstances.

Country risk is managed by setting appropriate maximum risk limits to reflect each country’s overall creditworthiness. These limits are informed by independent credit information from international sources. Risks and limits are monitored on an on going basis.

**Settlement risk**

Settlement risk arises in any situation where a payment in cash, securities or equities is made in the expectation of a corresponding receipt in cash, securities or equities. The settlement risk on many transactions is substantially mitigated when effected via assured payment systems, or on a delivery-versus-payment basis. Each counterparty is assessed in the credit process and clearing agents, correspondent banks and custodians are selected with a view to minimising settlement risk.

**Credit concentration risk**

Credit concentration risk arises where any single exposure or group of exposures, based on common risk characteristics, has the potential to produce losses large enough relative to EBS Group’s capital, total assets, earnings or overall risk level to threaten its health or ability to maintain its core operations.

**Risk identification and assessment**

All customer requests for credit are subject to a credit assessment process, which is exercised by an independent credit function.

# RISK MANAGEMENT REPORT (continued)

## 6.3 Credit Risk Management (continued)

**Risk identification and assessment (continued)**
Depending on the size and nature of the credit, the assessment process is assisted by standard application formats in order to assist the credit decision maker in making an informed credit decision. The credit approval authority is dependent on the size of the credit application and the grade of the borrower.

Another key tool used to assess credit risk is credit grading or credit scoring for each borrower or transaction both prior to approval of the credit exposure and subsequently. The methodology used produces a quantitative estimate of the likelihood of default for the borrower, typically referred to as a ‘grade’. This assessment is carried out at the individual borrower or transaction level.

In the retail book, which is characterised by a large number of customers with similar characteristics, risk assessment is largely informed through statistically-based scoring techniques. Mortgages are assessed centrally with particular reference to affordability and assisted by scoring models. Both application scoring for new customers and behavioural scoring for existing customers are used to assess and measure risk as well as to facilitate the management of these portfolios.

In the commercial property book (much diminished in size following deleveraging activity in 2012) the grading systems utilise a combination of objective information, essentially financial data and qualitative assessments of non-financial risk factors such as management quality and competitive position within its sector/industry.

Credit concentration risk is identified and assessed at single name counterparty level and at portfolio level. The EBS Board approved credit policies set the maximum limit by grade for exposures to individual counterparties or group of connected counterparties. Portfolio concentrations are identified and monitored by exposure and grade using internal sector codes.

Such measures facilitate the measurement of concentrations by balance sheet size and risk profile relative to other portfolios within EBS and in turn facilitate appropriate management action and decision making.

**Risk management and mitigation**
A framework of delegated authorities supports EBS Group’s management of credit risk. Credit approval is exercised by an independent credit function. Credit grading and scoring systems facilitate the early identification and management of any deterioration in loan quality.

Changes in the objective information (i.e. financial and business variables as described under risk identification and assessment) are reflected in the credit grade of the borrower with the resultant grade influencing the management of individual loans. Special attention is paid to lower quality graded loans or ‘Criticised’ loans. EBS has adopted the AIB Group definitions of grade quality, where criticised loans includes ‘Watch’ (Grade 8),’ Vulnerable’ (Grade 9), and ‘Impaired’ loans (Grade 10). These are defined as follows:

**Watch:** The credit is exhibiting weakness but with the expectation that existing debt can be fully repaid from normal cashflows.
**Vulnerable:** Credit where repayment is in jeopardy from normal cashflows and may be dependent on other sources.
**Impaired:** A loan is impaired if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the assets (a ‘loss event’) and that loss event (or events) has an impact such that the present value of future cash flows is less than the current carrying value of the financial asset or group of assets and requires an impairment provision to be recognised in the Income Statement.

EBS Group’s criticised advances are subject to more intense assessment and review, due to the increased risk associated with them.

# RISK MANAGEMENT REPORT (continued)

## 6.3 Credit Risk Management (continued)

**Risk management and mitigation (continued)**
The credit management process is underpinned by an independent system of credit review. Independent credit review teams assess the application of credit policies, processes and procedures across all areas of EBS. In 2012 EBS adopted AIB Group Credit Policies as a result credit policy and credit management standards are controlled and set centrally with input from EBS Group. Levels of concentrations by geography, sector and product are set through the Risk Appetite Statement which is required to be approved by the Board on an annual basis.

**Forbearance strategies**
EBS Group considers each request from customers who are experiencing cash flow difficulties on a case by case basis against the individual borrowers' current and likely future financial circumstances, their willingness to resolve these issues, as well as the legal and regulatory obligations.

EBS Group is implementing the standards as set out by the CBI in the Codes of Conduct in relation to customers in difficulty, ensuring these customers are dealt with in a professional and timely manner.

The types of forbearance solutions employed at AIB Group level for mortgage customers who are in difficulty and which provide short term relief include: interest only, part capital and interest, moratorium, capitalisation of arrears, term extension and deferred interest scheme. EBS Group has developed a Mortgage Arrears Resolution Strategy ('MARS') in line with AIB Group strategy for dealing with customers in difficulty or likely to be in difficulty.

The strategy is built on three key factors:
i) Segmentation – identifying customers in difficulty,
ii) Sustainability – customer assessment and
iii) Suitable Treatment – identifying solutions.

The core objective is to ensure that arrears solutions are sustainable in the long term for both the customer and for EBS Group and comply with the spirit and the letter of all regulatory requirements.

**Credit risk mitigants**
In relation to individual exposures, while the perceived strength of a borrower's repayment capacity is the primary factor in granting a loan, EBS Group uses various approaches to help mitigate risks relating to individual credits including: transaction structure, collateral and guarantees. Collateral or guarantees are required as a secondary source of repayment in the event of the borrower's default. The main types of collateral for loans and advances to customers are as follows:

- **Home mortgages:** EBS Group takes collateral in support of lending transactions for the purchase of residential property. There are clear policies in place which set out the type of property acceptable as collateral and the relationship of loan to property value. All properties are required to be fully insured and subject to a legal charge in favour of EBS Group.

- **Corporate/commercial lending:** EBS Group exited the commercial lending in 2008, however for property related lending that remains on EBS books, a charge over the property being financed is in place. This includes investment and residential properties. As part of the on going assessment of collateral, EBS Group uses an AIB Group Property Valuations standard. All EBS Group lending is property related lending.

EBS Group also has in place an interbank exposure policy which establishes the maximum exposure for each counterparty bank depending on credit grade. Each bank is assessed for the appropriate exposure limit within the policy.

**Risk monitoring and reporting**
Credit managers pro-actively manage EBS Group's credit risk exposures at transaction and relationship level. Credit risk at a portfolio level is monitored and reported regularly to senior management and the Board.

Single name counterparty concentrations are monitored at transaction level and managed within the Risk Appetite Statement. Large exposures and portfolio concentrations are reported regularly to senior management and the Board.

# RISK MANAGEMENT REPORT (continued)

### 6.4 Regulatory Compliance Risk

Regulatory Compliance Risk is the risk of legal or regulatory sanctions, material financial loss or loss to reputation which the EBS Group may suffer as a result of a failure to comply with the laws, regulations and self-regulatory codes which relate to the Group's regulated banking and financial services activities i.e. those activities which the EBS Group is licenced to conduct.

During 2012, the EBS Regulatory Compliance function integrated fully into the AIB Group Compliance function. Regulatory Compliance is an enterprise-wide function which operates independently of the business. The function is responsible for identifying compliance obligations arising in each of the Group's operating markets. Regulatory Compliance work closely with management in assessing compliance risks and provide advice and guidance on addressing these risks. Risk-based monitoring of compliance by the business with regulatory obligations is undertaken. The Regulatory Compliance function also promotes the embedding of an ethical framework to ensure that the Group operates with honesty, fairness and integrity. A Code of Business Ethics is in place for all staff alongside a Leadership Code for more senior staff. These are supported by a suite of policies.

New Board driven codes are being put in place to enhance and build on the existing codes. Regulatory Compliance report to the EBS Group ERC, business unit management teams and independently to the Board of Directors, through the Audit Committee, on the effectiveness of the processes established to ensure compliance with laws and regulations within its scope.

### 6.5 Liquidity Risk

Liquidity risk relates to the ability of the EBS Group to meet its' on and off balance sheet obligations in a timely manner as they fall due, without incurring excessive cost, whilst continuing to fund its assets and growth therein.

EBS Group is dependent, to a significant extent, on its parent, the AIB Group for funding and liquidity support and EBS's liquidity risk has been incorporated into the AIB p.l.c. centralised risk management model in line with AIB p.l.c. common approach to Treasury Risk management. Under this centralised approach the management of liquidity and related activities are overseen and controlled by AIB Treasury.

EBS Group applies the maturity mismatch approach to the management of liquidity following the adoption of this method by the CBI in July 2007. The overall purpose of a maturity mismatch approach is to ensure that the EBS Group will have, at any given time, a pool of highly liquid assets capable of being converted into cash within four business days, sufficient to cover a certain percentage of foreseeable cash outflows for future periods of time ('time bands'). Funding contingency plans are continually under review in light of unprecedented market and EBS Group specific events.

EBS Group conducts both regular and ad-hoc funding and liquidity risk stress testing to assess on an ongoing basis the ability of the EBS Group to withstand various idiosyncratic and systemic stress scenarios. Liquidity contingency plans are developed and updated on a continual basis reflecting the results of the stress tests. These activities are conducted in conjunction with AIB Group Asset & Liability Management.

Key measures used for managing liquidity risk are the liquidity ratios, calculated and reported on a daily basis internally to the Treasury Front Office and to AIB Group on a weekly basis for consolidation into the AIB Group Regulatory Liquidity Reports. They are also reported on a monthly basis to the EBS Management team and bi-monthly to the EBS Board. Any breaches of limits are escalated immediately in line with the escalation procedure.

EBS Limited was one of the Irish institutions included in the CIFS Scheme which ran from September 2008 to September 2010. EBS also joined the 'ELG' Scheme in early February 2010. EBS Limited continues to be one of the Irish covered institutions that are part of the 'ELG' Scheme. This scheme assisted EBS in attracting and maintaining customer funding in times of great economic uncertainty. The cost of the ELG scheme for 2013 was €47m (see note 2). On 26 February 2013, the Minister for Finance announced that the ELG 2009 will end for all new liabilities with effect from midnight on 28 March 2013. After this date, no new liabilities are guaranteed under the scheme.

# RISK MANAGEMENT REPORT (continued)

### 6.5 Liquidity Risk (continued)

AIB Group Treasury is responsible for the daily management of liquidity for EBS Group, supported by a dedicated EBS Treasury team, i.e. to ensure that resources are available at all times to meet EBS Groups' obligations arising from the daily business of the Bank. EBS Group reports its Liquidity positions to the CBI as part of the AIB Consolidated Liquidity Reporting.

The EBS Management team monitors these risks and reports on key developments to the EBS Limited Board on a regular basis via the Chief Risk Officers report.

Since October 2011, when the CBI revoked the requirement for EBS Group to comply with the 'Requirements for the Management of Liquidity Risk' regulatory document under Section 9.2 of that document. Where upon the EBS Liquidity Ratios would henceforth be reflected in the AIB Group Consolidated Liquidity Reports.

### 6.6 Market Risk

Market risk is the risk that changes in market prices, such as interest rate, foreign exchange rates and credit spreads (funding risk) will affect the EBS Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk. EBS is in the process of aligning the measurement methods and reporting of its market risk exposures to those employed by the AIB Group.

EBS Group does not engage in proprietary trading i.e. does not trade on its own account. EBS Group Treasury manages market risks using gap and sensitivity analysis in conjunction with AIB Group Treasury. Derivatives such as interest rate and foreign currency swap agreements and equity index options are used to hedge these market risks. The EBS Group Management team monitors these risks and reports on key developments to the Board on a regular basis via the CRO's report.

Interest rate risk in the banking book portfolio is the EBS Group's primary source of interest rate risk and is managed principally through monitoring interest rate gaps and by having various limits, processes and procedures. Interest rate risk in the reserve investment portfolio is managed under the Reserve Investment Policy as approved by the Board. In addition, EBS conducts regular Interest Rate Risk in the Banking Book ('IRRBB') stress testing to evaluate the exposure of the banking book portfolio and reserve investment portfolio to a parallel interest rate shift of 100 and 200 basis points and a series of yield curve twists. EBS Group has in place small operational foreign currency open position limits which are monitored on a daily basis.

### 6.7 Financial risks

EBS Group has exposure to the following risks from its use of financial instruments:

(i) Credit Risk
(ii) Liquidity risk
(iii) Market risk

This note presents information about EBS Group's exposure to each of the above risks and about EBS Group's objectives, policies and processes for measuring and managing risk.

# RISK MANAGEMENT REPORT (continued)

### 6.7.1 Credit exposure*

The following table sets out the maximum exposure to credit risk that arises within EBS and distinguishes between those assets that are carried in the Statement of Financial Position at amortised cost and those carried at fair value.

**Maximum exposure to credit risk***

The following table shows the Group's credit exposure, which is the maximum potential exposure including committed facilities:

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| *Non-derivative financial assets* | | | | |
| Cash and balances with Central Bank of Ireland | 73 | 8 | 74 | 8 |
| Available-for-sale financial assets | 3,009 | 4,545 | 217 | 1,568 |
| Loans and advances to credit institutions | 4,079 | 3,906 | 1,343 | 883 |
| Loans and advances to customers | 5,641 | 5,994 | 12,025 | 12,969 |
| NAMA senior bond | - | 305 | - | 305 |
| Items in transit | - | 24 | - | 26 |
| Interest accrued | 34 | 53 | 17 | 44 |
| Derivative financial instruments | 153 | 226 | 120 | 190 |
| Loan commitments (not unconditionally cancellable) | 107 | 80 | 147 | 104 |

The following table shows the fair value of collateral held for loans and advances to customers at 31 December 2013 and 2012:

**Group Collateral Held: Loans and Advances to Customers**

| | 2013 | | | 2012 | | |
|---|---|---|---|---|---|---|
| | Residential mortgages €m | Commercial mortgages €m | Total €m | Residential mortgages €m | Commercial mortgages €m | Total €m |
| **Impaired loans** | 2,551 | 113 | 2,664 | 2,230 | 100 | 2,330 |
| **Past due but not impaired** | 776 | 23 | 799 | 790 | 36 | 826 |
| **Non impaired / non past due** | 7,996 | 112 | 8,108 | 8,346 | 125 | 8,471 |
| **Total loans** | **11,323** | **248** | **11,571** | **11,366** | **261** | **11,627** |

**Company Collateral Held: Loans and Advances to Customers**

| | 2013 | | | 2012 | | |
|---|---|---|---|---|---|---|
| | Residential mortgages €m | Commercial mortgages €m | Total €m | Residential mortgages €m | Commercial mortgages €m | Total €m |
| **Impaired loans** | 1,388 | 113 | 1,501 | 1,267 | 100 | 1,367 |
| **Past due but not impaired** | 294 | 23 | 317 | 302 | 36 | 338 |
| **Non impaired / non past due** | 3,032 | 112 | 3,144 | 3,097 | 125 | 3,222 |
| **Total loans** | **4,714** | **248** | **4,962** | **4,666** | **261** | **4,927** |



*Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

### 6.7.1 Credit exposure (continued) *

**Residential mortgages**
While EBS considers a borrower's repayment capacity to be paramount in granting any loan, EBS also takes collateral in support of lending transactions for the purchase of residential property. There are clear policies in place which set out the type of property which is acceptable as collateral and the loan to property value relationship. Collateral valuations are required at the time of origination of each residential mortgage. The fair value at December 2013 of residential mortgages is based on the property values at origination and applying the CSO (Ireland) index to these values to take account of price movements in the interim. The collateral values above include all loans regardless of balances outstanding. Additional information in relation to Loan to Value ('LTV') and Days Past Due ('DPD') profiles for residential mortgages is noted below.

**Commercial property**
EBS has not issued new commercial property lending since 2008, except for the purpose of loss mitigation. The fair value at December 2013 of commercial mortgages is based on the property values at origination and applying the CSO (Ireland) index to these values to take account of price movements in the interim or valuation based on AIB Group property valuation guidelines.

**Measurement of credit risk**
One of the objectives of credit risk management is to accurately quantify the level of credit risk to which the Group is exposed. The use of internal credit rating models is fundamental in assessing the credit quality of loan exposures.

The primary model measures used are:
– Probability of default ('PD') – the likelihood that a borrower is unable to repay his obligations;
– Exposure at default ('EAD') – the exposure to a borrower who is unable to repay his obligations at the point of default; and
– Loss given default ('LGD') – the loss associated with a defaulted loan or borrower.

To calculate PD, the Group assesses the credit quality of borrowers and other counterparties and assigns a credit grade or score to these. This grading is fundamental to credit sanctioning and approval, and to the on-going credit risk management of loan portfolios. It is a key factor in determining whether credit exposure limits are sanctioned for new borrowers and how any existing limits are managed for current borrowers.

The ratings methodology and criteria used in assigning borrowers to grades vary across the models used for the portfolios, but models generally use a combination of statistical analysis (using both financial and non-financial inputs) and expert judgement.

For the purposes of calculating credit risk, each probability of default model segments counterparties into a number of rating grades, each representing a defined range of default probabilities (details of these rating scales are published in the Group's Pillar 3 disclosures). Exposures migrate between rating grades if the assessment of the counterparty probability of default changes. These individual rating models continue to be refined and recalibrated based on experience.

The calculation of internal ratings differs between portfolios. In the retail portfolio, which is characterised by a large number of customers with small individual exposures, risk assessment and decisioning is largely automated through the use of statistically-based scoring models. All counterparties are assessed using the appropriate model or scorecard prior to credit approval.

Mortgage applications are generally assessed centrally with particular reference to affordability, assisted by scoring models. Both application scoring for new customers and behavioural scoring for existing customers are used to assess and measure risk as well as to facilitate the management of these portfolios.

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# RISK MANAGEMENT REPORT (continued)

## 6.7.1 Credit exposure (continued)*

**Measurement of credit risk (continued)**
Credit grading and scoring systems facilitate the early identification and management of any deterioration in loan quality. Changes in the objective information are reflected in the credit grade of the borrower with the resultant grade influencing the management of individual loans. Special attention is paid to lower quality performing loans or 'criticised' loans. In AIB Group, criticised loans include 'watch', 'vulnerable' and 'impaired' loans which are defined as follows:

**Watch:** 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 dependent on other sources; and
**Impaired:** A loan is impaired if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event/events has an impact such that the present value of future cash flows is less than the current carrying value of the financial asset or group of assets and requires an impairment provision to be recognised in the Income Statement.

The Group's criticised loans are subject to more intense assessment and review because of the increased risk associated with them. Given the on-going deterioration in credit quality throughout 2012 and 2013 in the residential, retail and commercial markets, credit management and credit risk management continued to be the key area of focus. Resourcing, structures, policy and processes are subjected to on-going review in order to ensure that the Group is best placed to manage asset quality and assist borrowers in line with agreed treatment strategies.

**Provisioning for impairment**
The accounting policies of loans and advances to customers are outlined in the Accounting Policies section. A loan or portfolio of loans is impaired and an impairment loss is incurred if there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of an asset or group of assets**.**

Objective evidence can include both:
•Micro conditions – for example a breach in the repayment contract, i.e. arrears on the account, and
•Macro conditions – for example an adverse change in economic conditions.

An impairment loss event is an event which has an impact on the expected cash flows of the asset. Where the event has been incurred and has been identified, an individual provision is required. Where the loss has been incurred but has not yet been identified, an IBNR (portfolios of performing loans are assessed on a collective basis to estimate the amount of losses incurred, but which have yet to be individually identified) provision is required.

Provisions are calculated for assets which are deemed to be impaired where there is objective evidence of impairment. If the asset is deemed to be significant, then it is reviewed on an individual basis. Where the asset is impaired, but not significant, it is reviewed on a pooled or IBNR basis. Provisions are also calculated for individual assets where there is no objective evidence of individual impairment yet, but where impairment has been incurred. In this way, all assets are reviewed.

For Residential Loan Assets, EBS assesses loans for impairment where; loans which are €0.01 or more in arrears and where the arrears is not of a technical nature, or where there is other evidence of impairment, for example, where a customer makes a request for advanced forbearance. Categories of loans that will be classed as impaired regardless of arrears include: loans where the property is in possession of EBS and loans where fraudulent activity is suspected. 2013 saw the implementation of a new provisioning model for the Individually Insignificant loans (i.e. <=500k in balance). This model calculates provisions both for impaired assets (specific provisions classified as II) and non-impaired assets (collective pool classified as IBNR).

For Commercial Loan Assets, EBS assesses for impairment loans which have an internal credit grading of 7, 8 or 9 (i.e. they are on a watch list, are in default or are already holding a provision).



*Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

### 6.7.1 Credit exposure (continued)*

**Provisioning for impairment (continued)**

For Treasury Assets (counterparty credits) EBS defines impairment as, credits where there is a failure to make a scheduled payment within five working days, or credits which are impacted by a major credit event such as something which has gone from investment to sub-investment grade for investments of more than three months in duration.

Significant assets in EBS are defined as assets with an overall current value of more than €1.5m. This applies to non-retail loan and treasury assets: the threshold for Retail assets is set at €0.5m. Assets which are impaired and which are significant are reviewed on an individual case basis.

The loan value threshold is not applied to loans:
- where the property is in possession of the Group; or
- where fraudulent activity is suspected or proven.

All such loans are also assessed individually for provision.

All loans greater than 90 days past due are deemed impaired, regardless of significance.

**Collective Provisions**

All loans where the individual provision is zero, whether or not an individual assessment is completed, are part of the collective (impairment assessment on a collective basis for portfolios of loans that are not considered individually significant for specific provisions) provision calculation. A driving factor of the collective provision calculation is the emergence period. This has been increased from 6 to 9 months because new data is available, increasing the collective provisions as a consequence.

The calculation has two key components reflecting the stages in the movement of a loan to loss: probability of default ('PD'); and loss given default ('LGD').

Default is defined to be 3 (monthly) payments or more in arrears, i.e., at least 90 days past due. If a loan is already in default then its PD is 1, otherwise it is a number between 0 and 1 measuring the likelihood of the loan moving into default in the coming 12 months. The rate of default is adjusted to take into account expected movements in external macroeconomic factors (such as employment and GNP).

The rate of movement from default to repossession is assessed according to the number of payments missed – the deeper in default a loan is, the more likely it is that a loss will result. It also varies widely across the portfolios, being much higher for commercial lending.

The calculation of incurred loss is driven largely by expectation of property values at disposal. In this note, impaired assets are those for which an individual provision has been made.

**Retail mortgages**

Individually insignificant mortgage specific provisions are calculated using a collective mortgage provisioning model. This methodology is based on the calculation of three possible resolution outcomes: cure; advanced forbearance with loss; and repossession (forced and voluntary), with different loss rates associated with each. This replaces the existing two outcomes, repossession and cure. The methodology has been updated to reflect current data on loss history and portfolio development as well as incorporating additional loss parameters assessed on restructuring outcomes.

The model parameters at 31 December 2013 for owner occupier mortgages are as follows: cure (4%); and repossession/advanced forbearance (96%).

The corresponding buy-to-let model parameters are as follows: cure (1%); and repossession/advanced forbearance (99%).

**Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

### 6.7.1 Credit exposure (continued)*

**Retail mortgages (continued)**
Cured loans are loans that were impaired but are no longer impaired and have performed satisfactorily for 12 months excluding any impact from forbearance.

The modelled loss is calculated case by case by subtracting the net present value of the modelled recovery amount from the current loan balance. The model parameters are determined from observed data where possible. Where not directly observable, related measures are used to infer the parameter where possible; otherwise it is based on expert judgement. The relevant model parameters include: % of forced disposals; costs and time to dispose (voluntary and forced); peak to trough price decline, loss rate on advanced forbearance; and haircut on sale (voluntary and forced).

The model parameters are reviewed at the Group Credit Committee on a quarterly basis.

All loans where the specific provision is zero, whether or not an individual assessment is completed, are part of the collective provision calculation. These are termed the incurred but not reported (IBNR) provisions.

Individually assessed loans for which no evidence of loss has been specifically identified on an individual basis are grouped together according to their credit risk characteristics for the purpose of calculating an estimated collective loss. This reflects impairment losses that Group has incurred as a result of events occurring before the balance sheet date, which the Group is not able to identify on an individual loan basis, and that can be reliably estimated. These losses will only be individually identified in the future. As soon as information becomes available which identifies losses on individual loans within the group, those loans are removed from the group and assessed on an individual basis for impairment.

IBNR provisions can only be recognised for incurred losses i.e. losses that are present in the portfolio at the reporting date and are not permitted for losses that are expected to happen as a result of likely future events. IBNR provisions are determined by reference to loss experience in the portfolio and to the credit environment at the reporting date. IBNR provisions are maintained at levels that are deemed appropriate by management having considered and having taken into account:
– historical loss experience in portfolios of similar credit risk characteristics (for example, by sector, loan grade or product);
– the estimated period between impairment occurring and the loss being identified and evidenced by the establishment of an appropriate provision against the individual loan (emergence period);
– management’s experienced judgement as to whether current economic and credit conditions are such that the actual level of inherent losses at the balance sheet date is likely to be greater or less than that suggested by historical experience; and
– an assessment of higher risk portfolios, which include but are not limited to: non-impaired forborne mortgages; loans graded with a vulnerable credit rating; and loans > 90 days past due but not impaired.

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# RISK MANAGEMENT REPORT (continued)

### 6.7.1 Credit exposure (continued)*

**IBNR for mortgages portfolio (unaudited)**
The portfolio IBNR is calculated using the collective mortgage model as described above. The table below sets out the parameters used in the calculation of IBNR for the mortgage portfolio:

**Group**

| Grade | Average PD (%) | Average LGD (%) |
|---|---|---|
| Good Upper | 1.7 | 19.1 |
| Good Lower | 6.3 | 23.9 |
| Watch | 17.3 | 21.5 |
| Vulnerable | 50.2 | 22.2 |

| | Average PD (%) | Average LGD (%) |
|---|---|---|
| Performing | 6.8 | 20.5 |
| Non-performing non-impaired | 84.3 | 23.2 |

The parameters for Cured and Forborne – non-impaired, are set out below. As a result, these sub portfolios carry a higher level of IBNR:

| | | |
|---|---|---|
| Cured | 24.2 | 21.7 |

| | | |
|---|---|---|
| Forborne Not Impaired | 18.4 | 21.7 |

**Company**

| Grade | Average PD (%) | Average LGD (%) |
|---|---|---|
| Good Upper | 1.1 | 19.4 |
| Good Lower | 4.6 | 24.6 |
| Watch | 17.8 | 21.8 |
| Vulnerable | 66.7 | 23.3 |

| | Average PD (%) | Average LGD (%) |
|---|---|---|
| Performing | 6.1 | 20.6 |
| Non-performing non-impaired | 87.7 | 23.2 |

The parameters for Cured and Forborne – non-impaired, are set out below. As a result, these sub portfolios carry a higher level of IBNR:

| | | |
|---|---|---|
| Cured | 23.5 | 22.9 |

| | | |
|---|---|---|
| Forborne Not Impaired | 19.7 | 22.1 |

Average PD and LGD are based on the PDs and LGDs weighted by exposure for all owner-occupier and buy-to-let loans included in the collective mortgage model. The mortgage provision model calculates individually insignificant specific provisions and IBNR run rate provisions. Any additional IBNR as determined by management judgement is applied at a portfolio level and is not included in the analysis above. Non-performing, non-impaired loans in the table above, are defined as loans that are more than 90 days past due but not impaired.

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# RISK MANAGEMENT REPORT (continued)

### 6.7.1 Credit exposure (continued)*

**Emergence period**

The emergence period is key to determining the level of IBNR provisions. Emergence periods are determined by assessing the time it takes following a loss event for an unidentified impaired loan to be recognised as an impaired loan requiring a provision. Emergence periods for each portfolio are determined by taking into account current credit management practices, historic evidence of assets moving from ‘good’ to ‘bad’ and actual case studies.

Non-impaired provisions assets are split into homogenous pools on the basis of similar risk characteristics. The asset pools are multiplied by the ‘average annual loss rate’ for that pool, suitably adjusted where appropriate for any factors currently affecting the portfolio, which may not have been a feature in the past or vice versa. The resultant amount is then multiplied by the ‘Emergence Period’ for that pool to arrive at the IBNR Collective Impairment Provision. Loss rates are updated half yearly and emergence periods for each pool of loans are reviewed annually.

For the year ended 31 December 2013, the emergence period for the residential mortgage portfolio has moved from 6 months to 9 months resulting in an additional provision of € 35 million. The increase has been observed as more historical data has become available, particularly for the forbearance portfolio and customer behaviour has been observed over a longer period of time.

**Impairment Sensitivities for 2013**

Management is required to exercise judgement in making assumptions and estimations when calculating loan impairment provisions on both individually and collectively assessed loans and receivables. The most significant judgemental area is the calculation of collective impairment provisions. They are subject to estimation uncertainty, in part because of the large number of individually insignificant loans in the portfolio.

The methods involve the use of historical information which is supplemented with significant management judgement to assess whether current economic and credit conditions are such that the actual level of inherent losses is likely to be greater or less than that suggested by historical experience. In normal circumstances, historical experience provides the most objective and relevant information from which to assess inherent loss within each portfolio, though sometimes it provides less relevant information about the inherent loss in a given portfolio at the balance sheet date, for example, when there have been changes in economic, regulatory or behavioural conditions which result in the most recent trends in portfolio risk factors not being fully reflected in the statistical models. In these circumstances, the risk factors are taken into account by adjusting the impairment provisions derived solely from historical loss experience.

Risk factors include loan portfolio growth, product mix, unemployment rates, bankruptcy trends, geographical concentrations, loan product features, economic conditions such as national and local trends in housing markets, the level of interest rates, portfolio seasoning, account management policies and practices, changes in laws and regulations, and other influences on customer payment patterns. The methodology and the assumptions used in calculating impairment losses are reviewed regularly in the light of differences between loss estimates and actual loss experience. For example loss rates and the expected timing of future recoveries are benchmarked against actual outcomes where available to ensure they remain appropriate.

However, the exercise of judgement requires the use of assumptions which are highly subjective and very sensitive to the risk factors, in particular to changes in economic and credit conditions across a large number of geographical areas.

The key variables include peak to trough house price (which determines the collateral value supporting loans in the mortgage portfolio) and cure rates (rates by which defaulted or delinquent accounts are assumed to return to performing status).

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## RISK MANAGEMENT REPORT (continued)

### 6.7.1 Credit exposure (continued)*

**Impairment Sensitivities for 2013 (continued)**
Altering the key assumptions for provisions has varying impacts on the overall provision numbers. The following table shows the relative impacts of standardised changes.

| Factor 2013 | |
|---|---|
| 1. Probability of Default: Emergence Period | - Increasing the emergence period from 9 to 12 months would increase the IBNR (collective provision) by 37.0% for Home loans. |
| 2. Probability of Default: Cure Rate | - A 1% increase in cure rate would decrease the specific provision by 1.2% and the collective provision by 4.6% for Home loans. |
| 3. Roll rate from default to repossession : Higher roll rates assumed | - A 1% increase in repossession rate would increase the specific provision by 0.4% for Home loans. |
| 4. Loss Given repossession: Higher reductions in house prices from peak | - An increased Peak-to-Trough assumption (from 55% to 57%) would increase the specific provision by 3.9% and collective provision by 3.4% for Home loans. |

| Factor 2012 | |
|---|---|
| 1. Probability of Default: Interest Rate changes | - A 1% increase in Standard Variable Rate leads to a 0.5% increase in collective provisions for Home loans. |
| 2. Probability of Default: Macroeconomic factors | - A 2% fall in employment leads to a 0.8% increase in collective provisions for Retail assets (Home loans and Buy-to-Lets)<br>The GDP and GNP numbers alone have little influence |
| 3. Roll rate from default to repossession: Higher roll rates assumed | - An increase in 4% of the repossession rate will result in a 7.3% movement in stock of provisions. |
| 4. Loss Given repossession: Higher reductions in house prices from peak | - An increased peak to trough assumption (changing to 58% from 55%) increases collective provisions by 9.2%. |

The 2012 impairments sensitivities are based on the 2012 Retail II Mortgage Model. The model was updated in 2013. These figures are unaudited.

Credit risk can also be affected by macro-economic factors such as increased interest rates, increased unemployment, lower consumer spending, personal and corporate defaults/insolvency levels. The credit portfolio is also subjected to on-going stress testing and scenario analysis. Events are modelled at a Group wide level, at a segment and business unit level, and by rating model and portfolio.

Sensitivity analysis is the simple stressing of one risk driver to assess the Group's sensitivity to that risk driver. A risk driver is defined as an internal or external factor which has the potential to cause loss or damage to the Group e.g. macroeconomic risk drivers (GDP, unemployment rate etc.) and specific credit risk drivers (shift in PDs).

### 6.7.2 Credit Profile

**Credit quality**
The following table includes total EBS Group loans and advances to customers' gross of impairment provisions split on a core/non-core basis. Core includes home loans and non-core includes buy-to-let ('BTL') and commercial loans. The numbers presented are inclusive of unearned income and related provisions and deferred acquisition costs.

# RISK MANAGEMENT REPORT (continued)

## 6.7.2 Credit Profile (continued)*

### Credit quality (continued)

| Group | 2013 | | | 2012 | | |
|---|---|---|---|---|---|---|
| | Core | Non-Core | Total | Core | Non-Core | Total |
| **Loans and advances to customers** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** |
| Residential mortgages | 12,541 | 575 | 13,116 | 13,017 | 608 | 13,625 |
| Commercial property | - | 261 | 261 | - | 278 | 278 |
| **Total** | **12,541** | **836** | **13,377** | **13,017** | **886** | **13,903** |

In the Core portfolio, the Residential mortgages further declined during 2013 due to weaker customer demand and as a result of loan repayments.

Asset quality in the Group has been affected by an increase in the level of arrears, with 63.5% of the combined loan book maintaining a satisfactory payment profile in 2013 compared with 66.7% for 2012. The change in loan quality is reflected in a higher level of provisions, detailed below.

| Company | 2013 | | | 2012 | | |
|---|---|---|---|---|---|---|
| | Core | Non-Core | Total | Core | Non-Core | Total |
| **Loans and advances to customers** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** |
| Residential mortgages | 5,004 | 467 | 5,471 | 5,125 | 500 | 5,625 |
| Commercial property | - | 261 | 261 | - | 278 | 278 |
| **Total** | **5,004** | **728** | **5,732** | **5,125** | **778** | **5,903** |

Asset quality in the Company has been affected by an increase in the level of arrears, with 55.9% of the combined loan book maintaining a satisfactory payment profile in 2013 compared with 58.6% for 2012. The change in loan quality is reflected in a higher level of provisions, detailed below.

| | 2013 | | | 2012 | | |
|---|---|---|---|---|---|---|
| **Group Impairment Provisions** | **Core** | **Non-Core** | **Total** | **Core** | **Non-Core** | **Total** |
| | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** |
| Statement of financial position provisions | 1,094 | 258 | 1,352 | 715 | 219 | 934 |
| Statement of financial position provisions as a % of loans and advances | 8.7% | 30.9% | 10.1% | 5.5% | 24.7% | 6.7% |
| Specific provision as a % of impaired loans | 31.0% | 37.7% | 32.0% | 22.0% | 37.0% | 23.8% |
| Impairment charge as a % of total loans | 3.0% | 4.5% | 3.0% | 1.8% | (0.9%) | 1.3% |

Group loans and advances to customers amounted to €13,377m (2012: €13,903m) at 31 December 2013 and have decreased by €526m since December 2012 largely as a result of a weak customer demand. 36.5% or €4,885m of total Group loans and advances to customers are criticised of which €3,339m or 25% of total loans are impaired.

Statement of Financial Position impairment provisions of €1,352m (2012: €934m) provide cover on impaired loans of 40.5% and on total loans of 10.1%.

The 2013 consolidated Income Statement impairment provisions charge, including the Mortgage Indemnity Guarantee (‘MIG’) benefit of €20m (2012: €13m) amounts to €418m (2012: €229m) or 3.1% (2012: 1.6%) of the year end balances.

There were several changes implemented in 2013 which are driving the coverage rates up. Losses are now assumed to occur for loans not likely to go to repossession.

**Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

## 6.7.2 Credit Profile (continued)*

### Credit quality (continued)

In addition, parameter selection for the model has been influenced strongly by the feedback received from the CBI following the Balance Sheet Assessment in Q4 2013. The EBS Group impairment provision charge excluding MIG benefit for 2013 is €15m or 5.7% for borrowers in the Commercial property sector and €403m or 3.1% for Residential Mortgages.

The EBS Group impairment provision for 2013 is €80m or 30.7% for borrowers in the Commercial property sector, and €1,272m or 9.7% for Residential mortgages.

| | 2013 | | | 2012 | | |
|---|---|---|---|---|---|---|
| **Company Impairment Provisions** | **Core** | **Non-Core** | **Total** | **Core** | **Non-Core** | **Total** |
| | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** |
| Statement of financial position provisions | 585 | 230 | 815 | 386 | 196 | 582 |
| Statement of financial position provisions as a % of loans and advances | 11.7% | 31.6% | 14.2% | 7.5% | 25.2% | 9.9% |
| Specific provision as a % of impaired loans | 32.6% | 37.5% | 33.7% | 22.3% | 35.0% | 24.6% |
| Impairment charge as a % of total loans | 4.0% | 4.8% | 4.1% | 2.6% | (1.9%) | 2.0% |

Company loans and advances to customers amounted to €5,732m at 31 December 2013 and have decreased by €171m since December 2012 due to loan repayments and weak customer demand. 44.1% or €2,526m of total Company loans and advances to customers are criticised of which €1,850m or 32.3% of total loans are impaired.

Statement of Financial Position provisions of €815m provide cover on impaired loans of 44.1% and on total loans of 14.2%.

The 2013 income statement provision charge, net of the MIG benefit of €11m amounts to €222m (2012: €117m) or 4.0% (2012: 2.0%) of year end balances.

The Company impairment provision for 2013 is €80m or 30.7% for borrowers in the Commercial Property sector and €735m or 13.4% for residential mortgages.

### Residential mortgages

Residential mortgages amounted to €13,116m at 31 December 2013. This compares to €13,625m at 31 December 2012, with the decrease as a result of loan repayments and weak customer demand. The split of the residential mortgage book was owner-occupier, €12,541m and buy-to-let, €575m. The consolidated income statement impairment provision charge for 2013 was €403m or 3.1% for Residential mortgages. The statement of financial position impairment provisions of €1,272m were held at 31 December 2013, split €1,037m specific and €235m collective.

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# RISK MANAGEMENT REPORT (continued)

### 6.7.2 Credit Profile (continued)*

**Residential mortgages (continued)**

| **Group** | **2013** | | | **2012** | | |
|---|---|---|---|---|---|---|
| **Residential mortgage – Total** | **Owner-occupier (Core) (1) €m** | **Buy-to-let (Non-Core) €m** | **Total €m** | **Owner-occupier (Core) (1) €m** | **Buy-to-let (Non-Core) €m** | **Total €m** |
| **Mortgage Book** | | | | | | |
| Total Residential Mortgages | 12,541 | 575 | 13,116 | 13,017 | 608 | 13,625 |
| Not Past due and not in arrears | 8,773 | 213 | 8,986 | 9,514 | 237 | 9,751 |
| **Arrears** | | | | | | |
| 1 - 30 days past due but not impaired | 496 | 7 | 503 | 568 | 15 | 583 |
| 31 - 60 days past due but not impaired | 207 | 5 | 212 | 213 | 6 | 219 |
| 61 - 90 days past due but not impaired | 143 | 4 | 147 | 116 | 4 | 120 |
| 91 - 180 days past due but not impaired | 46 | 1 | 47 | 42 | 2 | 44 |
| 181 - 365 days past due but not impaired | 1 | - | 1 | - | 1 | 1 |
| Over 365 days past due but not impaired | - | 3 | 3 | 1 | 2 | 3 |
| **Impaired Loans** | | | | | | |
| Impaired Loans | *2,875* | *342* | *3,217* | *2,563* | *341* | *2,904* |
| of which impaired and not in arrears | 207 | 98 | 305 | 199 | 104 | 303 |
| of which impaired and in arrears | *2,668* | *244* | *2,912* | *2,364* | *237* | *2,601* |
| - of which 1 - 30 days past due | 76 | 14 | 90 | 74 | 17 | 91 |
| - of which 31 - 60 days past due | 55 | 5 | 60 | 65 | 11 | 76 |
| - of which 61 - 90 days past due | 71 | 13 | 84 | 74 | 12 | 86 |
| - of which 91 - 180 days past due | 359 | 23 | 382 | 367 | 17 | 384 |
| - of which 181 - 365 days past due | 536 | 39 | 575 | 551 | 38 | 589 |
| - of which over 365 days past due | 1,571 | 150 | 1,721 | 1,233 | 142 | 1,375 |
| Total Arrears (30+ days past due and/or impaired) | 3,272 | 355 | 3,627 | 2,935 | 356 | 3,291 |
| 90+ DPD Arrears (90+ days past due and/or impaired) | 2,922 | 346 | 3,268 | 2,606 | 346 | 2,952 |
| **Provisioning** | | | | | | |
| Statement of financial position specific provisions | 892 | 145 | 1,037 | 563 | 126 | 689 |
| Statement of financial position IBNR provisions | 202 | 33 | 235 | 152 | 28 | 180 |
| Income statement specific provisions YTD | 330 | 18 | 348 | 143 | 30 | 173 |
| Income statement specific IBNR provisions YTD | 50 | 5 | 55 | 94 | (25) | 69 |
| Specific provisions / impaired loans cover | | | **32.2%** | | | **23.7%** |

(1) The Owner Occupier category represents the Core portfolio.

The portfolio has experienced an increase in arrears. This is due to the harsh economic climate of the last few years. Even though 2013 has seen an improvement in the overall economy, it is likely that this will not impact on borrowers' repayment affordability until 2014 and later. The level of loans >90 days in arrears or impaired was 24.9% (of total residential mortgages) at 31 December 2013 compared with 21.7% at 31 December 2012.

The level of loans >90 days in arrears or impaired in the owner occupier book has increased significantly since 31 December 2012 from €2,606m (20.0% of mortgages) to €2,922m or 23.3% at 31 December 2013.

# RISK MANAGEMENT REPORT (continued)

## 6.7.2 Credit Profile (continued)*

### Residential mortgages (continued)

Unemployment, wage cuts and high levels of personal debt continued to be the principal drivers of increased arrears.

The level of loans >90 days in arrears or impaired in the Buy-to-Let ('BTL') portfolio has moved from €346m or 56.9% at 31 December 2012 to €347m or 60.3% at 31 December 2013.

Total owner occupier and BTL impaired loans were €3,217m at 31 December 2013. Total specific provisions of €1,037m provided cover of 32.2% of impaired loans and have been raised having assessed the peak to trough fall in house prices in Ireland (55.0%). Statement of financial position IBNR provisions of €235m are held for the non-impaired book (75.5% of residential mortgage book) based on management's view of incurred loss in this book. The total income statement charge for 2012 was €403m (specific €347m and collective €56m).

| **Company** | **2013** | | | **2012** | | |
|---|---|---|---|---|---|---|
| **Residential mortgage – Total** | **Owner-occupier (Core) (1) €m** | **Buy-to-let (Non-Core) €m** | **Total €m** | **Owner-occupier (Core) (1) €m** | **Buy-to-let (Non-Core) €m** | **Total €m** |
| **Mortgage Book** | | | | | | |
| Total Residential Mortgages | 5,004 | 467 | 5,471 | 5,125 | 500 | 5,625 |
| Not Past due and not in arrears | 3,245 | 155 | 3,400 | 3,451 | 177 | 3,628 |
| **Arrears** | | | | | | |
| 1 - 30 days past due but not impaired | 180 | 6 | 186 | 208 | 13 | 221 |
| 31 - 60 days past due but not impaired | 78 | 4 | 82 | 76 | 5 | 81 |
| 61 - 90 days past due but not impaired | 53 | 4 | 57 | 43 | 3 | 46 |
| 91 - 180 days past due but not impaired | 14 | 1 | 15 | 14 | 2 | 16 |
| 181 - 365 days past due but not impaired | - | - | - | - | 1 | 1 |
| Over 365 days past due but not impaired | - | 3 | 3 | 1 | 2 | 3 |
| **Impaired Loans** | | | | | | |
| Impaired Loans | 1,434 | 294 | 1,728 | 1,331 | 298 | 1,629 |
| of which impaired and not in arrears | 82 | 90 | 172 | 67 | 90 | 157 |
| of which impaired and in arrears | 1,352 | 204 | 1,556 | 1,264 | 208 | 1,472 |
| - of which 1 - 30 days past due | 36 | 13 | 49 | 33 | 17 | 50 |
| - of which 31 - 60 days past due | 24 | 4 | 28 | 28 | 10 | 38 |
| - of which 61 - 90 days past due | 24 | 10 | 34 | 29 | 10 | 39 |
| - of which 91 - 180 days past due | 134 | 17 | 151 | 156 | 13 | 169 |
| - of which 181 - 365 days past due | 229 | 31 | 260 | 260 | 29 | 289 |
| - of which over 365 days past due | 905 | 129 | 1,034 | 758 | 129 | 887 |
| Total Arrears (30+ days past due and/or impaired) | 1,579 | 306 | 1,885 | 1,465 | 311 | 1,776 |
| 90+ days past due Arrears (90+ days past due and/or impaired) | 1,448 | 298 | 1,746 | 1,346 | 303 | 1,649 |
| **Provisioning** | | | | | | |
| Statement of financial position specific provisions | 467 | 126 | 593 | 296 | 104 | 400 |
| Statement of financial position IBNR provisions | 118 | 24 | 142 | 90 | 27 | 117 |
| Income statement specific provisions YTD | 170 | 22 | 192 | 87 | 26 | 113 |
| Income statement specific IBNR provisions YTD | 28 | (2) | 26 | 47 | (28) | 19 |
| Specific provisions / impaired loans cover | | | **34.3%** | | | 24.6% |

(1) The Owner Occupier category represents the Core portfolio.

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# RISK MANAGEMENT REPORT (continued)

### 6.7.2 Credit Profile (continued)*

**Residential mortgages (continued)**
Residential mortgages amounted to €5,471m at 31 December 2013. This compares to €5,625m at 31 December 2012, with the decrease as a result of loan repayments and weak customer demand. The split of the residential mortgage book was owner-occupier €5,004m and buy-to-let €467m. The income statement impairment charge for 2013 was €218m or 4.0% for Residential mortgages. Statement of Financial Position provisions of €735m were held at 31 December 2013, split €593m specific and €142m for collective.

The portfolio has experienced an increase in arrears reflecting the impact of a harsher economic climate on borrowers' repayment affordability over the past few years. The level of loans >90 days in arrears or impaired was 31.9% at 31 December 2013 compared with 29.3% at 31 December 2012.

The level of loans >90 days in arrears or impaired in the owner occupier book has increased since 31 December 2012 from €1,346m (26.3% of mortgages) to €1,448m or 28.9% at 31 December 2013. Unemployment, wage cuts and high levels of personal debt continued to be the principal drivers of increased arrears.

The level of loans >90 days in arrears or impaired in the non-core portfolio has moved from €303m or 60.6% at 31 December 2012 to €299m or 64.0% at 31 December 2013.

Total owner occupier and BTL impaired loans were €1,728m at 31 December 2013. Total specific provisions of €593m provided cover of 34.3% of impaired loans and have been raised having assessed the peak to trough fall in house prices in Ireland (55%). Coverage rates on impaired loans have increased as a result of changes to the assumptions underpinning the provision calculation process in line with the CBI guidelines issued during 2013 on the estimation of impairments and losses. As an example, losses are now assumed to occur for loans not likely to go to possession.

Collective statement of financial position provisions of €142m are held for the non-impaired book (68.4% of residential mortgage book) based on management's view of incurred loss in this book. The total income statement charge for 2013 was €218m (specific €193m and collective €25m).

EBS Group has received a number of requests for forbearance from customers who are experiencing cash flow difficulties. EBS Group considers these against the borrowers' current and likely future financial circumstances, their willingness to resolve these issues, as well as the legal and regulatory obligations. As part of that process loans are tested for impairment and where appropriate, the loans are downgraded to impaired status and provisions raised.

**Group Asset Quality – Residential mortgages***

| | 2013 | | | | 2012 | | | |
|---|---|---|---|---|---|---|---|---|
| | Core €m | Non-Core €m | Total €m | % | Core €m | Non-Core €m | Total €m | % |
| Satisfactory | 8,281 | 167 | 8,448 | 64.4 | 9,043 | 182 | 9,225 | 67.7 |
| *Watch* | 945 | 50 | 995 | 7.6 | 1,005 | 67 | 1,072 | 7.9 |
| *Vulnerable* | 440 | 16 | 456 | 3.5 | 406 | 18 | 424 | 3.1 |
| *Impaired* | 2,875 | 342 | 3,217 | 24.5 | 2,563 | 341 | 2904 | 21.3 |
| Criticised | 4,260 | 408 | 4,668 | 35.6 | 3,974 | 426 | 4,400 | 32.3 |
| **Total** | **12,541** | **575** | **13,116** | **100** | **13,017** | **608** | **13,625** | **100** |

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## RISK MANAGEMENT REPORT (continued)

### 6.7.2 Credit Profile (continued)

**Company Asset Quality – Residential mortgages***

| | 2013 | | | | 2012 | | | |
|---|---|---|---|---|---|---|---|---|
| | Core €m | Non-Core €m | Total €m | % | Core €m | Non-Core €m | Total €m | % |
| Satisfactory | 3,045 | 116 | 3,161 | 57.8 | 3,267 | 132 | 3,399 | 60.4 |
| *Watch* | 364 | 42 | 406 | 7.4 | 378 | 55 | 433 | 7.7 |
| *Vulnerable* | 161 | 15 | 176 | 3.2 | 149 | 15 | 164 | 2.9 |
| *Impaired* | 1,434 | 294 | 1,728 | 31.6 | 1,331 | 298 | 1,629 | 29.0 |
| Criticised | 1,959 | 351 | 2,310 | 42.2 | 1,858 | 368 | 2,226 | 39.6 |
| **Total** | **5,004** | **467** | **5,471** | **100** | **5,125** | **500** | **5,625** | **100** |

**Commercial Property**
Loans and advances to customers in the Commercial property sector are outlined below. All EBS Commercial property lending is classed as non-core. EBS exited this market in early 2008, but still holds its remaining book.

| Group and Company<br>Provisions for Commercial Property* | 2013 Total €m | 2012 Total €m |
|---|---|---|
| Total Commercial Loans | 261 | 278 |
| >30 days past due or impaired | 138 | 137 |
| >90 days past due or impaired | 135 | 132 |
| Of which impaired | 122 | 110 |
| Statement of financial position specific provisions | 30 | 27 |
| Statement of financial position collective provisions | 50 | 38 |
| Income statement specific provisions | 3 | 7 |
| Income statement collective provisions | 12 | (20) |
| Statement of financial position provisions as a % of loans and advances | 30.7% | 23.4% |
| Specific provision as a % of impaired loans | 24.6% | 24.5% |
| Impairment charge / (credit) as a % of total loans | 5.7% | (4.7%) |

| Group and Company<br>Asset Quality | 2013 Non-Core Total €m | 2013 % | 2012 Non-Core Total €m | 2012 % |
|---|---|---|---|---|
| Satisfactory | 44 | 16.9 | 59 | 21.2 |
| *Watch* | 68 | 26.1 | 77 | 27.7 |
| *Vulnerable* | 27 | 10.3 | 32 | 11.5 |
| *Impaired* | 122 | 46.7 | 110 | 39.6 |
| Criticised | 217 | 83.1 | 219 | 78.8 |
| **Total** | **261** | **100** | **278** | **100.0** |

At 31 December 2013 EBS Commercial property portfolio was €261m. Total Criticised loans were €217m (83.1%) of the portfolio and €122m (46.7%) were impaired loans. Statement of Financial Position specific provisions of €30m providing cover of 11.5% are held for this portfolio (2012: €27m and (9.7%)) with total provisions to total loans of 30.7% (2012: 23.4%). The EBS provision charge in 2013 was €15m or 5.7% of loan balances up from (€13m) or (4.7%) of total loans in 2012.

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## RISK MANAGEMENT REPORT (continued)

### 6.7.3 Asset Quality*

The following tables show criticised loans for the total loan book split into Core and Non-Core assets. Criticised loans include watch, vulnerable and impaired loans.

| Group | 2013 | | | | 2012 | | | |
|---|---|---|---|---|---|---|---|---|
| | Core | Non-Core | Total | | Core | Non-Core | Total | |
| | €m | €m | €m | % | €m | €m | €m | % |
| Satisfactory | 8,281 | 211 | 8,492 | 63.5 | 9,043 | 240 | 9,283 | 66.7 |
| *Watch* | 945 | 118 | 1,063 | 7.9 | 1,005 | 145 | 1,150 | 8.3 |
| *Vulnerable* | 440 | 43 | 483 | 3.6 | 406 | 50 | 456 | 3.3 |
| *Impaired* | 2,875 | 464 | 3,339 | 25.0 | 2,563 | 451 | 3,014 | 21.7 |
| Criticised loans | 4,260 | 625 | 4,885 | 36.5 | 3,974 | 646 | 4,620 | 33.3 |
| Gross loans | 12,541 | 836 | 13,377 | 100 | 13,017 | 886 | 13,903 | 100 |
| Criticised as a % of total gross loans | 34.0% | 74.8% | 36.5% | | 30.5% | 72.9% | 33.2% | |
| Impaired as % of total gross loans | 22.9% | 55.5% | 25.0% | | 19.7% | 50.9% | 21.7% | |

EBS Group's criticised loans and advances to customers amounted to €4,885m or 36.5% of total customer loans. EBS criticised loans have increased by €265m since 31 December 2012. The main drivers of the increase in criticised loans have been the continuing lack of activity in the property sector and consequent impact on the housing sector, together with increased unemployment and reduced earnings which negatively affected borrowers' ability to repay loans.

| Total impaired loans | 2013 | | 2012 | |
|---|---|---|---|---|
| | €m | % | €m | % |
| Impaired loans – Core | 2,875 | 21.5 | 2,563 | 18.4 |
| Impaired loans – Non Core | 464 | 3.5 | 451 | 3.3 |
| **Total** | **3,339** | **25.0** | **3,014** | **21.7** |

EBS Group impaired loans were up €325m in 2013 to €3,339m (or 25.0% of total loans) mainly in the residential mortgage portfolio. This is due to the underlying deterioration in the book.

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# RISK MANAGEMENT REPORT (continued)

### 6.7.3 Asset Quality (continued)*

| Company | 2013 | | | | 2012 | | | |
|---|---|---|---|---|---|---|---|---|
| | Core | Non-Core | Total | | Core | Non-Core | Total | |
| | €m | €m | €m | % | €m | €m | €m | % |
| Satisfactory | 3,045 | 161 | 3,206 | 55.9 | 3,267 | 190 | 3,457 | 58.6 |
| *Watch* | 364 | 110 | 474 | 8.3 | 378 | 134 | 512 | 8.7 |
| *Vulnerable* | 161 | 41 | 202 | 3.5 | 149 | 47 | 196 | 3.3 |
| *Impaired* | 1,434 | 416 | 1,850 | 32.3 | 1,331 | 407 | 1,738 | 29.4 |
| Criticised loans | 1,959 | 567 | 2,526 | 44.1 | 1,858 | 588 | 2,446 | 41.4 |
| Gross loans | 5,004 | 728 | 5,732 | 100.0 | 5,125 | 778 | 5,903 | 100.0 |
| Criticised as a % of total gross loans | 39.1% | 77.9% | 44.1% | | 36.3% | 75.5% | 41.4% | |
| Impaired as % of total gross loans | 28.7% | 57.1% | 32.3% | | 26.0% | 52.3% | 29.4% | |

EBS company's criticised loans and advances to customers amounted to €2,526m or 44.1% of total customer loans. EBS company's criticised loans have increased by €80m since 31 December 2012.

The main drivers of the increase in criticised loans have been the impact of the continuing lack of activity in the property sector and consequent impact on the housing sector, together with increased unemployment and reduced earnings which negatively affected our borrowers' ability to repay loans.

| **Total impaired loans** | **2013** | | **2012** | |
|---|---|---|---|---|
| | **€m** | **%** | **€m** | **%** |
| Impaired loans – Core | 1,434 | 25.0 | 1,331 | 22.5 |
| Impaired loans – Non Core | 416 | 7.3 | 407 | 6.9 |
| **Total** | **1,850** | **32.3** | **1,738** | **29.4** |

EBS company's impaired loans were up €112m in the year to €1,850m (or 32.3% of total loans).

**Past due but not impaired***
Loans neither past due nor impaired have decreased from 71.1% of loan balances in 2012 to 68.0% as at December 2013. The value of loans past due has increased from 28.9% in 2012 to 32.0% in 2013.

| **Group** | **2013** | | | | **2012** | | | |
|---|---|---|---|---|---|---|---|---|
| | **Core** | **Non-Core** | **Total** | **%** | **Core** | **Non-Core** | **Total** | **%** |
| | **€m** | **€m** | **€m** | | **€m** | **€m** | **€m** | |
| Neither past due nor impaired | 8,774 | 328 | 9,102 | 68.0 | 9,514 | 369 | 9,883 | 71.1 |
| Past due but not impaired | 892 | 44 | 936 | 7.0 | 940 | 67 | 1,007 | 7.2 |
| Impaired – no provision | 21 | 107 | 128 | 1.0 | 114 | 21 | 135 | 1.0 |
| Impaired – provision held | 2,854 | 357 | 3,211 | 24.0 | 2,449 | 429 | 2,878 | 20.7 |
| **Gross loans and advances** | **12,541** | **836** | **13,377** | **100.0** | **13,017** | **886** | **13,903** | **100.0** |
| Provision for impairment | (1,094) | (258) | (1,352) | | (715) | (219) | (934) | |
| **Total loans and advances after provisions** | **11,447** | **578** | **12,025** | | **12,302** | **667** | **12,969** | |

**Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

### 6.7.3 Asset Quality (continued)*

**Past due but not impaired (continued)***

Loans neither past due nor impaired have decreased from 63.7% of loan balances in 2012 to 61.3% as at December 2013. The value of loans past due has increased from 36.3% in 2012 to 38.7% in 2013.

| Company | 2013 | | | | 2012 | | | |
|---|---|---|---|---|---|---|---|---|
| | Core €m | Non-Core €m | Total €m | % | Core €m | Non-Core €m | Total €m | % |
| Neither past due nor impaired | 3,245 | 270 | 3,515 | 61.3 | 3,452 | 309 | 3,761 | 63.7 |
| Past due but not impaired | 325 | 42 | 367 | 6.4 | 342 | 63 | 405 | 6.9 |
| Impaired – no provision | 6 | 107 | 113 | 2.0 | 68 | 20 | 88 | 1.5 |
| Impaired – provision held | 1,428 | 309 | 1,737 | 30.3 | 1,263 | 386 | 1,649 | 27.9 |
| **Gross loans and advances** | **5,004** | **728** | **5,732** | **100.0** | **5,125** | **778** | **5,903** | **100.0** |
| Provision for impairment | (585) | (230) | (815) | | (386) | (196) | (582) | |
| **Total loans and advances after provisions** | **4,419** | **498** | **4,917** | | **4,739** | **582** | **5,321** | |

**Aged analysis of loans and advances which are past due but not impaired***

Residential loans up to 90 days past due are not categorised as impaired. Non-core loans are assessed on a case by case basis.

| Group | 2013 | | | | 2012 | | | |
|---|---|---|---|---|---|---|---|---|
| | Core €m | Non-Core €m | Total €m | % | Core €m | Non-Core €m | Total €m | % |
| 1–30days | 496 | 7 | 503 | 55.1 | 568 | 15 | 583 | 60.2 |
| 31–60days | 207 | 5 | 212 | 23.2 | 213 | 6 | 219 | 22.6 |
| 61–90days | 142 | 4 | 146 | 16.0 | 116 | 4 | 120 | 12.4 |
| 91–180days | 46 | 2 | 48 | 5.3 | 42 | 2 | 44 | 4.5 |
| 181–365days | 1 | - | 1 | 0.1 | 1 | - | 1 | 0.1 |
| >365days | - | 3 | 3 | 0.3 | - | 2 | 2 | 0.2 |
| **Total** | **892** | **21** | **913** | **100.0** | **940** | **29** | **969** | **100.0** |

| Company | 2013 | | | | 2012 | | | |
|---|---|---|---|---|---|---|---|---|
| | Core €m | Non-Core €m | Total €m | % | Core €m | Non-Core €m | Total €m | % |
| 1–30days | 180 | 6 | 186 | 54.0 | 208 | 13 | 221 | 60.2 |
| 31–60days | 78 | 4 | 82 | 23.8 | 76 | 5 | 81 | 22.1 |
| 61–90days | 53 | 4 | 57 | 16.6 | 43 | 3 | 46 | 12.5 |
| 91–180days | 14 | 2 | 16 | 4.7 | 14 | 2 | 16 | 4.4 |
| 181–365days | - | - | - | - | - | 1 | 1 | 0.3 |
| >365days | - | 3 | 3 | 0.9 | 1 | 1 | 2 | 0.5 |
| **Total** | **325** | **19** | **344** | **100.0** | **342** | **25** | **367** | **100.0** |

Provisions are calculated for assets which are deemed to be impaired where there is objective evidence of impairment. If the asset is deemed to be significant, then it is reviewed on an individual basis. Where the asset is impaired, but not significant, it is reviewed on a collective basis.



**Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

### 6.7.3 Asset Quality (continued)*

**Aged analysis of loans and advances which are past due but not impaired (continued)**

| Group 2013* | Loans & Advances | Impaired Loans & Advances | Impaired % Of Loans | Individually Assessed | IBNR Assessed | Total Impairment Provision | Provision % of Impaired Loans | Provision % of Loans |
|---|---|---|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m | €m | | |
| Residential | 13,116 | 3,217 | 24.5% | 1,037 | 235 | 1,272 | 39.5% | 9.7% |
| Commercial Property | 261 | 122 | 46.7% | 30 | 50 | 80 | 65.6% | 30.7% |
| **Total** | **13,377** | **3,339** | **25.0%** | **1,067** | **285** | **1,352** | **40.5%** | **10.1%** |

| Group 2012* | Loans & Advances | Impaired Loans & Advances | Impaired % Of Loans | Individually Assessed | IBNR Assessed | Total Impairment Provision | Provision % of Impaired Loans | Provision % of Loans |
|---|---|---|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m | €m | | |
| Residential | 13,625 | 2,904 | 21.3% | 689 | 180 | 869 | 29.9% | 6.4% |
| Commercial Property | 278 | 110 | 39.6% | 27 | 38 | 65 | 59.1% | 23.4% |
| **Total** | **13,903** | **3,014** | **21.7%** | **716** | **218** | **934** | **31.0%** | **6.7%** |

| Company 2013 * | Loans & Advances | Impaired Loans & Advances | Impaired % Of Loans | Individually Assessed | IBNR Assessed | Total Impairment Provision | Provision % of Impaired Loans | Provision % of Loans |
|---|---|---|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m | €m | | |
| Residential | 5,471 | 1,728 | 31.6% | 593 | 142 | 735 | 42.5% | 13.4% |
| Commercial Property | 261 | 122 | 46.7% | 30 | 50 | 80 | 65.6% | 30.7% |
| **Total** | **5,732** | **1,850** | **32.3%** | **623** | **192** | **815** | **44.1%** | **14.2%** |

| Company 2012 * | Loans & Advances | Impaired Loans & Advances | Impaired % Of Loans | Individually Assessed | IBNR Assessed | Total Impairment Provision | Provision % of Impaired Loans | Provision % of Loans |
|---|---|---|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m | €m | | |
| Residential | 5,625 | 1,629 | 29.0% | 400 | 117 | 517 | 31.7% | 9.2% |
| Commercial Property | 278 | 110 | 39.4% | 27 | 38 | 65 | 59.1% | 23.3% |
| **Total** | **5,903** | **1,739** | **29.4%** | **427** | **155** | **582** | **33.8%** | **9.9%** |

Global and domestic economic markets continued to experience difficulties throughout 2013 which impacted negatively on the Group and Company's lending portfolios.

The main types of forbearance arrangements for residential mortgages only are analysed below.

### 6.7.4 Forbearance*

The Group uses a range of tools to support customers. The Group considers requests from customers who are experiencing cash flow difficulties on a case by case basis against their current and likely future financial circumstances and their willingness to resolve these difficulties, taking into account legal and regulatory obligations. The Group has implemented the standards for the Codes of Conduct in relation to customers in difficulty as set out by the CBI ensuring these customers are dealt with in a professional and timely manner.

A forbearance agreement is entered into where the customer is in financial difficulty to the extent that they are unable to repay both the principal and interest in accordance with the original contract terms.

**Forms an integral part of the audited financial statements*

## RISK MANAGEMENT REPORT (continued)

**6.7.4 Forbearance (continued)***

Modifications to the original contract can be of a temporary (e.g. interest only) or permanent (e.g. term extension) nature and a loan is considered to be no longer a forborne loan once the modified terms and conditions have expired.

As we are still in the early stages of implementing advanced forbearance solutions, the sustainability of the individual forbearance measures will be reviewed and assessed over time. The impact on provisioning will also be reviewed.

The Group has developed a Mortgage Arrears Resolution Strategy (‘MARS’) for dealing with mortgage customers in difficulty or likely to be in difficulty. This builds on and formalises the Group’s Mortgage Arrears Resolution Process.

The strategy is built on three key factors:
i) Segmentation – identifying customers in difficulty;
ii) Sustainability – customer assessment; and
iii) Suitable Treatment – identifying solutions.

The core objectives are to ensure that arrears solutions are sustainable in the long term and they comply with the spirit and the letter of all regulatory requirements. MARS includes the following new longer-term forbearance solutions which have been devised to assist existing Republic of Ireland primary residential mortgage customers in difficulty:

Split mortgages – a split mortgage will be considered where a customer can afford a mortgage but their income is not sufficient to fully support their current mortgage. The existing mortgage is split into two parts: Loan A being the sustainable element, which is repaid on the basis of principal and interest, and Loan B being the unsustainable element, which is deferred and becomes repayable at a later date, this may also include an element of debt write-off;

Negative equity trade down – This allows a customer to sell their house and subsequently purchase a new property and transfer the negative equity portion to a new loan secured on the new property. A negative equity trade down mortgage will be considered where a customer will reduce monthly loan repayments and overall indebtedness by trading down to a property more appropriate to his/her current financial and other circumstances;

Voluntary sale for loss – A voluntary sale for loss solution will be considered where the loan is deemed to be unsustainable and the customer is agreeable to sell the property and put an appropriate agreement in place to repay any residual debt.

Forbearance mortgage loans, as for any loan classified as impaired, may be upgraded from impaired status, subject to a satisfactory assessment by the appropriate credit authority as to the borrower’s continuing ability and willingness to repay and confirmation that the relevant security held by the Bank continues to be enforceable. In this regard, the borrower is required to display a satisfactory performance following the period of restructure of the loan, comprising a period of twelve months consecutive payments of full principal and interest and typically, the upgrade would initially be to Watch/Vulnerable grades. If a loan is upgraded from impaired, it will be included in the Bank’s collective assessment for IBNR provisions.

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# RISK MANAGEMENT REPORT (continued)

## 6.7.4 Forbearance (continued)*

### Group Owner Occupier Mortgages

| | 2013* | | 2013* | |
|---|---|---|---|---|
| | Total loans in forbearance | | Loans >90 days in arrears and/or impaired at year end | |
| | Number of loans | Balance €m | Number of loans | Balance €m |
| **Temporary Restructures** | | | | |
| Interest only | 1,977 | 289 | 716 | 106 |
| Deferred interest scheme | 11 | 3 | 4 | 1 |
| Other | 145 | 16 | 60 | 7 |
| **Temporary Restructures Sub-total** | **2,133** | **308** | **780** | **114** |
| **Permanent Restructures** | | | | |
| Arrears capitalisation | 3,646 | 464 | 2,081 | 253 |
| Term extension | 3,644 | 324 | 725 | 65 |
| Negative equity trade down mortgage | 7 | 1 | - | - |
| Split mortgage | 192 | 28 | 137 | 19 |
| Sale for loss | 47 | 4 | 43 | 3 |
| **Permanent Restructures Sub-total** | **7,536** | **821** | **2,986** | **340** |
| **Total** | **9,669** | **1,129** | **3,766** | **454** |

| | 2012 | | 2012 | |
|---|---|---|---|---|
| | Total loans in forbearance | | Loans >90 days in arrears and/or impaired at year end | |
| | Number of loans | Balance €m | Number of loans | Balance €m |
| **Temporary Restructures** | | | | |
| Interest only | 5,119 | 808 | 1,788 | 292 |
| Deferred interest scheme | 10 | 3 | 4 | 1 |
| Other | 297 | 36 | 138 | 18 |
| **Temporary Restructures Sub-total** | **5,426** | **847** | **1,930** | **311** |
| **Permanent Restructures** | | | | |
| Arrears capitalisation | 1,362 | 193 | 946 | 130 |
| Term extension | 3,579 | 317 | 593 | 48 |
| Split mortgage | 8 | - | 4 | 1 |
| **Permanent Restructures Sub-total** | **4,949** | **510** | **1,543** | **179** |
| **Total** | **10,375** | **1,357** | **3,473** | **490** |



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# RISK MANAGEMENT REPORT (continued)

### 6.7.4 Forbearance (continued)*

**Group Buy-to-let Mortgages**

| | 2013* | | 2013* | |
|---|---|---|---|---|
| | Total loans in forbearance | | Loans >90 days in arrears and/or impaired at year end | |
| | Number of loans | Balance €m | Number of loans | Balance €m |
| **Temporary Restructures** | | | | |
| Interest only | 158 | 65 | 90 | 50 |
| Other | 23 | 17 | 18 | 16 |
| **Temporary Restructures Sub-total** | **181** | **82** | **108** | **66** |
| **Permanent Restructures** | | | | |
| Arrears capitalisation | 57 | 25 | 49 | 23 |
| Term extension | 80 | 10 | 20 | 2 |
| Sale for Loss | 6 | 1 | 6 | 1 |
| **Permanent Restructures Sub-total** | **143** | **36** | **75** | **26** |
| Total | **324** | **118** | **183** | **92** |

| | 2012 | | 2012 | |
|---|---|---|---|---|
| | Total loans in forbearance | | Loans >90 days in arrears and/or impaired at year end | |
| | Number of loans | Balance €m | Number of loans | Balance €m |
| **Temporary Restructures** | | | | |
| Interest only | 318 | 98 | 158 | 67 |
| Other | 25 | 10 | 14 | 8 |
| **Temporary Restructures Sub-total** | **343** | **108** | **172** | **75** |
| **Permanent Restructures** | | | | |
| Arrears capitalisation | 11 | 8 | 8 | 8 |
| Term extension | 66 | 7 | 17 | 1 |
| **Permanent Restructures Sub-total** | **77** | **15** | **25** | **9** |
| Total | **420** | **123** | **197** | **84** |

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## RISK MANAGEMENT REPORT (continued)

### 6.7.4 Forbearance (continued)*

**Group Total Mortgages**

| | 2013* | | 2013* | |
|---|---|---|---|---|
| | Total loans in forbearance | | Loans >90 days in arrears and/or impaired at year end | |
| | Number of loans | Balance €m | Number of loans | Balance €m |
| **Temporary Restructures** | | | | |
| Interest only | 2,135 | 354 | 806 | 156 |
| Deferred interest scheme | 11 | 3 | 4 | 1 |
| Other | 168 | 33 | 78 | 23 |
| **Temporary Restructures Sub-total** | **2,314** | **390** | **888** | **180** |
| **Permanent Restructures** | | | | |
| Arrears capitalisation | 3,703 | 489 | 2,130 | 276 |
| Term extension | 3,724 | 334 | 745 | 67 |
| Split mortgage | 192 | 28 | 137 | 19 |
| Sale for loss | 53 | 5 | 49 | 4 |
| Negative equity trade down mortgage | 7 | 1 | - | - |
| **Permanent Restructures Sub-total** | **7,679** | **857** | **3,061** | **366** |
| **Total** | **9,993** | **1,247** | **3,949** | **546** |

| | 2012 | | 2012 | |
|---|---|---|---|---|
| | Total loans in forbearance | | Loans >90 days in arrears and/or impaired at year end | |
| | Number of loans | Balance €m | Number of loans | Balance €m |
| **Temporary Restructures** | | | | |
| Interest only | 5,437 | 908 | 1,946 | 359 |
| Deferred interest scheme | 10 | 3 | 4 | 1 |
| Other | 322 | 46 | 153 | 26 |
| **Temporary Restructures Sub-total** | **5,769** | **957** | **2,103** | **386** |
| **Permanent Restructures** | | | | |
| Arrears capitalisation | 1,373 | 201 | 954 | 137 |
| Term extension | 3,645 | 324 | 610 | 50 |
| Split mortgage | 8 | - | 4 | 1 |
| **Permanent Restructures Sub-total** | **5,026** | **525** | **1,568** | **188** |
| **Total** | **10,795** | **1,482** | **3,671** | **574** |

Of the total Group residential mortgage book of €13,116m, 9.5% are subject to forbearance measures as at 31 December 2013, compared to 10.9% as at 31 December 2012.

€546m (43.8%) of the loans under forbearance were >90 days past due or impaired as at 31 December 2013, compared to 38.7% as at 31 December 2012.

**Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

### 6.7.4 Forbearance (continued)*

**Group Residential Mortgages in Forbearance - index linked LTV***

| 2013* | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| Less than 50% | 105 | 8 | 113 |
| 50% - 70% | 105 | 9 | 114 |
| 71% - 80% | 80 | 12 | 92 |
| 81% - 90% | 87 | 18 | 105 |
| 91% - 100% | 95 | 11 | 106 |
| 101% - 120% | 211 | 29 | 240 |
| 121% - 150% | 253 | 26 | 279 |
| Greater than 150% | 193 | 5 | 198 |
| **Total** | **1,129** | **118** | **1,247** |

| 2012 | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| Less than 50% | 82 | 8 | 90 |
| 50% - 70% | 104 | 11 | 115 |
| 71% - 80% | 77 | 12 | 89 |
| 81% - 90% | 84 | 10 | 94 |
| 91% - 100% | 108 | 8 | 116 |
| 101% - 120% | 241 | 28 | 269 |
| 121% - 150% | 354 | 30 | 384 |
| Greater than 150% | 309 | 16 | 325 |
| **Total** | **1,359** | **123** | **1,482** |

Forbearance stock - past due but not impaired*

| 2013* | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| 1 – 30 days | 100 | - | 100 |
| 31 – 60 days | 36 | 1 | 37 |
| 61 – 90 days | 27 | 1 | 28 |
| 91 – 180 days | 11 | - | 11 |
| 181 – 365 days | - | - | - |
| > 365 days | - | - | - |
| **Total** | **174** | **2** | **176** |

| 2012 | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| 1 – 30 days | 109 | 3 | 112 |
| 31 – 60 days | 56 | - | 56 |
| 61 – 90 days | 26 | 1 | 28 |
| 91 – 180 days | 11 | 1 | 11 |
| 181 – 365 days | - | - | - |
| > 365 days | - | - | - |
| **Total** | **202** | **5** | **207** |

**Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

### 6.7.4 Forbearance (continued)*

**Group Residential Mortgages in Forbearance - index linked LTV (continued)**

Forbearance stock – impaired*

| 2013* | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| Not past due | 99 | 59 | 158 |
| 1 – 30 days | 44 | 5 | 49 |
| 31 – 60 days | 30 | 3 | 33 |
| 61 – 90 days | 24 | 2 | 26 |
| 91 – 180 days | 70 | 3 | 73 |
| 181 – 365 days | 66 | 6 | 72 |
| > 365 days | 110 | 14 | 124 |
| **Total** | **443** | **92** | **535** |

| 2012 | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| Not past due | 76 | 39 | 115 |
| 1 – 30 days | 35 | 4 | 39 |
| 31 – 60 days | 25 | 5 | 30 |
| 61 – 90 days | 20 | 4 | 24 |
| 91 – 180 days | 96 | 6 | 102 |
| 181 – 365 days | 112 | 16 | 128 |
| > 365 days | 115 | 9 | 124 |
| **Total** | **479** | **83** | **562** |

Forbearance stock – summary*

| 2013* | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| Past due but not impaired | 174 | 2 | 176 |
| Impaired | 443 | 92 | 535 |
| Neither past due nor impaired | 512 | 24 | 536 |
| **Total** | **1,129** | **118** | **1,247** |

| 2012 | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| Past due but not impaired | 202 | 5 | 207 |
| Impaired | 480 | 83 | 563 |
| Neither past due nor impaired | 677 | 35 | 712 |
| **Total** | **1,359** | **123** | **1,482** |

### 6.7.5 Group Residential Repossessions*

For the purpose of the following tables, a property is considered repossessed when legal title has transferred to AIB. AIB seeks to avoid repossession through working with customers, but where agreement cannot be reached, proceeds to repossession of the property or the appointment of a fixed asset receiver, using external agents to realise the maximum value as soon as is practicable. Where the Group believes that the proceeds of sale of a repossessed property will comprise only part of the recoverable amount of the loan against which it was being held as security, the customer remains liable for the outstanding balance and the remaining loan continues to be recognised on the statement of financial position.

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# RISK MANAGEMENT REPORT (continued)

### 6.7.5 Group Residential Repossessions (continued)*

| Residential Mortgages - Repossessions | | | | | 2013 | |
|---|---|---|---|---|---|---|
| Movements in residential repossessions | Core | | Non-Core | | Total | |
| | No. of properties | Loan balance at repossession €m | No. of properties | Loan balance at repossession €m | No. of properties | Loan balance at repossession €m |
| Opening stock 1 January 2013 | 55 | 16 | 11 | 3 | 66 | 19 |
| Repossessions in 2013 | 74 | 19 | 2 | - | 76 | 19 |
| Disposals | (50) | (14) | (4) | (1) | (54) | (15) |
| **Closing stock 31 December 2013** | **79** | **21** | **9** | **2** | **88** | **23** |

| | Core | Non-Core | Total |
|---|---|---|---|
| | No. of properties | No. of properties | No. of properties |
| **Of which at 31 December 2013:** | | | |
| Voluntary Surrenders | 30 | 2 | **32** |
| Enforcement of security | 44 | - | **44** |
| Total | **74** | **2** | **76** |

EBS Group held 88 properties as at 31 December 2013, representing an increase of 22 compared with 2012. The EBS Group disposed of 54 properties during 2013 recognising a loss on disposal of €9m.

| Residential Mortgages – Repossessions | | | | | 2012 | |
|---|---|---|---|---|---|---|
| Movements in residential repossessions | Core | | Non-Core | | Total | |
| | No. of properties | Loan balance at repossession €m | No. of properties | Loan balance at repossession €m | No. of properties | Loan balance at repossession €m |
| Opening stock 1 January 2012 | 69 | 24 | 10 | 1 | 79 | 25 |
| Repossessions in 2012 | 22 | 4 | 8 | 5 | 30 | 9 |
| Disposals | (36) | (11) | (7) | (4) | (43) | (14) |
| **Closing stock 31 December 2012** | **55** | **17** | **11** | **2** | **66** | **20** |

**Forms an integral part of the audited financial statements*

## RISK MANAGEMENT REPORT (continued)

### 6.7.5 Group Residential Repossessions (continued)*

**Residential Mortgages – Repossessions (continued)**

| | Core | Non-Core | Total |
|---|---|---|---|
| | No. of properties | No. of properties | No. of properties |
| **Of which at 31 December 2012:** | | | |
| Voluntary Surrenders | 14 | 7 | **21** |
| Enforcement of security | 8 | 1 | **9** |
| Total | **22** | **8** | **30** |

EBS Group held 66 properties at year end, representing a decrease of 13 compared with 2012. The EBS Group disposed of 43 properties during 2013 recognising a loss on disposal of €9.7m.

| Group Stock / Activity | Number of disposals | Balance outstanding at sale €m | Gross sales proceeds €m | Cost to sell €m | Loss on sale €m | Weighted Average LTV at sale % |
|---|---|---|---|---|---|---|
| **2013** | | | | | | |
| Owner Occupier | 50 | 13 | 5 | 1 | 9 | 282% |
| Buy-to-let | 4 | 1 | - | - | 1 | 239% |
| **Total repossessions** | **54** | **14** | **5** | **1** | **10** | **279%** |
| **2012** | | | | | | |
| Owner Occupier | 36 | 11 | 4 | 1 | 7 | 253% |
| Buy-to-let | 7 | 4 | 1 | - | 2 | 278% |
| **Total repossessions** | **43** | **15** | **5** | **1** | **9** | **259%** |

### 6.7.6 Residential mortgage lending - index linked LTV

**Group Residential mortgage lending – Total***
The property values used in the completion of the following loan to value tables are determined with reference to the most recent valuation indexed to the CSO Residential Property Price Index.

| 2013* | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| Less than 50% | 1,324 | 51 | 1,375 |
| 50% - 70% | 1,271 | 61 | 1,332 |
| 71% - 80% | 840 | 41 | 881 |
| 81% - 90% | 949 | 42 | 991 |
| 91% - 100% | 1,130 | 51 | 1,181 |
| 101% - 120% | 2,387 | 110 | 2,497 |
| 121% - 150% | 2,537 | 110 | 2,647 |
| Greater than 150% | 2,103 | 109 | 2,212 |
| **Total** | **12,541** | **575** | **13,116** |

**Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

### 6.7.6 Residential mortgage lending - index linked LTV (continued)

**Group Residential mortgage lending – Total (continued)**

| 2012 | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| Less than 50% | 1,206 | 48 | 1,254 |
| 50% - 70% | 1,161 | 48 | 1,209 |
| 71% - 80% | 749 | 32 | 781 |
| 81% - 90% | 859 | 45 | 904 |
| 91% - 100% | 980 | 49 | 1,029 |
| 101% - 120% | 2,478 | 100 | 2,578 |
| 121% - 150% | 2,890 | 143 | 3,033 |
| Greater than 150% | 2,694 | 143 | 2,837 |
| **Total** | **13,017** | **608** | **13,625** |

44.0% of the owner-occupier and 42.8% of the buy-to-let mortgages were in positive equity at 31 December 2013. In terms of the total portfolio, 56.1% (2012: 62.0%) was in negative equity at 31 December 2013, reflecting the overall decline in residential property prices in Ireland by 2013. The weighted average indexed loan to value ratio for the total book was 107.4% at 31 December 2013 whilst the indexed loan to value ratio for the 90 days past due and/or impaired book was higher at 126.6%. The indexed loan to value ratio of new loans advanced during 2013 was 78.1%.

**Group Residential - Neither past due nor impaired***
The following tables profile the residential mortgage portfolio that is neither past due nor impaired by the indexed loan to value ratios at 31 December 2013 and 2012.

| **2013*** Neither past due nor impaired | Core €m | Non-Core €m | Total €m |
|---|---|---|---|
| Less than 50% | 1,131 | 26 | 1,157 |
| 50% - 70% | 1,021 | 21 | 1,042 |
| 71% - 80% | 672 | 17 | 689 |
| 81% - 90% | 749 | 16 | 765 |
| 91% - 100% | 859 | 16 | 875 |
| 101% - 120% | 1,760 | 26 | 1,786 |
| 121% - 150% | 1,606 | 29 | 1,635 |
| Greater than 150% | 976 | 62 | 1,038 |
| **Total** | **8,774** | **213** | **8,987** |

# RISK MANAGEMENT REPORT (continued)

### 6.7.6 Residential mortgage lending - index linked LTV (continued)

**Group Residential - Neither past due nor impaired (continued)***

| **2012** | **Core €m** | **Non-Core €m** | **Total €m** |
|---|---|---|---|
| Less than 50% | 1,037 | 26 | 1,063 |
| 50% - 70% | 949 | 19 | 968 |
| 71% - 80% | 603 | 11 | 614 |
| 81% - 90% | 693 | 16 | 709 |
| 91% - 100% | 776 | 20 | 796 |
| 101% - 120% | 1,943 | 30 | 1,973 |
| 121% - 150% | 1,983 | 35 | 2,018 |
| Greater than 150% | 1,530 | 80 | 1,610 |
| **Total** | **9,514** | **237** | **9,751** |

Among loans neither past due nor impaired, 50.5% (2012: 42.7%) of the owner-occupier and 45.1% (2012: 38.9%) of the buy-to-let mortgages were in positive equity at 31 December 2013. In terms of the total portfolio, 49.6% (2012: 57.4%) was in negative equity at 31 December 2013, reflecting the overall decline in residential property prices in Ireland in 2013.

**90 days past due or impaired***
The following tables profile the residential mortgage portfolio that was > 90 days past due and /or impaired by the indexed loan to value ratios at 31 December 2013 and 2012.

| **2013*** >90 days past due and/or impaired | **Core €m** | **Non-Core €m** | **Total €m** |
|---|---|---|---|
| Less than 50% | 136 | 23 | 159 |
| 50% - 70% | 182 | 38 | 220 |
| 71% - 80% | 119 | 23 | 142 |
| 81% - 90% | 137 | 25 | 162 |
| 91% - 100% | 186 | 34 | 220 |
| 101% - 120% | 451 | 80 | 531 |
| 121% - 150% | 733 | 77 | 810 |
| Greater than 150% | 978 | 46 | 1,024 |
| **Total** | **2,922** | **346** | **3,268** |

| **2012** >90 days past due and/or impaired | **Core €m** | **Non-Core €m** | **Total €m** |
|---|---|---|---|
| Less than 50% | 111 | 20 | 131 |
| 50% - 70% | 151 | 27 | 178 |
| 71% - 80% | 102 | 19 | 121 |
| 81% - 90% | 107 | 27 | 134 |
| 91% - 100% | 142 | 25 | 167 |
| 101% - 120% | 361 | 69 | 430 |
| 121% - 150% | 672 | 99 | 771 |
| Greater than 150% | 960 | 60 | 1,020 |
| **Total** | **2,606** | **346** | **2,952** |

26% of the owner-occupier and 41.3% of the BTL mortgages were in positive equity at 31 December 2013. In terms of the total portfolio, 72.4% was in negative equity at 31 December 2013, reflecting the overall decline in residential property prices in Ireland in 2013.

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# RISK MANAGEMENT REPORT (continued)

### 6.7.6 Residential mortgage lending - index linked LTV (continued)

**Group Residential Mortgage Lending with Fair Value Collateral**

Group Residential Mortgage lending – Total*

The property values used in the completion of the following EBS Group loan to value tables are determined with reference to the most recent valuation indexed to the CSO Residential Property Price Index.

In the tables below, for loans with an LTV <100% the outstanding loan value is deemed to be the collateral value. For loans with an LTV >100%, the value of collateral is indexed valuations based on the CSO property valuation for Residential Property.

| **2013*** | **Core €m** | **Non-Core €m** | **Total €m** |
|---|---|---|---|
| *Fully Collateralised* | | | |
| Less than 50% | 1,324 | 51 | 1,375 |
| 50% - 70% | 1,271 | 61 | 1,332 |
| 71% - 80% | 840 | 41 | 881 |
| 81% - 90% | 949 | 42 | 991 |
| 91% - 100% | 1,130 | 51 | 1,181 |
| *Partially Collateralised* | | | |
| *Book Value* | *7,027* | *329* | *7,356* |
| Value of Collateral | 5,323 | 240 | 5,563 |
| **Total** | **10,837** | **486** | **11,323** |

| **2012** | **Core €m** | **Non-Core €m** | **Total €m** |
|---|---|---|---|
| *Fully Collateralised* | | | |
| Less than 50% | 1,206 | 48 | 1,254 |
| 50% - 70% | 1,161 | 48 | 1,209 |
| 71% - 80% | 749 | 32 | 781 |
| 81% - 90% | 859 | 45 | 904 |
| 91% - 100% | 980 | 49 | 1,029 |
| *Partially Collateralised* | | | |
| *Book Value* | *8,061* | *386* | *8,447* |
| Value of Collateral | 5,916 | 273 | 6,189 |
| **Total** | **10,871** | **495** | **11,366** |

Group Residential Mortgage lending – Neither past due nor impaired

The following Group tables profile the residential mortgage portfolio that is neither past due nor impaired by the indexed loan to value ratios at 31 December 2013 and 2012.

| **2013***<br>Neither past due nor impaired | **Core €m** | **Non-Core €m** | **Total €m** |
|---|---|---|---|
| *Fully Collateralised* | | | |
| Less than 50% | 1,132 | 26 | 1,158 |
| 50% - 70% | 1,021 | 21 | 1,042 |
| 71% - 80% | 672 | 17 | 689 |
| 81% - 90% | 749 | 16 | 765 |
| 91% - 100% | 859 | 16 | 875 |
| *Partially Collateralised* | | | |
| *Book Value* | *4,341* | *116* | *4,457* |
| Value of Collateral | 3,393 | 74 | 3,467 |
| **Total** | **7,826** | **170** | **7,996** |



*Forms an integral part of the audited financial statements

# RISK MANAGEMENT REPORT (continued)

## 6.7.6 Residential mortgage lending - index linked LTV (continued)

**Group Residential Mortgage Lending with Fair Value Collateral (continued)***

| **2012**<br>Neither past due nor impaired | **Core**<br>**€m** | **Non-Core**<br>**€m** | **Total**<br>**€m** |
|---|---|---|---|
| *Fully Collateralised* | | | |
| Less than 50% | 1,037 | 26 | 1,063 |
| 50% - 70% | 949 | 19 | 968 |
| 71% - 80% | 603 | 11 | 614 |
| 81% - 90% | 693 | 16 | 709 |
| 91% - 100% | 776 | 20 | 796 |
| *Partially Collateralised* | | | |
| *Book Value* | *5,456* | *145* | *5,601* |
| Value of Collateral | 4,103 | 93 | 4,196 |
| **Total** | **8,161** | **185** | **8,346** |

Group Residential Mortgage lending – Past due not impaired

The following Group tables profile the residential mortgage portfolio that is past due not impaired by the indexed loan to value ratios at 31 December 2013 and 2012.

| **2013***<br>Past due not impaired | **Core**<br>**€m** | **Non-Core**<br>**€m** | **Total**<br>**€m** |
|---|---|---|---|
| *Fully Collateralised* | | | |
| Less than 50% | 58 | 2 | 60 |
| 50% - 70% | 71 | 4 | 75 |
| 71% - 80% | 50 | 2 | 52 |
| 81% - 90% | 66 | 1 | 67 |
| 91% - 100% | 88 | 1 | 89 |
| *Partially Collateralised* | | | |
| *Book Value* | *559* | *11* | *570* |
| Value of Collateral | 423 | 9 | 432 |
| **Total** | **756** | **19** | **775** |

| **2012**<br>Past due not impaired | **Core**<br>**€m** | **Non-Core**<br>**€m** | **Total**<br>**€m** |
|---|---|---|---|
| *Fully Collateralised* | | | |
| Less than 50% | 61 | 2 | 63 |
| 50% - 70% | 65 | 3 | 68 |
| 71% - 80% | 45 | 3 | 48 |
| 81% - 90% | 60 | 2 | 62 |
| 91% - 100% | 64 | 4 | 68 |
| *Partially Collateralised* | | | |
| *Book Value* | *645* | *15* | *660* |
| Value of Collateral | 471 | 10 | 481 |
| **Total** | **766** | **24** | **790** |

# RISK MANAGEMENT REPORT (continued)

### 6.7.6 Residential mortgage lending - index linked LTV (continued)

**Group Residential Mortgage Lending with Fair Value Collateral (continued)***

Group Residential Mortgage lending – 90 days past due or impaired
The following tables profile the Group residential mortgage portfolio that was >90 days past due or impaired by the indexed loan to value ratios at 31 December 2013 and 2012.

| **2013***<br>90 days past due or impaired | **Core**<br>**€m** | **Non-Core**<br>**€m** | **Total**<br>**€m** |
|---|---|---|---|
| *Fully Collateralised* | | | |
| Less than 50% | 136 | 23 | 159 |
| 50% - 70% | 182 | 38 | 220 |
| 71% - 80% | 119 | 23 | 142 |
| 81% - 90% | 137 | 25 | 162 |
| 91% - 100% | 186 | 34 | 220 |
| *Partially Collateralised* | | | |
| *Book Value* | *2,162* | *203* | *2,365* |
| *Value of Collateral* | 1,531 | 159 | 1,690 |
| **Total** | **2,291** | **302** | **2,593** |

| **2012**<br>90 days past due or impaired | **Core**<br>**€m** | **Non-Core**<br>**€m** | **Total**<br>**€m** |
|---|---|---|---|
| *Fully Collateralised* | | | |
| Less than 50% | 111 | 20 | 131 |
| 50% - 70% | 151 | 27 | 178 |
| 71% - 80% | 102 | 19 | 121 |
| 81% - 90% | 107 | 27 | 134 |
| 91% - 100% | 142 | 25 | 167 |
| *Partially Collateralised* | | | |
| *Book Value* | *1,993* | *228* | *2,221* |
| *Value of Collateral* | 1,366 | 170 | 1,536 |
| **Total** | **1,979** | **288** | **2,267** |

Group Residential Mortgage lending – Impaired
The following tables profile the Group residential mortgage portfolio that was impaired by the indexed loan to value ratios at 31 December 2013 and 2012.

| **2013***<br>**Impaired** | **Core**<br>**€m** | **Non-Core**<br>**€m** | **Total**<br>**€m** |
|---|---|---|---|
| *Fully Collateralised* | | | |
| Less than 50% | 135 | 23 | 158 |
| 50% - 70% | 179 | 36 | 215 |
| 71% - 80% | 117 | 23 | 140 |
| 81% - 90% | 134 | 25 | 159 |
| 91% - 100% | 182 | 34 | 216 |
| *Partially Collateralised* | | | |
| *Book Value* | *2,127* | *201* | *2,328* |
| Value of Collateral | 1,506 | 158 | 1,664 |
| **Total** | **2,253** | **299** | **2,552** |



**Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

### 6.7.6 Residential mortgage lending - index linked LTV (continued)

**Group Residential Mortgage Lending with Fair Value Collateral (continued)***

Group Residential Mortgage lending – Impaired (continued)

| **2012 Impaired** | **Core €m** | **Non-Core €m** | **Total €m** |
|---|---|---|---|
| *Fully Collateralised* | | | |
| Less than 50% | 108 | 20 | 128 |
| 50% - 70% | 148 | 26 | 174 |
| 71% - 80% | 101 | 17 | 118 |
| 81% - 90% | 105 | 27 | 133 |
| 91% - 100% | 140 | 25 | 164 |
| *Partially Collateralised* | | | |
| *Book Value* | *1,961* | *226* | *2,187* |
| Value of Collateral | 1,343 | 169 | 1,512 |
| **Total** | **1,945** | **284** | **2,229** |

Group vintage analysis – Residential and Impaired

The following table profiles the Republic of Ireland residential mortgage book and impaired residential mortgage book at 31 December 2013 and 2012 by year of origination.

| **Loan Origination Profile of Residential Mortgages (before provision for impairment)** | **TOTAL 2013** | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **Residential Mortgage Loan Book** | | **Loans >90 days in arrears but not impaired at year end** | | **Loans classified as impaired at year end** | | **Loans >90 days in arrears and/or impaired at year end** | |
| | **Number of loans** | **Balance €m** | **Number of loans** | **Balance €m** | **Number of loans** | **Balance €m** | **Number of loans** | **Balance €m** |
| 1996 and before | 4,611 | 126 | 6 | - | 754 | 29 | 760 | 29 |
| 1997 | 1,923 | 57 | 2 | - | 230 | 10 | 232 | 10 |
| 1998 | 2,154 | 79 | 5 | - | 288 | 14 | 293 | 14 |
| 1999 | 2,868 | 120 | 7 | - | 393 | 28 | 400 | 28 |
| 2000 | 3,103 | 172 | 7 | - | 449 | 34 | 456 | 34 |
| 2001 | 3,369 | 244 | 9 | 1 | 541 | 51 | 550 | 52 |
| 2002 | 4,776 | 411 | 12 | 1 | 764 | 82 | 776 | 83 |
| 2003 | 5,801 | 562 | 6 | 1 | 1,128 | 135 | 1,134 | 136 |
| 2004 | 7,812 | 907 | 25 | 3 | 1,466 | 214 | 1,491 | 217 |
| 2005 | 11,488 | 1,458 | 35 | 4 | 2,313 | 380 | 2,348 | 384 |
| 2006 | 14,587 | 2,227 | 60 | 12 | 3,523 | 686 | 3,583 | 698 |
| 2007 | 14,032 | 2,219 | 73 | 13 | 3,933 | 706 | 4,006 | 719 |
| 2008 | 13,444 | 2,185 | 54 | 9 | 3,347 | 601 | 3,401 | 610 |
| 2009 | 8,168 | 1,132 | 26 | 4 | 1,127 | 176 | 1,153 | 180 |
| 2010 | 6,900 | 1,006 | 13 | 3 | 444 | 68 | 457 | 71 |
| 2011 | 738 | 97 | - | - | 12 | 3 | 12 | 3 |
| 2012 | 142 | 13 | - | - | 3 | - | 3 | - |
| 2013 | 705 | 101 | 1 | - | - | - | 1 | - |
| **Total** | **106,621** | **13,116** | **341** | **51** | **20,715** | **3,217** | **21,056** | **3,268** |



*Forms an integral part of the audited financial statements

# RISK MANAGEMENT REPORT (continued)

### 6.7.6 Residential mortgage lending - index linked LTV (continued)

**Group Residential Mortgage Lending with Fair Value Collateral (continued)***

Group Vintage analysis – Residential and Impaired (continued)

| Loan Origination Profile of Residential Mortgages (before provision for impairment) | TOTAL December 2012 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Residential Mortgage Loan Book | | Loans >90 days in arrears but not impaired at year end | | Loans classified as impaired at year end | | Loans >90 days in arrears and/or impaired at year end | |
| | Number of loans | Balance €m | Number of loans | Balance €m | Number of loans | Balance €m | Number of loans | Balance €m |
| 1996 and before | 5,624 | 152 | 25 | 1 | 758 | 29 | 783 | 30 |
| 1997 | 2,080 | 68 | 4 | - | 219 | 10 | 223 | 10 |
| 1998 | 2,461 | 92 | 5 | - | 272 | 14 | 277 | 14 |
| 1999 | 3,099 | 138 | 5 | - | 373 | 26 | 378 | 26 |
| 2000 | 3,310 | 193 | 10 | - | 407 | 31 | 417 | 32 |
| 2001 | 3,552 | 266 | 10 | 1 | 496 | 47 | 506 | 47 |
| 2002 | 5,054 | 449 | 7 | 1 | 722 | 77 | 729 | 77 |
| 2003 | 6,226 | 602 | 22 | 2 | 1,049 | 124 | 1,071 | 127 |
| 2004 | 8,094 | 957 | 31 | 4 | 1,314 | 196 | 1,345 | 199 |
| 2005 | 11,850 | 1,532 | 29 | 4 | 2,109 | 350 | 2,138 | 353 |
| 2006 | 15,091 | 2,327 | 54 | 10 | 3,132 | 623 | 3,186 | 632 |
| 2007 | 14,275 | 2,300 | 55 | 10 | 3,514 | 639 | 3,569 | 651 |
| 2008 | 13,909 | 2,205 | 57 | 9 | 2,979 | 544 | 3,036 | 553 |
| 2009 | 8,403 | 1,177 | 25 | 3 | 923 | 144 | 948 | 148 |
| 2010 | 7,089 | 1,050 | 17 | 3 | 307 | 47 | 324 | 50 |
| 2011 | 757 | 106 | - | - | 11 | 3 | 11 | 3 |
| 2012 | 147 | 11 | - | - | 3 | - | 3 | - |
| **Total** | **111,021** | **13,625** | **356** | **48** | **18,588** | **2,904** | **18,944** | **2,952** |

### 6.7.7 Analysis of loans and advances to customers by contractual residual maturity and interest rate sensitivity*

The following tables analyse gross loans to customers by maturity and interest rate sensitivity. Approximately 6.5% of EBS loan portfolio is provided on a fixed rate basis. The interest rate risk exposure is managed by Global Treasury at AIB Group level within agreed policy parameters.

**Group loans and advances to customers**

| | Fixed | Variable | Total | Within 1 year | After 1 year but within 5 years | After 5 Years | Total |
|---|---|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m | €m | €m |
| **2013** | **873** | **12,504** | **13,377** | **3,370** | **219** | **9,788** | **13,377** |
| 2012 | 2,016 | 11,887 | 13,903 | 3,027 | 182 | 13,694 | 16,903 |



*Forms an integral part of the audited financial statements

## RISK MANAGEMENT REPORT (continued)

### 6.7.8 Cross-border outstandings*

Cross-border outstandings are based on the country of domicile of the borrower and comprise placings with banks and money at call and short notice, loans to customers and other monetary assets. EBS monitors geographic breakdown based on the country of the borrower and the guarantor of ultimate risk. Cross-border outstandings exceeding 1% of total assets in 2013 were Nil (2012: €184m).

### 6.7.9 Large exposures*

At 31 December 2013, EBS Group's top 50 exposures amounted to €180m, and accounted for 1.4% (€190m and 1.4% at 31 December 2012) of the on-balance sheet total gross loans and advances to customers. No single customer exposure exceeds regulatory guidelines.

### 6.7.10 Treasury assets and derivatives*

Treasury assets consist of cash and balances with CBI, central government bills and other eligible bills, derivative financial instruments, available-for-sale, held-to-maturity financial assets and loans and advances to credit institutions excluding operating bank accounts.

The following tables present an analysis of Treasury asset counterparties based on EBS' internal ratings mapped to an external rating agency scale. Where the counterparty is government guaranteed a sovereign rating has been used.

The ratings listed below are provided by Moody's, Fitch or S&P and are sourced from Bloomberg.

| | Cash & Balances with Central Bank of Ireland €m | Govt. & Other Eligible Bills €m | Other AFS Financial Assets €m | Derivatives €m | Loans & Advances to Credit Institutions €m | Commitments & Contingent Liabilities €m |
|---|---|---|---|---|---|---|
| **Group 2013** | | | | | | |
| Balances at 31 December 2013 | 74 | 214 | 3 | 120 | 1,343 | - |
| Aaa | 100% | - | - | - | 2% | - |
| Aa3 to Aa1 | - | - | - | 31% | - | - |
| A3 to A1 | - | - | - | - | 17% | - |
| Lower than A3 | - | 100% | 100% | 69% | 81% | - |
| Unrated | - | - | - | - | - | 100% |
| **Company 2013** | | | | | | |
| Balances at 31 December 2013 | 73 | 214 | 2,795 | 153 | 4,079 | - |
| Aaa | 100% | - | - | - | 1% | - |
| Aa3 to Aa1 | - | - | - | 24% | - | - |
| A3 to A1 | - | - | - | - | - | - |
| Lower than A3 | - | 100% | 100% | 76% | 99% | - |
| Unrated | - | - | - | - | - | 100% |



*Forms an integral part of the audited financial statements

# RISK MANAGEMENT REPORT (continued)

### 6.7.10 Treasury assets and derivatives (continued)*

| | Cash & Balances with Central Bank of Ireland €m | Govt. & Other Eligible Bills €m | Other AFS Financial Assets €m | Derivatives €m | Loans & Advances to Credit Institutions €m | Commitments & Contingent Liabilities €m |
|---|---|---|---|---|---|---|
| **Group 2012** | | | | | | |
| Balances at 31 December 2012 | 8 | 721 | 1,152 | 190 | 883 | 104 |
| Aaa | 100.0% | - | 22.8% | 22.9% | 2.4% | - |
| Aa3 to Aa1 | - | - | 5.2% | 49.4% | 18.1% | - |
| A3 to A1 | - | - | 17.0% | 3.3% | 6.2% | - |
| Lower than A3 | - | 100.0% | 55.0% | 24.4% | 73.3% | - |
| Unrated | - | - | - | - | - | 100.0% |
| **Company 2012** | | | | | | |
| Balances at 31 December 2012 | 8 | 721 | 4,129 | 226 | 3,906 | 80 |
| Aaa | 100.0% | - | 6.4% | 19.1% | 0.5% | - |
| Aa3 to Aa1 | - | - | 5.6% | 41.5% | 0.6% | - |
| A3 to A1 | - | - | 4.7% | 2.8% | 0.4% | - |
| Lower than A3 | - | 100.0% | 83.3% | 36.6% | 98.5% | - |
| Unrated | - | - | - | - | - | 100.0% |

EBS has put in place a number of Credit Support Annexes ('CSA') which historically covered the majority of outstanding derivatives. Derivatives covered by these agreements are marked to market on an ongoing basis resulting in the determination of the amount to be posted as collateral under the CSA and thereby removing the counterparty credit risk. The counterparty credit risk relating to the remaining derivatives not covered by CSA's were mitigated by the fact that under our counterparty credit risk policy we can only transact derivatives with counterparties who warrant a minimum rating of 4 based on the EBS internal rating based ('IRB') system if a CSA agreement is not in place.

In quarters two and three of 2013, EBS novated the vast majority of its derivative book to AIB, leaving just one external Rabobank deal, which is covered by a CSA. It is not envisaged that any future external derivative deals will be entered into by EBS, as AIB is expected to be the market facing brand going forward.

EBS has established and enforces operating limits and other practices that maintain exposures within levels consistent with their internal policies. EBS adheres to the principles of sound practices for managing interest rate risk and complies with any regulatory requirements as a minimum.

EBS transacted derivatives for the purpose of reducing or eliminating Interest Rate Risk in the Banking Book (IRRBB). EBS used interest rate, cross currency and foreign exchange swaps for this purpose. Treasury Assets are monitored on a daily basis.

Commitments and contingent liabilities include EBS' obligations to the CBI and loan commitments.

### 6.7.11 Liquidity risk*

Liquidity risk relates to the ability of the Group to meet its on and off balance sheet obligations in a timely manner as they fall due, without incurring excessive cost, whilst continuing to fund its assets and growth therein.

EBS is dependent, to a significant extent on its' parent the AIB p.l.c. for funding and liquidity support and EBS' liquidity risk has been incorporated into the AIB p.l.c. centralised risk management model in line with AIB p.l.c. common approach to Treasury Risk management. Under this centralised approach the management of liquidity and related activities are overseen and controlled by AIB Treasury.

*Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

### 6.7.11 Liquidity risk (continued)*

EBS applies the maturity mismatch approach to the management of liquidity following the adoption of this method by the CBI in July 2007. The overall purpose of a maturity mismatch approach is to ensure that the Group will have, at any given time, a pool of highly liquid assets capable of being converted into cash within four business days, sufficient to cover a certain percentage of foreseeable cash outflows for future periods of time ('time bands').

Funding contingency plans are continually under review in light of unprecedented market and EBS specific events. AIB Group conducts both regular and ad-hoc funding and liquidity risk stress testing to assess on an ongoing basis the ability of the Group to withstand various idiosyncratic and systemic stress scenarios. Liquidity contingency plans are developed and updated on a continual basis reflecting the results of the stress tests.

Key measures used for managing liquidity risk are the liquidity ratios, calculated and reported on a daily basis internally to the Treasury Front Office and to AIB Group, on a weekly basis for consolidation into the AIB Group Regulatory Liquidity reports and on a monthly basis to the EBS Management team. Any breaches of limits are escalated immediately in line with the escalation procedure.

EBS was one of the Irish institutions included in the 'CIFS' scheme which ran from September 2008 to September 2010. EBS also joined the ELG Scheme in early February 2010. EBS continues to be one of the Irish covered institutions that are part of the ELG Scheme. This scheme assisted EBS in attracting and maintaining customer funding in times of great economic uncertainty. The cost of the ELG scheme for 2013 was €47m (2012: €55m) (see note 2). On 26 February 2013, the Minister for Finance announced that the Eligible Liabilities Guarantee Scheme 2009 will end for all new liabilities with effect from midnight on 28 March 2013.

**Exposure to liquidity risk***

The following table analyses gross contractual maturities of financial liabilities including interest payable at the next interest payment date held by the Group.

**Group**

| | Up to 1 month | Over 1 month to 3 months | Over 3 months to 6 months | Over 6 months to 1 year | 1 to 2 years | Over 2 years | Total |
|---|---|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m | €m | €m |
| **31 December 2013** | | | | | | | |
| *Financial liabilities* | | | | | | | |
| Deposits by Central Bank of Ireland | 375 | - | - | - | 600 | - | 975 |
| Deposits by credit institutions | 49 | - | - | - | 69 | 547 | 665 |
| Customer accounts | 2,417 | 1,493 | 1,294 | 2,473 | 623 | 1,441 | 9,741 |
| Derivative financial instruments | 1 | - | - | - | - | - | 1 |
| Debt securities in issue | 9 | 95 | - | 75 | 1,020 | 857 | 2,056 |
| Loan commitments | 25 | 27 | 7 | - | 1 | 87 | 147 |
| **Total financial liabilities** | **2,876** | **1,615** | **1,301** | **2,548** | **2,313** | **2,932** | **13,585** |
| **31 December 2012** | | | | | | | |
| *Financial liabilities* | | | | | | | |
| Deposits by Central Bank of Ireland | 1,161 | 700 | - | - | - | 600 | 2,461 |
| Deposits by credit institutions | 180 | 58 | - | - | - | - | 238 |
| Customer accounts | 2,792 | 1,630 | 1,695 | 2,186 | 927 | 1,459 | 10,689 |
| Derivative financial instruments | 30 | 22 | 13 | 18 | 12 | 91 | 186 |
| Debt securities in issue | 32 | 83 | 24 | 7 | 139 | 1,951 | 2,236 |
| Loan commitments | 6 | 2 | 2 | 3 | 1 | 90 | 104 |
| **Total financial liabilities** | **4,201** | **2,495** | **1,734** | **2,214** | **1,079** | **4,191** | **15,914** |

*Forms an integral part of the audited financial statements*

## RISK MANAGEMENT REPORT (continued)

### 6.7.11 Liquidity risk (continued)*

**Exposure to liquidity risk (continued)***

The following table analyses gross contractual maturities of financial liabilities held by the Group:

**Company**

| | Up to 1 month | Over 1 month to 3 months | Over 3 months to 6 months | Over 6 months to 1 year | 1 to 2 years | Over 2 years | Total |
|---|---|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m | €m | €m |
| **31 December 2013** | | | | | | | |
| *Financial liabilities* | | | | | | | |
| Deposits by Central Bank of Ireland | 375 | - | - | - | 600 | - | 975 |
| Deposits by credit institutions | 63 | - | - | - | 69 | 547 | 679 |
| Customer accounts | 2,417 | 1,493 | 1,293 | 2,473 | 623 | 2,243 | 10,542 |
| Derivative financial instruments | 1 | - | - | - | - | - | 1 |
| Debt securities in issue | 9 | 94 | - | 25 | 1,020 | 55 | 1,203 |
| Loan commitments | 15 | 20 | 7 | - | 1 | 64 | 107 |
| **Total financial liabilities** | **2,880** | **1,607** | **1,300** | **2,498** | **2,313** | **2,909** | **13,507** |
| | | | | | | | |
| **31 December 2012** | | | | | | | |
| *Financial liabilities* | | | | | | | |
| Deposits by Central Bank of Ireland | 1,161 | 700 | - | - | - | 600 | 2,461 |
| Deposits by credit institutions | 237 | 58 | - | - | - | - | 295 |
| Customer accounts | 2,792 | 1,630 | 1,695 | 2,186 | 927 | 2,306 | 11,536 |
| Derivative financial instruments | 51 | 21 | 13 | 18 | 12 | 65 | 180 |
| Debt securities in issue | 32 | 83 | 24 | 7 | 89 | 1,105 | 1,340 |
| Loan commitments | 6 | 2 | 2 | 3 | 1 | 66 | 80 |
| **Total financial liabilities** | **4,279** | **2,494** | **1,734** | **2,214** | **1,029** | **4,142** | **15,892** |

The previous tables show the undiscounted cash flows (other than for derivatives) on each of the Group and EBS Limited's financial liabilities and unrecognised loan commitments on the basis of contractual maturity. Liabilities and unrecognised loan commitments, which include offers and undrawn credit facilities, are included according to the earliest possible date of obligation. The disclosure for derivatives shows a net amount as the derivatives are all net settled. The Group's expected cash flows on these instruments (other than derivatives) may vary significantly from this analysis. Liquidity is now managed centrally by AIB Group.

### 6.7.12 Market risk*

**Interest rate sensitivity gap analysis 2013**

The tables overleaf give an indication of the interest rate re-pricing mismatch in the Group's Statement of Financial Position. A cumulative net liability position in a time band indicates an exposure to a rise in interest rates.



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**6.7.12 Market risk (continued)**
**Interest rate sensitivity gap analysis 2013 (continued)***

**Group**

| | Not more than 1 month | Over 1 month but not more than 3 months | Over 3 months but not more than 12 months | Over 1 year but not more than 2 years | Over 2 years but not more than 3 years | Over 3 years but not more than 4 years | Over 4 years but not more than 5 years | Over 5 years | Non Interest Bearing | Trading | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m | €m | €m | €m | €m | €m | €m |
| **ASSETS** | | | | | | | | | | | |
| Cash and balances with Central Bank of Ireland | - | - | - | - | - | - | - | - | 74 | - | **74** |
| Loans and advances to credit institutions | 1,324 | - | - | - | - | - | - | - | 19 | - | **1,343** |
| Loans and advances to customers | 12,500 | 262 | 75 | 192 | 211 | 53 | 41 | 43 | (1,352) | - | **12,025** |
| Available-for-sale financial assets | - | - | - | - | - | - | - | 214 | 3 | - | **217** |
| NAMA senior bonds | - | - | - | - | - | - | - | - | - | - | **-** |
| Other assets | - | - | - | - | - | - | - | - | 438 | 42 | **480** |
| **Total assets** | **13,824** | **262** | **75** | **192** | **211** | **53** | **41** | **257** | **(818)** | **42** | **14,139** |
| **LIABILITIES** | | | | | | | | | | | |
| Deposits by central banks and banks | 1,640 | - | - | - | - | - | - | - | - | - | **1,640** |
| Customer accounts | 2,955 | 1,280 | 3,318 | 485 | 311 | 782 | 166 | - | - | - | **9,297** |
| Debt securities in issue | 833 | 160 | 21 | 987 | - | - | - | - | - | - | **2,001** |
| Retirement Benefit Liabilities | - | - | - | - | - | - | - | - | 37 | - | **37** |
| Other liabilities | - | - | - | - | - | - | - | - | 339 | 44 | **383** |
| Shareholders equity | - | - | - | - | - | - | - | - | 781 | - | **781** |
| **Total liabilities** | **5,428** | **1,440** | **3,339** | **1,472** | **311** | **782** | **166** | **-** | **1,157** | **44** | **14,139** |
| Derivatives affecting interest rate sensitivity | - | - | - | - | - | - | - | - | - | - | **-** |
| **Interest rate sensitivity gap** | **8,396** | **(1,178)** | **(3,264)** | **(1,280)** | **(100)** | **(729)** | **(125)** | **257** | **(1,975)** | **(2)** | |
| **Cumulative gap** | **8,396** | **7,218** | **3,954** | **2,674** | **2,574** | **1,845** | **1,720** | **1,977** | **2** | **-** | |

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**6.7.12 Market risk (continued)**
**Interest rate sensitivity gap analysis 2012*(Restated)**

**Group**

| | Not more than 1 month | Over 1 month but not more than 3 months | Over 3 months but not more than 12 months | Over 1 year but not more than 2 years | Over 2 years but not more than 3 years | Over 3 years but not more than 4 years | Over 4 years but not more than 5 years | Over 5 years | Non Interest Bearing | Trading | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m | €m | €m | €m | €m | €m | €m |
| **ASSETS** | | | | | | | | | | | |
| Cash and balances with Central Bank of Ireland | 4 | - | - | - | - | - | - | - | 4 | - | **8** |
| Loans and advances to credit institutions | 883 | - | - | - | - | - | - | - | - | - | **883** |
| Loans and advances to customers | 12,095 | 313 | 753 | 300 | 204 | 112 | 52 | 74 | (934) | - | **12,969** |
| Available-for-sale financial assets | 38 | 112 | 363 | 130 | 647 | 28 | 6 | 242 | 2 | - | **1,568** |
| NAMA senior bonds | 305 | - | - | - | - | - | - | - | - | - | **305** |
| Other assets | - | - | - | - | - | - | - | - | 521 | 63 | **584** |
| **Total assets** | **13,325** | **425** | **1,116** | **430** | **851** | **140** | **58** | **316** | **(407)** | **63** | **16,317** |
| **LIABILITIES** | | | | | | | | | | | |
| Deposits by central banks and banks | 2,628 | 70 | - | - | - | - | - | - | - | - | **2,698** |
| Customer accounts | 4,928 | 1,211 | 2,695 | 594 | 162 | 214 | 291 | 22 | - | - | **10,117** |
| Debt securities in issue | - | 48 | 31 | 99 | 1,158 | - | - | 846 | - | - | **2,182** |
| Retirement Benefit Liabilities | - | - | - | - | - | - | - | - | 62 | - | **62** |
| Other liabilities | - | - | - | - | - | - | - | - | 507 | 62 | **569** |
| Shareholders equity | - | - | - | - | - | - | - | - | 689 | - | **689** |
| **Total liabilities** | **7,556** | **1,329** | **2,726** | **693** | **1,320** | **214** | **291** | **868** | **1,258** | **62** | **16,317** |
| Derivatives affecting interest rate sensitivity | (4,051) | 929 | 1,606 | 298 | 592 | 101 | 534 | (9) | - | - | **-** |
| **Interest rate sensitivity gap** | **1,718** | **25** | **(4)** | **35** | **123** | **27** | **301** | **(561)** | **(1,665)** | **1** | **-** |
| **Cumulative gap** | **1,718** | **1,743** | **1,739** | **1,774** | **1,897** | **1,924** | **2,225** | **1,664** | **(1)** | **-** | **-** |

**Forms an integral part of the audited financial statements*

# RISK MANAGEMENT REPORT (continued)

## 6.7.12 Market risk (continued)*

**Interest rate sensitivity gap analysis 2013 (continued)***
In the tables above the assets and liabilities are allocated to time buckets based on the next re-pricing date of the individual assets and liabilities underlying the categories above.

There are some limitations associated with the above analysis, mainly due to market effects, over aggregation and run-offs. However, measures have been taken to minimise the effect of these limitations in line with industry practice and we are satisfied that the sensitivity analysis is an appropriate tool for measuring interest rate risk.

**Interest rate stress testing***
EBS historically conducted daily stress testing on the Banking Book Portfolio, evaluating the exposure of the Group and EBS to a parallel interest rate shift of 100 bps and a series of yield curve twist tests. The Group also conducts at least monthly interest rate stress testing on the Reserve Investment Portfolio, evaluating the exposure of the Group and EBS to a parallel interest rate shift of 100 bps and a series of yield curve twist tests. Stress testing methodologies are now aligned and prepared on an AIB Group basis.

The tables below provide an analysis of the EBS Group's sensitivity to an increase or decrease in market rates:

| | 100 bps parallel shift (increase / decrease) | | | |
|---|---|---|---|---|
| | | 2013 €m | | 2012 €m |
| **Banking book portfolio** | | | | |
| Average for the period | - / + | 2 | - / + | 3 |
| Maximum for the period | - / + | 8 | - / + | 7 |
| Minimum for the period | - / + | - | - / + | - |
| **Reserve investment portfolio** | | | | |
| Average for the period | - / + | 16 | - / + | 17 |
| Maximum for the period | - / + | 19 | - / + | 17 |
| Minimum for the period | - / + | 13 | - / + | 15 |

The above table shows the present value effect that would be realised in the Statement of Comprehensive Income on an accruals basis on the banking book and reserve investment book over the life of the assets and liabilities contained therein.

Overall interest rate risk positions are managed by AIB Group Treasury. The use of derivatives to manage interest rate risk is described in note 30.

**Foreign exchange risk***
The Group and EBS take the euro as their base currency. However, through the normal course of business operations, EBS naturally accumulates foreign currency positions. The Group is therefore exposed to movements in foreign exchange rates that may have an adverse effect on the economic value of the Group and EBS Limited. The size of the foreign currency open positions is kept within small operational limits.

**Group and Company**

| | 2013 | 2012 |
|---|---|---|
| ***Net of Assets and Liabilities (including derivatives) denominated in currency other than Euro:*** | | |
| Sterling | 1 | 1 |
| **Total** | **1** | **1** |

** Forms integral part of the audited financial statements*

## RISK MANAGEMENT REPORT (continued)

### 6.7.12 Market risk (continued)*

**Foreign exchange risk (continued)**
The main methods used for mitigating foreign exchange risk include prohibiting the running of a trading book in any foreign currency, monitoring and centrally managing foreign exchange risk and hedging open currency positions through the use of derivatives. The Group and EBS have no substantial net exposure to foreign exchange rate fluctuations or changes in foreign currency interest rates.

**Funding risk - credit spreads**
Funding risk (not relating to changes in the obligor / issuer's credit standing) is closely managed by Group Treasury and is monitored on an ongoing basis by the EBS Management team.

**Forms an integral part of the audited financial statements*

# INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF EBS LIMITED

We have audited the financial statements of EBS Limited for the year ended 31 December 2013 which comprise the Group Financial Statements: the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated Statement of Financial Position, the Consolidated Statement of Cash Flows, the Consolidated Statement of Changes in Shareholders' Equity, the Parent Company Financial Statements: the Company Statement of Financial Position, the Company Statement of Cash Flows, the Company Statement of Changes in Shareholders' Equity and the related notes 1 to 40. The financial reporting framework that has been applied in the preparation of the group financial statements is Irish law and IFRS as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is Irish law and IFRS as adopted by the European Union.

This report is made solely to the company's members, as a body, in accordance with Section 193 of the Companies Act, 1990. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

## Respective responsibilities of directors and auditors

As explained more fully in the Statement of Directors' Responsibilities, the directors are responsible for the preparation of the financial statements giving a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with Irish law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

## Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's and the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Directors' Report and Annual Financial Statements to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

## Opinion on financial statements

In our opinion:

- the group's financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the group's affairs as at 31 December 2013 and of its result for the year then ended;
- the parent company statement of financial position gives a true and fair view, in accordance with IFRSs, as adopted by the European Union as applied in accordance with the provisions of the Companies Acts, 1963 to 2013, of the state of the parent company's affairs as at 31 December 2013; and
- the financial statements have been properly prepared in accordance with the requirements of the Companies Acts, 1963 to 2013.

# INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF EBS LIMITED (continued)

## Matters on which we are required to report by the Companies Acts, 1963 to 2013

- We have obtained all the information and explanations which we consider necessary for the purposes of our audit.
- In our opinion proper books of accounts have been kept by the parent company.
- The parent company statement of financial position is in agreement with the books of account.
- In our opinion the information given in the directors' report is consistent with the financial statements.
- The net assets of the parent company, as stated in the parent company statement of financial position are more than half of the amount of its called up share capital and, in our opinion, on that basis there did not exist at 31 December 2013 a financial situation which under Section 40 (1) of the Companies (Amendment) Act, 1983 would require the convening of an extraordinary general meeting of the parent company.

## Matters on which we are required to report by exception

We have nothing to report in respect of the provisions in the Companies Acts, 1963 to 2013 which require us to report to you if, in our opinion the disclosures of directors' remuneration and transactions specified by law are not made.

**John McCarroll**
**For and on behalf of Deloitte & Touche**
**Chartered Accountants and Statutory Audit Firm**
**Hardwicke House**
**Hatch Street**
**Dublin 2**
**Ireland**

**13 March 2014**

# ACCOUNTING POLICIES

## 1.1 Reporting Entity

EBS Limited (the 'Company') is a company domiciled in Ireland. The address of the Company's registered office is 2 Burlington Road, Dublin 4, Ireland

The consolidated financial statements include the financial statements of EBS Limited and its subsidiary undertakings and where appropriate, certain special purpose entities. These are collectively referred to as the 'Group', and are made up to the end of the financial year. The Group is primarily involved in the provision of mortgage lending, savings, investments and insurance arrangement services to customers. The Group's immediate and ultimate parent is AIB p.l.c.

## 1.2 Statement of Compliance

The consolidated financial statements have been prepared in accordance with International Accounting Standards and IFRS as issued by the International Accounting Standards Board ('IASB') and International Financial Reporting Standards as adopted by the European Union ('EU') and applicable for the year ended 31 December 2013. The accounting policies have been consistently applied by Group entities and are consistent with the previous year, unless otherwise described. The financial statements also comply with the Companies Acts 1963 to 2013 and the European Communities (Credit Institutions: Accounts) Regulations, 1992 (as amended) and the Asset Covered Securities Acts 2001 and 2007. The EBS company financial statements have been prepared in accordance with both IFRS as issued by the IASB and IFRS Standards as adopted by the EU as applicable for the year ended 31 December 2013 and with Irish Statute. In publishing the EBS company financial statements together with the Group financial statements, EBS has taken advantage of the exemption in paragraph 2 of the European Communities (Credit Institutions: Accounts) Regulations, 1992 not to present its parent company Income Statement, Statement of Comprehensive Income and related notes that form part of these approved financial statements.

## 1.3 Basis of Preparation

### Functional and presentation currency

The financial statements are presented in euro (€), which is the functional currency of the parent company and all of its subsidiaries, rounded to the nearest million (€1m), except where otherwise indicated.

### Basis of measurement

The financial statements have been prepared under the historical cost basis, with the exception of the following assets and liabilities which are stated at their fair value: derivative financial instruments, financial instruments at fair value through profit or loss, certain hedged financial assets and financial liabilities and financial assets classified as available-for-sale.

The financial statements comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Group and Company Statements of Financial Position, the Group and Company Statements of Cash Flows, and the Group and Company Statement of Changes in Shareholders' Equity together with the related notes. These notes also include financial instrument related disclosures which are required by IFRS 7 and revised IAS 1; contained in the Risk Management Report of this Annual Financial Statements. The relevant information on those pages is identified as forming an integral part of the audited financial statements.

### Use of estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of certain assets, liabilities, revenues and expenses, and disclosures of contingent assets and liabilities. The estimates and assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Since management's judgement involves making estimates concerning the likelihood of future events, the actual results could differ from those estimates. The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future period affected. The estimates that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are in the areas of loan impairment and impairment of other financial instruments; the recoverability of deferred tax; determination of the fair value of certain financial assets and financial liabilities; and retirement benefit obligations. In addition, the designation of financial assets and financial liabilities has a significant impact on their income statement treatment and could have a significant impact on reported income.

# ACCOUNTING POLICIES (continued)

## 1.3 Basis of Preparation (continued)

**Use of estimates and judgements (continued)**
A description of these estimates and judgements is set out within Financial review - Critical accounting policies and estimates. This section is identified as forming an integral part of the audited financial statements.

Arising from the results of the Prudential Capital Assessment Review ('PCAR')/Prudential Liquidity Assessment Review ('PLAR') in March 2011, AIB is required to dispose of non-core financial assets. Accordingly, a certain number of these financial assets are classified as held for sale at 31 December 2013. These assets do not constitute a major line of business or a geographical area of operations, but are included within 'Disposal groups and non-current assets held for sale' (note 11).

## 1.4 Critical Accounting Policies and Estimates

The estimates that have a significant impact on these financial statements, and estimates with a significant risk of material adjustment in the next year, are set out below:

***(a) Going concern***

The Companys' activities are subject to risk factors as set out in the Risk Management Report. The continued financial crisis has increased these risk factors.

In making its going concern assessment, the Companys' Directors have considered the economic, political, market risks and uncertainties currently impacting Irish financial institutions, including the Group. In particular these relate to challenges in terms of liquidity, funding, and capital. The Company is dependent on the financial support from its parent, Allied Irish Banks p.l.c, to meet its capital requirements and ultimately its funding requirements. Since 1 July 2011, the Group has received the full support of AIB p.l.c. in meeting the necessary capital and funding requirements, and for the full year 2013, the Company has received the full support of AIB p.l.c. in meeting its necessary capital and funding requirements.

The financial statements have been prepared on a going concern basis on the basis of the assessment of the above mentioned risks and the commitment from AIB p.l.c. to support the funding and capital needs of the EBS Group and similarly the commitment from EBS to support the funding and capital needs of the Company. In making this assessment, the Directors have considered the basis on which AIB Group concluded that it is appropriate to prepare its own financial statements for the year ended 31 December 2013 on a going concern basis.

**Extract from the AIB p.l.c. Annual report and financial statements for the year ended 31 December 2013 (on this extract the Group refers to AIB Group)**

> **Going concern**
> The financial statements for the year ended 31 December 2013 have been prepared on a going concern basis as the Directors are satisfied, having considered the risks and uncertainties impacting the Group, that it has the ability to continue in business for the period of assessment. The period of assessment used by the Directors is twelve months from the date of approval of these annual financial statements.
>
> In making its assessment, the Directors have considered a wide range of information relating to present and future conditions. These have included financial plans covering the period 2014 to 2016 approved by the Board in December 2013, the restructuring plan submitted to the European Commission in September 2012, liquidity and funding forecasts, and capital resources projections, all of which have been prepared under base and stress scenarios. In addition, the Directors have considered the commitment of support provided to AIB by the Irish Government. The Directors have also considered the risk factors which could materially affect the Group's future business performance and profitability.
>
> Furthermore, the Directors have considered the outlook for the Irish economy, taking into account such factors as the successful exit by the Irish Government from the three-year bailout programme in December 2013 without a back-up credit line, the forecast expansion of the economy, and the forecast fall in unemployment rates in 2014. The forecast turnaround in the economy is supported by various economic indicators such as a modest growth in economic output and reduced unemployment levels together with increasing consumer confidence and a stabilisation of house prices, particularly in Dublin, during 2013.

# ACCOUNTING POLICIES (continued)

**1.4 Critical Accounting Policies and Estimates (continued)**

**Extract from the AIB p.l.c. Annual report and financial statements for the year ended 31 December 2013 (on this extract the Group refers to AIB Group) (continued)**

**Going concern (continued)**
The Directors have also considered the outlook for the Eurozone and UK economies which are slowly emerging from recession. In the EU, following the sovereign and bank debt crises, the actions taken at an EU level lead to a marked easing of the crises and improvement of conditions in Eurozone financial markets since the second half of 2012. The various support measures adopted for the euro since the beginning of 2011 and the pronouncements of the ECB demonstrate the strong commitment of EU institutions and the euro area Member States to do whatever is necessary to preserve the euro. In addition, the UK economy in which the Group has significant interests has returned to growth following a period of stagnation similar to the Eurozone.

The Irish Government, as AIB's principal shareholder, has confirmed its recognition of AIB as a 'Pillar Bank', given its key role in supporting the Irish economy. In support of this role, it has ensured that AIB has been sufficiently capitalised to meet the capital targets set by the CBI through its 2011 PCAR and PLAR assessment. The Directors have reviewed the capital and financial plans for the period of assessment, and believe that the capital resources are sufficient to ensure that the Group is adequately capitalised both in a base and stress scenario.

In relation to liquidity and funding, the Directors are satisfied, based on AIB's position as one of the two 'Pillar Banks' that in all reasonable circumstances, the required liquidity and funding from the CBI/ECB will be available to the Group during the period of assessment.

**Conclusion**
On the basis of the above, the Directors believe that it is appropriate to prepare the financial statements on a going concern basis having concluded that there are no material uncertainties related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern over the period of assessment.

**1.5 Critical Accounting Judgements and Estimates**

***(a) Loan impairment***

EBS's accounting policy for impairment of financial assets is set out in accounting policy number 1.17. Provisions for impairment on loans and receivables at 31 December 2013 represent management's best estimate of the losses incurred in the loan portfolios at the reporting date. The estimation of loan losses is inherently uncertain and depends upon many factors, including loan loss trends, portfolio grade profiles, local and international economic climates, conditions in various industries to which the Bank is exposed, and other external factors such as legal and regulatory requirements.

The management process for the identification of loans requiring provision is underpinned by a series of independent stages, including regular monitoring of credit quality and loan loss provisions by Credit and Risk Management. A quarterly assessment of provision adequacy is also considered by AIB Group Credit Committee prior to Audit Committee and Board approval being sought.

***Specific provisions***

A specific provision is made against problem loans when, in the judgement of management, the estimated repayment realisable from the obligor, including the value of any security available, is likely to fall short of the amount of principal and interest outstanding on the obligor's loan account. The amount of the specific provision made in the Bank's financial statements is intended to cover the difference between the assets' carrying value and the present value of estimated future cash flows discounted at the assets' original effective interest rates. Specific provisions are created for cases that are individually significant (i.e. above certain thresholds), and also collectively for assets that are not individually significant.

The amount of specific provision required on an individually assessed loan is highly dependent on estimates of the amount of future cash flows and their timing. Individually insignificant impaired loans are collectively evaluated for impairment. As this process is model driven, the total amount of the Bank's impairment provisions on these loans is somewhat uncertain as it may not totally reflect the impact of the prevailing market conditions.

# ACCOUNTING POLICIES (continued)

## 1.5 Critical Accounting Judgements and Estimates (continued)

***Specific provisions*** **(continued)**

Changes in the estimate of the value of security and the time it takes to receive those cash flows could have a significant effect on the amount of impairment provisions required on the income statement expense, and on the statement of changes in financial position. For example, in assessing the value of residential property held as collateral for impaired mortgage loans in Ireland, EBS uses a 'peak to trough' house price decline of 55% as a base. In certain circumstances, realisation costs of 4% to 15% are also deducted.

For larger impaired loans (individually significant) other factors such as recent transactional evidence and/or local knowledge are considered, which can result in higher discounts to collateral values. CSO statistics for December 2013 outline a 'peak to trough' decline of 46.4% for residential property nationally. If prices were to decline by a further 2% from EBS Mortgage Finance 's assumed values (resulting in a cumulative peak to trough fall of 57%) and this decline fell directly through to the collateral values of its impaired mortgage loans in Ireland, the additional impairment provision impact would be in the range of approximately €11 million to €13 million.

***Incurred but not reported provisions***

Incurred but not reported ('IBNR') provisions are also maintained to cover loans which are impaired at the reporting date and, while not specifically identified, are known from experience to be present in any portfolio of loans. IBNR provisions are maintained at levels that are deemed appropriate by management having considered: credit grading profiles and grading movements; historic loan loss rates; changes in credit management; procedures, processes and policies; levels of credit management skills; local and international economic climates; portfolio sector profiles/industry conditions; and current estimates of loss in the portfolio.

The total amount of impairment loss in the Bank's non-impaired portfolio, and therefore the adequacy of the IBNR allowance, is inherently uncertain. There may be factors in the portfolio that have not been a feature of the past and changes in credit grading profiles and grading movements may lag the change in the credit profile of the customer. In addition, current estimates of losses within the non-impaired portfolio and the period of time it takes following a loss event for an individual loan to be recognised as impaired ('emergence period'), are subject to a greater element of estimation due to the speed of change in the economies in which the Bank operates and the unprecedented market conditions. Furthermore, the potential impact of customers' attitudes to debt obligations following new Personal Insolvency legislation, which took effect in December 2013, may impact the level of impairment provisions required.

***Forbearance***

The Bank has developed a number of forbearance strategies for both short-term and long-term solutions to assist customers experiencing financial difficulties. The forbearance strategies involve modifications to contractual repayment terms in order to improve the collectability of outstanding debt, to avoid default, and where relevant, to avoid repossessions. The longer-term advanced forbearance strategies are currently in the process of being rolled to relevant residential mortgage customers in Ireland, accordingly. Where level of forbearance is significant, higher levels of judgement and estimation uncertainty are involved in determining their effects on impairment provisions. Further information on forbearance strategies is set in the 'Risk Management Report' section of these financial statements.

***(b) Deferred tax***

Deferred tax assets are recognised for unused tax losses to the extent that it is probable (defined for this purpose as more likely than not) that there will be sufficient future taxable profits against which the losses can be used. For a company with a history of recent losses, there must be convincing evidence to underpin this assessment. 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 judgements to be made about the projection of long-term future profitability because of the period over which recovery extends.

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

- absence of any expiry dates for Irish tax losses;
- non-enduring nature of the loan impairments at levels which resulted in recent years' losses;

# ACCOUNTING POLICIES (continued)

## 1.5 Critical Accounting Judgements and Estimates (continued)

***(b) Deferred tax (continued)***

- generation of operating profits before provisions in recent years; and
- return to profitability within the Bank's internal medium-term financial plan and the ability to grow profits thereafter.

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

- the potential instability in the Eurozone and global economies over an extended period; and
- recent taxation changes (including Bank Levy) and the likelihood of future developments and their impact on profitability and utilisation.

Taking account of all relevant factors, the Bank believes that it is more likely than not that it will return to profitability within the timescale of the Bank's medium-term financial plan and will achieve profits producing a sustainable market-range return on equity in the long term. In the absence of any expiry date for tax losses in Ireland, the Bank therefore believes that it is more likely than not that there will be future profits against which to use the tax losses.

The Bank has carried out an exercise to determine the likely number of years required to utilise the deferred tax, which indicates the deferred tax asset (€0.3bn) will be fully utilised within 22 years, assuming a sustainable market return on equity (8.5%) over the long term for future profitability levels in Ireland and a GDP growth in Ireland of 2.5%. Furthermore, under this scenario, it is expected that 64% of the deferred tax asset will be utilised in 15 years with 93% utilised in 20 years. In a more stressed scenario with a return on equity of 7.0% and GDP growth of 1.5%, the utilisation period increases by a further 1 year. The Group's analysis of the results of the scenario examined would not alter the basis of recognition or the current carrying value.

IAS 12 does not permit a company to apply present value discounting to its deferred tax assets or liabilities, regardless of the estimated timescales over which those assets or liabilities are projected to be realised. The Bank's deferred tax assets are projected to be realised over a long timescale, benefiting from the absence of any expiry date for Irish tax losses. As a result, the carrying value of the deferred tax assets on the statement of financial position does not reflect the economic value of those assets.

***(c) Determination of fair value of financial instruments***

The Group's accounting policy for the determination of fair value of financial instruments is set out in accounting policy number 1.18. The best evidence of fair value is quoted prices in an active market. The absence of quoted prices increases reliance on valuation techniques and requires the use of judgement in the estimation of fair value. This judgement includes but is not limited to: evaluating available market information; determining the cash flows for the instruments; identifying a risk free discount rate and applying an appropriate credit spread.

Valuation techniques that rely to a greater extent on non-observable data require a higher level of management judgement to calculate a fair value than those based wholly on observable data.

The choice of contributors, the quality of market data used for pricing, and the valuation techniques used are all subject to internal review and approval procedures. Given the uncertainty and subjective nature of valuing financial instruments at fair value, any change in these variables could give rise to the financial instruments being carried at a different valuation, with a consequent impact on shareholders' equity and, in the case of derivatives, the income statement.

***(d) Retirement benefit obligations***

The Group provides employees with post retirement benefits mainly in the form of pensions.

The Group provides a number of retirement benefit schemes, including defined benefit and defined contribution, as well as a hybrid scheme that has both defined benefit and defined contribution elements.

# ACCOUNTING POLICIES (continued)

## 1.5 Critical Accounting Judgements and Estimates (continued)

***(d) Retirement benefit obligations (continued)***

In addition, the Group contributes, according to local law in the various countries in which it operates, to governmental and other schemes which have the characteristics of defined contribution schemes. The majority of the defined benefit schemes are funded.

Full actuarial valuations of defined benefit schemes are undertaken every three years and are updated to reflect current conditions at each year-end reporting date. Scheme assets are measured at fair value and determined by using current bid prices. Scheme liabilities are measured on an actuarial basis by estimating the amount of future benefit that employees have earned for their service in current and prior periods and discounting that benefit at the market yield on a high quality corporate bond of equivalent term and currency to the liability. The calculation is performed by a qualified actuary using the projected unit credit method. The difference between the fair value of the scheme assets and the present value of the defined benefit obligation at the year-end reporting date is recognised in the statement of financial position. Schemes in surplus are shown as assets and schemes in deficit, together with unfunded schemes, are shown as liabilities. Actuarial gains and losses are recognised immediately in other comprehensive income.

Changes with regard to benefits payable to retirees which represent a constructive obligation under IAS 37 Provisions, Contingent Liabilities and Contingent Assets, are accounted for as a negative past service cost. These are recognised in the income statement.

The cost of providing defined benefit pension schemes to employees, comprising the service cost and net interest on the net defined benefit liability (asset), calculated by applying the discount rate to the net defined benefit liability (asset), is charged to the income statement within personnel expenses. Remeasurements of the net defined benefit liability (asset), comprising actuarial gains and losses and the return on scheme assets, are recognised in other comprehensive income. Amounts recognised in other comprehensive income in relation to remeasurements of the net defined benefit liability (asset) will not be reclassified to profit or loss in a subsequent period.

The Group recognises the effect of an amendment to a defined benefit scheme when the plan amendment occurs, which is when the Group introduces or withdraws a defined benefit scheme, or changes the benefits payable under existing defined benefit schemes. A curtailment is recognised when a significant reduction in the number of employees covered by a defined benefit scheme occurs. Gains or losses on plan amendments and curtailments are recognised in the income statement as a past service cost.

The costs of managing the defined benefit scheme assets are deducted from the return on scheme assets. All costs of running the defined benefit schemes are recognised in profit or loss when they are incurred.

The cost of the Group’s defined contribution schemes is charged to the income statement in the accounting period in which it is incurred. Any contributions unpaid at the year-end reporting date are included as a liability. The Group has no further obligation under these schemes once these contributions have been paid.

*Short-term employee benefits*

Short-term employee benefits, such as salaries and other benefits, are accounted for on an accruals basis over the period during which employees have provided services. Bonuses are recognised to the extent that the Group has a legal or constructive obligation to its employees that can be measured reliably. The cost of providing subsidised staff loans is charged within personnel expenses.

*Termination benefits*

Termination benefits are recognised as an expense at the earlier of when the Group can no longer withdraw the offer of those benefits and when the Group recognises costs for a restructuring under IAS 37 Provisions, Contingent Liabilities and Contingent Assets, which includes the payment of termination benefits.

For termination benefits payable as a result of an employee’s decision to accept an offer of voluntary redundancy, which is not within the scope of IAS 37 Provisions, Contingent Liabilities and Contingent Assets, the Group recognises the expense at the earlier of when the employee accepts the offer and when a restriction on the Group’s ability to withdraw the offer takes effect.

# ACCOUNTING POLICIES (continued)

### 1.6 Adoption of New Accounting Standards

The following amendments to standards have been adopted by the Group during the year ended 31 December 2013.

**Amendments to IAS 1 Presentation of Items in Other Comprehensive Income**

These amendments are effective from 1 July 2012. The amendments require companies preparing financial statements in accordance with IFRSs to group together items within other comprehensive income that may be reclassified to the profit or loss section of the income statement. The amendments also reaffirm existing requirements that items in other comprehensive income and profit or loss should be presented as either a single statement or two consecutive statements. The adoption of these amendments has resulted in a change in the presentation of other comprehensive income.

**IAS 19 Employee Benefits**

This revised standard is effective from 1 January 2013. The amendments result in significant changes to accounting for defined benefit pension plans. The revised standard eliminates the option to defer recognition of gains and losses (this option had not been adopted by AIB Group in the past). Actuarial gains and losses are now required to be recognised in other comprehensive income and are excluded permanently from profit or loss. The expected return and the interest cost are replaced by recording net interest in profit or loss. Net interest is calculated using the discount rate used to measure the pension obligation. Unvested past service costs can no longer be deferred and recognised over the future vesting period. Instead, all past service costs will be recognised at the earlier of when the amendment/curtailment occurs and when the entity recognises related restructuring or termination costs. The impact of the restatement is detailed in note 37.

**Consolidation standards**

**IFRS 10 Consolidated Financial Statements**

This standard, which is effective from 1 January 2013, replaces the consolidation guidance in IAS 27 Consolidated and Separate Financial Statements, and SIC-12 Consolidation – Special Purpose Entities. It introduces a single consolidation model for all entities based on control, irrespective of the nature of the investee. IFRS 10 builds on the existing principles by identifying the concept of control as the determining factor in which an entity should be included within the consolidated financial statements of the parent company. The adoption of this standard did not have a significant impact on the financial position or performance of the Group.

**IFRS 11 Joint Arrangements**

This standard is effective from 1 January 2013. IFRS 11 introduces new accounting requirements for joint arrangements, replacing IAS 31 Interests in Joint Ventures, by focusing on the rights and obligations of the arrangement, rather than its legal form. The option to apply the proportional consolidation method when accounting for jointly controlled entities is removed. The adoption of this standard did not have any impact on the financial position or performance of the Group.

**IFRS 12 Disclosure of Interests in Other Entities**

This standard which is effective from 1 January 2013 sets out the required disclosures for entities reporting under the two new standards, IFRS 10 Consolidated Financial Statements, and IFRS 11 Joint Arrangements. It also replaces the disclosure requirements in IAS 28 Investments in Associates and Joint Ventures. The required disclosures aim to provide information to enable users to evaluate the nature of, and risks associated with, an entity's interests in other entities and the effects of those interests on the entity's financial position, financial performance and cash flows. This basic principle is further supported by more detailed disclosure objectives and requirements. This new standard impacts the disclosures required for the Group's subsidiaries and associates, as well as unconsolidated structured entities.

**IAS 27 Separate Financial Statements (revised 2011)**

The revised standard is effective from 1 January 2013. The requirements relating to separate financial statements are unchanged and are included in the revised IAS 27. The other sections of IAS 27 are replaced by IFRS 10 Consolidated Financial Statements. IAS 27 is renamed 'Separate Financial Statements' and is now a standard dealing solely with separate financial statements. The existing guidance and disclosure requirements for separate financial statements are unchanged. The adoption of this standard has not had an impact on Group reporting.

# ACCOUNTING POLICIES (continued)

## 1.6 Adoption of New Accounting Standards (continued)

**IAS 28 Investments in Associates and Joint Ventures (revised 2011)**
This standard which is effective from 1 January 2013 prescribes the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures. IAS 28 (revised 2011) does not include any disclosure requirements; these are now included in IFRS 12 Disclosure of Interests in Other Entities. The adoption of this standard did not have any impact on the financial position or performance of the Group.

**IFRS 13 Fair Value Measurement**
This standard which is effective from 1 January 2013 establishes a single source of guidance for fair value measurements under IFRSs. IFRS 13 defines fair value, provides guidance on its determination and introduces consistent requirements for disclosures on fair value measurements. The standard requires entities to disclose information about the valuation techniques and inputs used to measure fair value, as well as information about the uncertainty inherent in fair value measurements. This information is required for both financial and non-financial assets and liabilities. The adoption of this standard has resulted in additional disclosures.

Other amendments, resulting from improvements to IFRSs which the Group adopted in 2013, did not have any impact on the accounting policies, financial position or performance of the Group.

**Changes to accounting policies**
Arising from the adoption of the IFRSs set out above, the following accounting policies were revised effective from 1 January 2013:

- Basis of consolidation
- Employee benefits
- Determination of fair value of financial instruments
- Non-current assets held for sale and discontinued operations

## 1.7 Basis of Consolidation

*Subsidiary undertakings*
A subsidiary undertaking is an investee controlled by the Group. The Group controls an investee when it has power over the investee, is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Subsidiaries are consolidated in the Group's financial statements from the date on which control commences until the date that control ceases.

The Group reassesses whether it controls a subsidiary when facts and circumstances indicate that there are changes to one or more elements of control.

*Loss of control*
If the Group loses control of a subsidiary, the Group:

- derecognises the assets (including any goodwill) and liabilities of the former subsidiary at their carrying amounts at the date control is lost;
- derecognises the carrying amount of any non-controlling interests in the former subsidiary at the date control is lost (including any attributable amounts in other comprehensive income);
- recognises the fair value of any consideration received and any distribution of shares of the subsidiary;
- recognises any investment retained in the former subsidiary at its fair value at the date when control is lost; and
- recognises any resulting difference of the above items as a gain or loss in the income statement.

The Group subsequently accounts for any investment retained in the former subsidiary in accordance with IAS 39 Financial Instruments: Recognition and Measurement, or when appropriate, IAS 28 Investments in Associates and Joint Ventures.

*Structured entities*
A structured entity is an entity designed so that its activities are not governed by way of voting rights. The Group assesses whether it has control over such an entity by considering factors such as the purpose and design of the entity; the nature of its relationship with the entity; and the size of its exposure to the variability of returns of the entity.

# ACCOUNTING POLICIES (continued)

## 1.7 Basis of Consolidation (continued)

*Business combinations*
The Group accounts for the acquisition of businesses using the acquisition method except for those businesses under common control. Under the acquisition method, the consideration transferred in a business combination is measured at fair value, which is calculated as the sum of:
– the acquisition date fair value of assets transferred by the Group;
– liabilities incurred by the Group to the former owners of the acquiree; and
– the equity interests issued by the Group in exchange for control of the acquiree.

Acquisition related costs are recognised in the Income Statement as incurred.

Goodwill is measured as the excess of the sum of:
– the fair value of the consideration transferred;
– the amount of any non-controlling interests in the acquiree; and
– the fair value of the acquirer's previously held equity interest in the acquiree, if any; less
– the net of the acquisition date fair value of the identifiable assets acquired and liabilities assumed.

The Group commonly acts as trustee and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. These assets, and income arising thereon, are excluded from the financial statements, as they are not assets of the Group.

*Non-controlling interests*
For each business combination, the Group recognises any non-controlling interest in the acquiree either:
– at fair value; or
– at their proportionate share of the acquiree's identifiable net assets.

For changes in the Group's interest in a subsidiary that do not result in a loss of control, the Group adjusts the carrying amounts of the controlling and non-controlling interests to reflect the changes in their relative interests in the subsidiary. The difference between the change in value of the non-controlling interest and the fair value of the consideration paid or received is recognised directly in equity and attributed to the equity holders of the parent.

*Common control transactions*
The Group accounts for the acquisition of businesses or investments in subsidiary undertakings between members of the Group at carrying value at the date of the transaction unless prohibited by company law or IFRS. This policy also applies to the acquisition of businesses by the Group of other entities under the common control of the Irish Government. Where the carrying value of the acquired net assets exceeds the fair value of the consideration paid, the excess is accounted for as a capital contribution. On impairment of the subsidiary in the parent company's separate financial statements, an amount equal to the impairment charge net of tax in the Income Statement is transferred from capital contribution reserves to revenue reserves. The entire capital contribution is transferred to revenue reserves on final sale of the subsidiary.

For acquisitions under common control, comparative data is not restated. The consolidation of the acquired entity is effective from the acquisition date, with intercompany balances eliminated at a Group level on this date.

*Associated undertakings*
An associated undertaking is an entity over which the Group has significant influence, but not control, over the entity's operating and financial policy decisions. If the Group holds 20% or more of the voting power of an entity, it is presumed that the Group has significant influence, unless it is clearly demonstrable that this is not the case.

Investments in associated undertakings are initially recorded at cost and increased (or decreased) each year by the Group's share of the post acquisition net income (or loss), and other movements reflected directly in Other Comprehensive Income of the associated undertaking.

Goodwill arising on the acquisition of an associated undertaking is included in the carrying amount of the investment. When the Group's share of losses in an associate has reduced the carrying amount to zero, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations to make payments on behalf of the associate.

# ACCOUNTING POLICIES (continued)

## 1.7 Basis of Consolidation (continued)

*Associated undertakings* (continued)
Where the Group continues to hold more than 20% of the voting power in an investment but ceases to have significant influence, the investment is no longer accounted for as an associate.

On the loss of significant influence, the Group measures the investment at fair value recognises any difference between the carrying value and fair value in profit or loss, and accounts for the investment in accordance with IAS 39 Financial Instruments: Recognition and Measurement.

The Group's share of the results of associated undertakings after tax reflects the Group's proportionate interest in the associated undertaking and is based on financial statements made up to a date not earlier than three months before the period end reporting date, adjusted to conform with the accounting policies of the Group.

Since goodwill that forms part of the carrying amount of the investment in an associate is not recognised separately, it is therefore not tested for impairment separately. Instead, the entire amount of the investment in an associate is tested for impairment as a single asset when there is objective evidence that the investment in an associate may be impaired.

*Transactions eliminated on consolidation*
Intra-group balances and any unrealised income and expenses, arising from intra-group transactions are eliminated on consolidation. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment. Unrealised gains and losses on transactions with associated undertakings are eliminated to the extent of the Group's interest in the investees.

Consistent accounting policies are applied throughout the Group for the purposes of consolidation.

## 1.8 Foreign Currency Translation

Items included in the financial statements of each of the Group's entities are measured using their functional currency, being the currency of the primary economic environment in which the entity operates.

*Transactions and balances*
Foreign currency transactions are translated into the respective entity's functional currency using the exchange rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate prevailing at the period end. Foreign exchange gains and losses resulting from the settlement of such transactions and from the retranslation at period end exchange rates of the amortised cost of monetary assets and liabilities denominated in foreign currencies are recognised in the Income Statement.

## 1.9 Interest Income and Expense Recognition

Interest income and expense is recognised in the income statement for all interest-bearing financial instruments using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period. The relevant period is assessed on an annual basis and resulting changes are charged / credited to the income statement. The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial instrument to the net carrying amount of the financial asset or financial liability. The application of the method has the effect of recognising income on the instrument evenly in proportion to the amount outstanding over the period to maturity or repayment.

In calculating the effective interest rate, the Group estimates cash flows (using projections based on its experience of customers' behaviour) considering all contractual terms of the financial instrument but excluding future credit losses. The calculation takes into account all fees, including those for early redemption, and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums and discounts.

All costs associated with mortgage incentive schemes are included in the effective interest rate calculation. Fees and commissions payable to third parties in connection with lending arrangements, where these are direct and incremental costs related to the issue of a financial instrument, are included in interest income as part of the effective interest rate.

## ACCOUNTING POLICIES (continued)

### 1.9 Interest Income and Expense Recognition (continued)

Interest income and expense presented in the Income Statement includes:

- Interest on financial assets and financial liabilities at amortised cost on an effective interest method;
- Interest on financial investments available-for-sale on an effective interest method;
- Net interest income and expense on qualifying hedge derivatives designated as cash flow hedges or fair value hedges which are recognised in interest income or interest expense; and
- Interest income and funding costs of trading portfolio financial assets, excluding dividends on equity shares.

### 1.10 Fee and Commission Income

Fees and commissions are generally recognised on an accruals basis when the service has been provided, unless they have been included in the effective interest rate calculation.

Portfolio and other management advisory and service fees are recognised based on the applicable service contracts. Asset management fees relating to investment funds are recognised over the period the service is provided.

### 1.11 Net Trading Income

Net trading income comprises gains less losses relating to trading assets and trading liabilities and includes all realised and unrealised fair value changes.

### 1.12 Operating Leases

Payments made under operating leases are recognised in the Income Statement on a straight line basis over the term of the lease. Lease incentives received and premiums paid at inception of the lease are recognised as an integral part of the total lease expense over the term of the lease.

### 1.13 Employee Benefits

*Retirement benefit obligations*

The Group provides employees with post retirement benefits mainly in the form of pensions. The Group provides a number of retirement benefit schemes, including defined benefit and defined contribution as well as a hybrid scheme that has both defined benefit and defined contribution elements. In addition, the Group contributes, according to local law in the various countries in which it operates, to governmental and other schemes which have the characteristics of defined contribution schemes. The majority of the defined benefit schemes are funded.

Full actuarial valuations of defined benefit schemes are undertaken every three years and are updated to reflect current conditions at each year-end reporting date. Scheme assets are measured at fair value determined by using current bid prices. Scheme liabilities are measured on an actuarial basis by estimating the amount of future benefit that employees have earned for their service in current and prior periods and discounting that benefit at the market yield on a high quality corporate bond of equivalent term and currency to the liability. The calculation is performed by a qualified actuary using the projected unit credit method. The difference between the fair value of the scheme assets and the present value of the defined benefit obligation at the year-end reporting date is recognised in the Statement of Financial Position. Schemes in surplus are shown as assets and schemes in deficit, together with unfunded schemes, are shown as liabilities. Actuarial gains and losses are recognised immediately in Other Comprehensive Income.

Changes with regard to benefits payable to retirees which represent a constructive obligation under IAS 37 Provisions, Contingent Liabilities and Contingent Assets are accounted for as a negative past service cost. These are recognised in the Income Statement.

The cost of providing defined benefit pension schemes to employees, comprising the service cost and net interest on the net defined benefit liability (asset), calculated by applying the discount rate to the net defined benefit liability (asset), is charged to the Income Statement within personnel expenses. Remeasurements of the net defined benefit liability (asset), comprising actuarial gains and losses and the return on scheme assets are recognised in Other Comprehensive Income. Amounts recognised in other comprehensive income in relation to remeasurements of the net defined benefit liability (asset) will not be reclassified to profit or loss in a subsequent period.

The Group recognises the effect of an amendment to a defined benefit scheme when the plan amendment occurs, which is when the Group introduces or withdraws a defined benefit scheme, or changes the benefits payable under existing defined benefit schemes.

## ACCOUNTING POLICIES (continued)

### 1.13 Employee Benefits (continued)

*Retirement benefit obligations (continued)*
A curtailment is recognised when a significant reduction in the number of employees covered by a defined benefit scheme occurs. Gains or losses on plan amendments and curtailments are recognised in the Income Statement as a past service cost.

The costs of managing the defined benefit scheme assets are deducted from the return on scheme assets. All costs of running the defined benefit schemes are recognised in profit or loss when they are incurred.

The cost of the Group's defined contribution schemes is charged to the Income Statement in the accounting period in which it is incurred. Any contributions unpaid at the year-end reporting date are included as a liability. The Group has no further obligation under these schemes once these contributions have been paid.

*Short-term employee benefits*
Short-term employee benefits, such as salaries and other benefits, are accounted for on an accruals basis over the period during which employees have provided services. Bonuses are recognised to the extent that the Group has a legal or constructive obligation to its employees that can be measured reliably. The cost of providing subsidised staff loans is charged within personnel expenses.

*Termination benefits*
Termination benefits are recognised as an expense at the earlier of when the Group can no longer withdraw the offer of those benefits and when the Group recognises costs for a restructuring under IAS 37 Provisions, Contingent Liabilities and Contingent Assets, which includes the payment of termination benefits.

For termination benefits payable as a result of an employee's decision to accept an offer of voluntary redundancy, which is not within the scope of IAS 37 Provisions, Contingent Liabilities and Contingent Assets, the Group recognises the expense at the earlier of when the employee accepts the offer and when a restriction on the Group's ability to withdraw the offer takes effect.

### 1.14 Non-credit Risk Provisions
Provisions are recognised for present legal or constructive obligations arising as consequences of past events where it is probable that a transfer of economic benefit will be necessary to settle the obligation, and it can be reliably estimated.

When the effect is material, provisions are determined by discounting expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Payments are deducted from the present value of the provision and interest, at the relevant discount rate, is charged annually to interest expense using the effective interest method. Changes in the present value of the liability as a result of movements in interest rates are included in other financial income. The present value of provisions is included in other liabilities.

When a leasehold property ceases to be used in the business, a provision is made where the unavoidable costs of future obligations relating to the lease are expected to exceed anticipated income. The provision is calculated using market rates of interest to reflect the long-term nature of the cash flows. Before the provision is established, the Group recognises any impairment loss on the assets associated with the lease contract.

*Legal claims and other contingencies*
Provisions are made for legal claims where the Group has present legal or constructive obligations as a result of past events and it is more likely than not that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated.

Contingent liabilities are possible obligations whose existence will be confirmed only by the occurrence of uncertain future events or present obligations where the transfer of economic benefit is uncertain or cannot be reliably estimated. Contingent liabilities are not recognised but are disclosed in the notes to the financial statements unless the possibility of the transfer of economic benefit is remote.

A provision is recognised for a constructive obligation where a past event has led to an obligating event. This obligating event has left the Group with little realistic alternative but to settle the obligation and the Group has created a valid expectation in other parties that it will discharge the obligation.

# ACCOUNTING POLICIES (continued)

**1.15 Income Tax, including Deferred Income Tax**

Income tax comprises of current and deferred tax. Income tax is recognised in the Income Statement except to the extent that it relates to items recognised in Other Comprehensive Income, in which case it is recognised in Other Comprehensive Income. Income tax relating to items in equity is recognised directly in equity.

Current tax is the expected tax payable on the taxable income for the year using tax rates enacted or substantively enacted at the reporting date and any adjustment to tax payable in respect of previous years.

Deferred income tax is provided, using the financial statement liability method, on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred income tax is determined using tax rates based on legislation enacted or substantively enacted at the reporting date and expected to apply when the deferred tax asset is realised or the deferred tax liability is settled. Deferred income tax assets are recognised when it is probable that future taxable profits will be available against which the temporary differences will be utilised.

The tax effects of income tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

Deferred and current tax assets and liabilities are only offset when they arise in the same tax reporting group and where there is both the legal right and the intention to settle the current tax assets and liabilities on a net basis or to realise the asset and settle the liability simultaneously.

The principal temporary differences arise from losses forward and also depreciation of property, plant and equipment, revaluation of certain financial assets and financial liabilities including derivative contracts, provisions for pensions and other post retirement benefits, and in relation to acquisitions, on the difference between the fair values of the net assets acquired and their tax base.

Deferred income tax is provided on temporary differences arising from investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the difference will not reverse in the foreseeable future. In addition, temporary differences are not provided for assets and liabilities, the initial recognition of which affects neither accounting nor taxable profit. Income tax payable on profits, based on the applicable tax law in each jurisdiction, is recognised as an expense in the period in which the profits arise.

**1.16 Impairment of Property, Plant and Equipment and Intangible Assets**

Annually, or more frequently where events or changes in circumstances dictate, property, plant and equipment and intangible assets are assessed for indications of impairment. If indications are present, these assets are subject to an impairment review.

Intangible assets not yet available for use are subject to an annual impairment review. The impairment review comprises a comparison of the carrying amount of the asset or cash generating unit with its recoverable amount. Cash generating units are the lowest level at which management monitors the return on investment in assets. The recoverable amount is determined as the higher of fair value less costs to sell of the asset or cash generating unit and its value in use. Fair value less costs to sell is calculated by reference to the amount at which the asset could be disposed of in an arms length transaction evidenced by an active market or recent transactions for similar assets.

Value in use is calculated by discounting the expected future cash flows obtainable as a result of the asset's continued use, including those resulting from its ultimate disposal, at a market-based discount rate on a pre-tax basis. For intangible assets not yet available for use, the impairment review takes into account the cash flows required to bring the asset into use.

The carrying values of property, plant and equipment and intangible assets are written down by the amount of any impairment and this loss is recognised in the Income Statement in the period in which it occurs. A previously recognised impairment loss relating to a fixed asset may be reversed in part or in full when there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the asset’s recoverable amount. The carrying amount of the asset will only be increased up to the amount that it would have been had the original impairment not been recognised.

# ACCOUNTING POLICIES (continued)

**1.17 Impairment of Financial Assets**

It is Group policy to make provisions for impairment of financial assets to reflect the losses inherent in those assets at the reporting date.

*Impairment*

The Group assesses at each reporting date whether there is objective evidence that a financial asset or a portfolio of financial assets are impaired. A financial asset, or portfolio of financial assets, are impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of the asset and on or before the reporting date ('a loss event'), and that loss event or events has had an impact such that the estimated present value of future cash flows is less than the current carrying value of the financial asset, or portfolio of financial assets.

Objective evidence that a financial asset, or a portfolio of financial assets, are impaired includes observable data that comes to the attention of the Group about the following loss events:

a) significant financial difficulty of the issuer or obligor;
b) a breach of contract, such as a default or delinquency in interest or principal payments;
c) the granting to the borrower of a concession, for economic or legal reasons relating to the borrower's financial difficulty that the Group would not otherwise consider;
d) it becomes probable that the borrower will enter bankruptcy or other financial reorganisation;
e) the disappearance of an active market for that financial asset because of financial difficulties; or
f) observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio, including:
   i. adverse changes in the payment status of borrowers in the portfolio; and
   ii. national or local economic conditions that correlate with defaults on the assets in the portfolio.

*Incurred but not reported*

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and collectively for financial assets that are not individually significant (i.e. individually insignificant). If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset under the collective incurred but not reported ('IBNR') assessment. A collective impairment provision represents an interim step pending the identification of impairment losses on an individual asset in a group of financial assets. As soon as information is available that specifically identifies losses on individually impaired assets in a group, those assets are removed from the group. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

*Collective evaluation of impairment*

For the purpose of collective evaluation of impairment (individually insignificant impaired assets and collective), financial assets are grouped on the basis of similar risk characteristics. These characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the counterparty's ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future repayment behaviour for a group of financial assets that are collectively evaluated for impairment is assessed on the basis of the historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist.

The methodology and assumptions used for estimating repayment behaviour and loss are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

*Impairment loss*

For loans and advances and assets held to maturity, the amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The amount of the loss is recognised using an allowance account and is included in the income statement.

Following impairment, interest income is recognised using the original effective rate of interest which was used to discount the future cash flows for the purpose of measuring the impairment loss.

# ACCOUNTING POLICIES (continued)

## 1.17 Impairment of Financial Assets (continued)

*Impairment loss (continued)*
If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the Income Statement.

When a loan has been subjected to a specific provision and the prospects of recovery do not improve, a time will come when it may be concluded that there is no real prospect of recovery. When this point is reached, the amount of the loan which is considered to be beyond the prospect of recovery is written off against the related provision for loan impairment. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the Income Statement.

*Collateralised financial assets – Repossessions*
The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure, costs for obtaining and settling the collateral, and whether or not foreclosure is probable.

For loans which are impaired, the Group may repossess collateral previously pledged as security in order to achieve an orderly realisation of the loan. AIB will then offer this repossessed collateral for sale. However, if the Group believes the proceeds of the sale will comprise only part of the recoverable amount of the loan with the customer remaining liable for any outstanding balance, the loan continues to be recognised and the repossessed asset is not recognised.

However, if the Group believes that the sale proceeds of the asset will comprise all or substantially all of the recoverable amount of the loan, the loan is derecognised and the acquired asset is accounted for in accordance with the applicable accounting standard. Any further impairment of the repossessed asset is treated as an impairment of the relevant asset and not as an impairment of the original loan.

**Loans renegotiated and forbearance**
From time to time, the Bank will modify the original terms of a customer’s loan either as part of the on-going relationship with the customer or arising from changes in the customer’s circumstances such that he is unable to make the agreed original contractual repayments.

**Forbearance**
A forbearance agreement is entered into where the customer is in financial difficulty to the extent that they are unable to repay both the principal and interest on their loan in accordance with their original contract. Following an assessment of the customer’s repayment capacity, a potential solution will be determined from the options available. A request for a forbearance solution acts as a trigger for an impairment test under IAS 39 as it may confirm that a loss event has occurred. There are a number of different types of forbearance options including interest and/or arrears capitalisation, interest rate adjustments, payment holidays, term extensions and equity swaps. These are detailed in the Credit Risk section 6.7.2.

All loans that are assessed for a forbearance solution are tested for impairment under IAS 39 and where a loan is deemed impaired, an appropriate provision is raised to cover the difference between the loan’s carrying value and the present value of estimated future cash flows discounted at the loan’s original effective interest rate. Where, having assessed the loan for impairment and the loan is not deemed to be impaired, it is included within the collective assessment as part of the IBNR provision calculation.

Forbearance loans classified as impaired may be upgraded from impaired status to performing status where the borrower displays a satisfactory performance following the period of restructure of the loan, comprising a minimum period of twelve months consecutive payments of the new contractually agreed terms, typically being full principal and interest. The upgrade is subject to a satisfactory assessment by the appropriate credit authority as to the borrower’s continuing ability and willingness to repay and confirmation that the relevant security held by the Bank continues to be enforceable. Where loans are upgraded from impaired, they are included in the Bank’s collective assessment for impairment provisioning (IBNR).

# ACCOUNTING POLICIES (continued)

## 1.17 Impairment of Financial Assets (continued)

**Forbearance (continued)**
Where the terms on a renegotiated loan which has been subject to an impairment provision differ substantially from the original loan terms either in a quantitative or qualitative analysis, the original loan is derecognised and a new loan is recognised at fair value. Any difference between the carrying amount of the loan and the fair value of the new renegotiated loan terms is recognised as an additional impairment provision. Interest accrues on the new loan based on the current market rates.

Where a loan has been subject to an impairment provision and the renegotiation leads to a customer granting equity to the Bank in exchange for any loan balance outstanding, the new instrument is recognised at fair value with any difference to the loan carrying amount recognised in the income statement as a further impairment.

**Non-forbearance renegotiation**
Occasionally, the Bank may temporarily amend the contractual repayments term on a loan (e.g. payment moratorium) for a short period of time due to a temporary change in the life circumstances of the borrower.

Because such events are not directly linked to repayment capacity, these amendments are not considered forbearance. The changes in expected cash flows are accounted for under IAS 39.AG8 i.e. the carrying amount of the loan is adjusted to reflect the revised estimated cash flows which are discounted at the original effective interest rate. Any adjustment to the carrying amount of the loan is reflected in the Income Statement.

Where the terms on a renegotiated loan differ substantially from the original loan terms, either in a quantitative or qualitative analysis, the original loan is derecognised and a new loan is recognised at fair value. Any difference arising between the derecognised loan and the new loan is recognised in the Income Statement.

Where a customer’s request for a modification to the original loan agreement is deemed not to be a forbearance request (i.e. the customer is not in financial difficulty to the extent that they are unable to repay both the principal and interest), these loans are not disaggregated for monitoring/reporting of IBNR assessment purposes.

*Past due loans*
When a borrower fails to make a contractually due payment, a loan is deemed to be past due. ‘Past due days’ is a term used to describe the cumulative numbers of days that a missed payment is overdue. Past due days commence from the close of business on the day on which a payment is due but not received. In the case of overdrafts, past due days are counted once a borrower:

- has breached an advised limit;
- has been advised of a limit lower than the then current outstandings; or
- has drawn credit without authorisation.

When a borrower is past due, the entire exposure is reported as past due, rather than the amount of any excess or arrears.

*Loans and advances renegotiated*
Loans and advances renegotiated are those facilities outstanding at the reporting date that, during the financial year have had their terms renegotiated, resulting in an upgrade from 90+ days past due or impaired status to performing status.

Where possible, the Group seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan’s original effective interest rate.

*Financial investments available-for-sale*
In the case of equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether impairment exists. Where such evidence exists, the cumulative net loss that had previously been recognised in Other Comprehensive Income is recognised in the Income Statement as a reclassification adjustment. Reversals of impairment of equity securities are not recognised in the Income Statement and increases in the fair value of equity securities after impairment are recognised in Other Comprehensive Income.

# ACCOUNTING POLICIES (continued)

### 1.17 Impairment of Financial Assets (continued)

In the case of debt securities classified as available-for-sale, impairment is assessed on the same criteria as for all other financial assets. Impairment is recognised by transferring the cumulative loss that has been recognised directly in Other Comprehensive Income to the Income Statement. Any subsequent increase in the fair value of an available-for-sale debt security is included in Other Comprehensive Income unless the increase in fair value can be objectively related to an event that occurred after the impairment was recognised in the Income Statement, in which case the impairment loss or part thereof is reversed.

### 1.18 Determination of Fair Value of Financial Instruments

The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Group has access at that date. The Group considers the impact of non-performance risk when valuing its financial liabilities.

Financial instruments are initially recognised at fair value and, with the exception of financial assets at fair value through profit or loss, the initial carrying amount is adjusted for direct and incremental transaction costs. In the normal course of business, the fair value on initial recognition is the transaction price (fair value of consideration given or received).

If the Group determines that the fair value at initial recognition differs from the transaction price and the fair value is determined by a quoted price in an active market for the same financial instrument, or by a valuation technique which uses only observable market inputs, the difference between the fair value at initial recognition and the transaction price is recognised as a gain or loss. If the fair value is calculated by a valuation technique that features significant market inputs that are not observable, the difference between the fair value at initial recognition and the transaction price is deferred. Subsequently, the difference is recognised in the Income Statement on an appropriate basis over the life of the financial instrument, but no later than when the valuation is supported by wholly observable inputs; the transaction matures; or is closed out.

Subsequent to initial recognition, the methods used to determine the fair value of financial instruments include quoted prices in active markets where those prices are considered to represent actual and regularly occurring market transactions. Where quoted prices are not available or are unreliable because of market inactivity, fair values are determined using valuation techniques. These valuation techniques maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The valuation techniques used incorporate the factors that market participants would take into account in pricing a transaction.

Valuation techniques include the use of recent orderly transactions between market participants, reference to other similar instruments, option pricing models, discounted cash flow analysis and other valuation techniques commonly used by market participants.

*Quoted prices in active markets*
Quoted market prices are used where those prices are considered to represent actual and regularly occurring market transactions on an arm’s length basis, in active markets.

Valuations for negotiable instruments, such as debt and equity securities, are determined using bid prices for asset positions and offer prices for liability positions. Where securities are traded on an exchange, the fair value is based on prices from the exchange. The market for debt securities largely operates on an ‘over the counter’ basis which means that there is not an official clearing or exchange price for these security instruments. Therefore, market makers and/or investment banks (‘contributors’) publish bid and offer levels which reflect an indicative price that they are prepared to buy and sell a particular security. The Group’s valuation policy requires that the prices used in determining the fair value of securities quoted in active markets must be sourced from established market makers and/or investment banks.

*Valuation techniques*
In the absence of quoted market prices, or in the case of over-the-counter derivatives, fair value is calculated using valuation techniques. Fair value may be estimated using quoted market prices for similar instruments, adjusted for differences between the quoted instrument and the instrument being valued. Where the fair value is calculated using discounted cash flow analysis, the methodology is to use, to the extent possible, market data that is either directly observable or is implied from instrument prices, such as interest rate yield curves, equities and commodities prices, credit spreads, option volatilities and currency rates. In addition, the Group considers the impact of own credit risk when valuing its derivative liabilities.

# ACCOUNTING POLICIES (continued)

### 1.18 Determination of Fair Value of Financial Instruments (continued)

*Valuation techniques (continued)*
The valuation methodology is to calculate the expected cash flows under the terms of each specific contract and then discount these values back to a present value. The assumptions involved in these valuation techniques include:

- The likelihood and expected timing of future cash flows of the instrument. These cash flows are generally governed by the terms of the instrument, although management judgement may be required when the ability of the counterparty to service the instrument in accordance with the contractual terms is in doubt. In addition, future cash flows may also be sensitive to the occurrence of future events, including changes in market rates; and
- Selecting an appropriate discount rate for the instrument, based on the interest rate yield curves including the determination of an appropriate spread for the instrument over the risk-free rate. The spread is adjusted to take into account the specific credit risk profile of the exposure.

All adjustments in the calculation of the present value of future cash flows are based on factors market participants would take into account in pricing the financial instrument.

Certain financial instruments (both assets and liabilities) may be valued on the basis of valuation techniques that feature one or more significant market inputs that are not observable. When applying a valuation technique with unobservable data, estimates are made to reflect uncertainties in fair values resulting from a lack of market data, for example, as a result of illiquidity in the market. For these instruments, the fair value measurement is less reliable. Inputs into valuations based on non-observable data are inherently uncertain because there is little or no current market data available from which to determine the level at which an orderly transaction between market participants would occur under current market conditions.

However, in most cases there is some market data available on which to base a determination of fair value, for example historical data, and the fair values of most financial instruments will be based on some market observable inputs even where the non-observable inputs are significant. All unobservable inputs used in valuation techniques reflect assumptions market participants would use when fair valuing the financial instruments.

The Group tests the outputs of the model to ensure that it reflects current market conditions. The calculation of fair value for any financial instrument may require adjustment of the quoted price or the valuation technique output to reflect the cost of credit risk, the liquidity of the market, if market participants would include one, where these are not embedded in underlying valuation techniques or prices used.

The choice of contributors, the quality of market data used for pricing, and the valuation techniques used are all subject to internal review and approval procedures.

*Transfers between levels of the fair value hierarchy*
The Group recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change occurred.

### 1.19 NAMA Senior Bonds Designation and Valuation

NAMA senior bonds were received as consideration for financial assets transferred to NAMA and also as part of the ‘Anglo’ and ‘EBS’ transactions (notes 8 and 12 to the financial statements). These bonds are designated as loans and receivables and are separately disclosed in the statement of financial position as ‘NAMA senior bonds’.

The bases for measurement, interest recognition and impairment are the same as those for loans and receivables (see accounting policy numbers 1.9, 1.17 and 1.20).

At initial recognition, the bonds were measured at fair value. The bonds carry a guarantee of the Irish Government, however, they are not marketable instruments. The only secondary market activity in the instruments is their sale and repurchase (‘repo’) to the ECB within the regular Eurosystem open market operations. The bonds are not traded in the market and there are no comparable bonds trading in the market.

The fair value on initial recognition was determined using a valuation technique. The absence of quoted prices in an active market required increased use of management judgement in the estimation of fair value.

ACCOUNTING POLICIES (continued)

### 1.19 NAMA Senior Bonds Designation and Valuation (continued)

This judgement included but was not limited to: evaluating available market information; evaluating relevant features of the instruments which market participants would factor into an appropriate valuation technique; determining the cash flows generated by the instruments including cash flows from assumed repo transactions; identifying a risk free discount rate; and applying an appropriate credit spread.

### 1.20 Financial Assets

The Group classifies its financial assets into the following categories: - financial assets at fair value through profit or loss; loans and advances; and available-for-sale financial assets.

Purchases and sales of financial assets are recognised on trade date, being the date on which the Group commits to purchase or sell the assets. Loans are recognised when cash is advanced to the borrowers.

Interest is calculated using the effective interest method and credited to the Income Statement. Dividends on available-for-sale equity securities are recognised in the Income Statement when the entity's right to receive payment is established. Impairment losses and translation differences on monetary items are recognised in the Income Statement.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or when the Group has transferred substantially all the risks and rewards of ownership.

*Financial assets at fair value through profit or loss*

This category can have two sub categories: - financial assets held for trading; and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if it is acquired principally for the purpose of selling in the near term; part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking; or if it is so designated at initial recognition by management, subject to certain criteria.

The assets are recognised initially at fair value and transaction costs are taken directly to the Income Statement. Interest and dividends on assets within this category are reported in interest income, and dividend income respectively. Gains and losses arising from changes in fair value are included directly in the Income Statement within net trading income.

Derivatives are also classified in this category unless they have been designated as hedges or are financial guarantee contracts.

*Loans and advances*

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and which are not classified as available-for-sale. They arise when the Group provides money or services directly to a customer with no intention of trading the loan. Loans and advances are initially recognised at fair value including direct and incremental transaction costs and are subsequently carried on an amortised cost basis.

*Available-for-sale*

Available-for-sale financial assets are non-derivative financial investments that are designated as available-for-sale and are not categorised into any of the other categories described above. Available-for-sale financial assets are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. Available-for-sale financial assets are initially recognised at fair value including direct and incremental transaction costs. They are subsequently held at fair value. Gains and losses arising from changes in fair value are included in other comprehensive income until sale or impairment when the cumulative gain or loss is transferred to the Income Statement as a reclassification adjustment. Assets reclassified from the held for trading category are recognised at fair value.

*Parent Company financial statements: Investment in subsidiary undertakings*

The Company accounts for investments in subsidiary undertakings that are not classified as held-for-sale at cost less provisions for impairment. If the investment is classified as held-for-sale, the Company accounts for it at the lower of its carrying value and fair value less costs to sell.

## ACCOUNTING POLICIES (continued)

### 1.20 Financial Assets (continued)

*Parent Company financial statements: Investment in subsidiary undertakings (continued)*
Dividends from a subsidiary undertaking are recognised in the Income Statement, when the Company's right to receive the dividend is established.

Acquisitions of businesses or investments in subsidiary undertakings between members of the Group are measured at their carrying value at the date of the transaction, except where prohibited by Company law or IFRS.

### 1.21 Financial Liabilities

Issued financial instruments or their components are classified as liabilities where the substance of the contractual arrangement results in the Group having a present obligation to either deliver cash or another financial asset to the holder, to exchange financial instruments on terms that are potentially unfavourable or to satisfy the obligation otherwise than by the exchange of a fixed amount of cash or another financial asset for a fixed number of equity shares.

Financial liabilities are initially recognised at fair value, being their issue proceeds (fair value of consideration received) net of transaction costs incurred. Financial liabilities are subsequently measured at amortised cost, with any difference between the proceeds net of transaction costs and the redemption value recognised in the income statement using the effective interest method.

Where financial liabilities are classified as trading they are also initially recognised at fair value and the related transaction costs are taken directly to the Income Statement. Gains and losses arising from changes in fair value are recognised directly in the Income Statement within net trading income.

The Group derecognises a financial liability when its contractual obligations are discharged, cancelled or expired. Any gain or loss on the extinguishment or re-measurement of a financial liability is recognised in profit or loss.

### 1.22 Property, Plant and Equipment

Property, plant and equipment are stated at cost, or deemed cost, less accumulated depreciation and provisions for impairment, if any. Additions and subsequent expenditures are capitalised only to the extent that they enhance the future economic benefits expected to be derived from the asset. No depreciation is provided on freehold land. Property, plant and equipment are depreciated on a straight line basis over their estimated useful economic lives. Depreciation is calculated based on the gross carrying amount, less the estimated residual value at the end of the assets' economic life.

The Group uses the following useful lives when calculating depreciation:

| | |
|---|---|
| Freehold buildings and long leasehold property | 50 years |
| Short leasehold property | life of lease, up to 50 years |
| | |
| Costs of adaptation of freehold and leasehold property | |
| Branch properties | up to10 years[1] |
| Office properties | up to 15 years[1] |
| Computers and similar equipment | 3 – 7 years |
| Fixtures and fittings and other equipment | 5 – 10 years |

The Group reviews its depreciation rates regularly, at least annually, to take account of any change in circumstances. When deciding on useful lives and methods, the principal factors that the Group takes into account are the expected rate of technological developments and expected market requirements for, and the expected pattern of usage of, the assets. When reviewing residual values, the Group estimates the amount that it would currently obtain for the disposal of the asset, after deducting the estimated cost of disposal if the asset were already of the age and condition expected at the end of its useful life.

Gains and losses on disposal of property, plant and equipment are included in the Income Statement. It is Group policy not to revalue its property, plant and equipment.

[1]*Subject to the maximum remaining life of the lease.*

## ACCOUNTING POLICIES (continued)

### 1.23 Intangible Assets

*Computer software and other intangible assets*
Computer software and other intangible assets are stated at cost, less amortisation on a straight line basis and provisions for impairment, if any. The identifiable and directly associated external and internal costs of acquiring and developing software are capitalised where the software is controlled by the Group, and where it is probable that future economic benefits that exceed its cost will flow from its use over more than one year. Costs associated with maintaining software are recognised as an expense when incurred. Capitalised computer software is amortised over 3 to 10 years. Other intangible assets are amortised over the life of the asset.

Computer software and other intangible assets are reviewed for impairment when there is an indication that the asset may be impaired. Intangible assets not yet available for use are reviewed for impairment on an annual basis.

### 1.24 Derivatives and Hedge Accounting

Derivatives, such as interest rate swaps, forward rate agreements, currency swaps, and equity index options are used for hedging purposes as part of the Group's risk management strategy against assets, liabilities, positions and cash flows.

*Derivatives*
Derivatives are measured initially at fair value on the date on which the derivative contract is entered into and subsequently re-measured at fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and from valuation techniques using discounted cash flow models and option pricing models as appropriate. Derivatives are included in assets when their fair value is positive and in liabilities when their fair value is negative, unless there is the legal ability and intention to settle an asset and liability on a net basis.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets.

Profits or losses are only recognised on initial recognition of derivatives when there are observable current market transactions or valuation techniques that are based on observable market inputs.

*Embedded derivatives*
Some hybrid contracts contain both a derivative and a non-derivative component. In such cases, the derivative component is termed an embedded derivative. Where the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract, and the hybrid contract itself is not carried at fair value through profit or loss, the embedded derivative is treated as a separate derivative, and reported at fair value with gains and losses being recognised in the Income Statement.

*Hedging*
All derivatives are carried at fair value and the accounting treatment of the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. Where derivatives are held for risk management purposes, and where transactions meet the criteria specified in IAS 39 'Financial Instruments: Recognition and Measurement', the Group designates certain derivatives as either:

i. hedges of the fair value of recognised assets or liabilities or firm commitments ('fair value hedge'); or
ii. hedges of the exposure to variability of cash flows attributable to a recognised asset or liability, or a highly probable forecasted transaction ('cash flow hedge').

When a financial instrument is designated as a hedge, the Group formally documents the relationship between the hedging instrument and hedged item as well as its risk management objectives and its strategy for undertaking the various hedging transactions.

The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of the hedged items.

# ACCOUNTING POLICIES (continued)

## 1.24 Derivatives and Hedge Accounting (continued)

*Hedging (continued)*
The Group discontinues hedge accounting when:
a) it is determined that a derivative is not, or has ceased to be, highly effective as a hedge;
b) the derivative expires, or is sold, terminated, or exercised;
c) the hedged item matures or is sold or repaid; or
d) a forecast transaction is no longer deemed highly probable.

To the extent that the changes in the fair value of the hedging derivative differ from changes in the fair value of the hedged risk in the hedged item; or the cumulative change in the fair value of the hedging derivative differs from the cumulative change in the fair value of expected future cash flows of the hedged item, ineffectiveness arises. The amount of ineffectiveness (taking into account the timing of the expected cash flows, where relevant) provided it is not so great as to disqualify the entire hedge for hedge accounting, is recorded in the Income Statement.

In certain circumstances, the Group may decide to cease hedge accounting even though the hedge relationship continues to be highly effective by no longer designating the financial instrument as a hedge.

*Fair value hedge accounting*
Changes in the fair value of derivatives that qualify and are designated as fair value hedges are recorded in the Income Statement, together with changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. If the hedge no longer meets the criteria for hedge accounting, the fair value hedging adjustment cumulatively made to the carrying value of the hedged item is, for items carried at amortised cost, amortised over the period to maturity of the previously designated hedge relationship using the effective interest method.

For available-for-sale items the fair value hedging adjustment remains in equity, until the hedged item affects the Income Statement and is recognised in the Income Statement using the effective interest method. If the hedged item is sold or repaid, the unamortised fair value adjustment is recognised immediately in the Income Statement.

*Cash flow hedge accounting*
The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is initially recognised directly in Other Comprehensive Income and included in the Cash Flow hedging reserve in the Statement of Changes in Equity. The amount recognised in Other Comprehensive Income is re-classed to profit or loss as a reclassification adjustment in the same period as the hedged cash flows affect profit or loss, and in the same line item in the statement of comprehensive income. Any ineffective portion of the gain or loss on the hedging instrument is recognised in the income statement immediately.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss recognised in Other Comprehensive Income from the time when the hedge was effective remains in equity and is reclassified to the Income Statement as a reclassification adjustment as the forecast transaction affects profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was recognised in Other Comprehensive Income from the period when the hedge was effective is reclassified from equity to the Income Statement.

*Net investment hedge*
Hedges of net investments in foreign operations, including monetary items that are accounted for as part of the net investment, are accounted for similarly to cash flow hedges. The effective portion of the gain or loss on the hedging instrument is recognised in other comprehensive income and the ineffective portion is recognised immediately in the Income Statement. The cumulative gain or loss previously recognised in Other Comprehensive Income is recognised in the income statement on the disposal or partial disposal of the foreign operation. Hedges of net investments may include non-derivative liabilities as well as derivative financial instruments.

*Derivatives that do not qualify for hedge accounting*
Certain derivative contracts entered into as economic hedges do not qualify for hedge accounting. Changes in the fair value of derivative instruments that do not qualify for hedge accounting are recognised immediately in the Income Statement.

# ACCOUNTING POLICIES (continued)

### 1.25 Collateral and Netting

The Group enters into master netting agreements with counterparties, to ensure that if an event of default occurs, all amounts outstanding with those counterparties will be settled on a net basis.

*Collateral*

The Group obtains collateral in respect of customer liabilities where this is considered appropriate. The collateral normally takes the form of a lien over the customer's assets and gives the Group a claim on these assets for both existing and future liabilities. The collateral is, in general, not recorded on the Statement of Financial Position.

The Group also receives collateral in the form of cash or securities in respect of other credit instruments, such as stock borrowing contracts and derivative contracts in order to reduce credit risk.

Collateral received in the form of securities is not recorded on the Statement of Financial Position. Collateral received in the form of cash is recorded on the Statement of Financial Position with a corresponding liability. These items are assigned to deposits received from banks or other counterparties in the case of cash collateral received. Any interest payable or receivable arising is recorded as interest expense or interest income respectively.

In certain circumstances, the Group will pledge collateral in respect of liabilities or borrowings. Collateral pledged in the form of securities or loans and advances continues to be recorded on the Statement of Financial Position. Collateral paid away in the form of cash is recorded in loans and advances to banks or customers. Any interest payable or receivable arising is recorded as interest expense or interest income respectively.

*Netting*

Financial assets and financial liabilities are offset and the net amount reported in the Statement of Financial Position if, and only if, there is a currently enforceable legal right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. This is not generally the case with master netting agreements where the related assets and liabilities are presented gross on the Statement of Financial Position.

### 1.26 Sale and Repurchase Agreements

Financial assets may be lent or sold subject to a commitment to repurchase them ('repos'). Such securities are retained on the Statement of Financial Position when substantially all the risks and rewards of ownership remain with the Group. The liability to the counterparty is included separately on the Statement of Financial Position as appropriate. The difference between the sale and repurchase price is accrued over the life of the agreements using the effective interest method.

### 1.27 Leases

*Lessor*

Assets leased to customers are classified as finance leases if the lease agreements transfer substantially all the risks and rewards of ownership, with or without ultimate legal title. When assets are held subject to a finance lease, the present value of the lease payments, discounted at the rate of interest implicit in the lease, is recognised as a receivable. The difference between the total payments receivable under the lease and the present value of the receivable is recognised as unearned finance income, which is allocated to accounting periods under the pre-tax net investment method to reflect a constant periodic rate of return.

Assets leased to customers are classified as operating leases if the lease agreements do not transfer substantially all the risks and rewards of ownership. The leased assets are included within property, plant and equipment on the Statement of Financial Position and depreciation is provided on the depreciable amount of these assets on a systematic basis over their estimated useful lives. Lease income is recognised on a straight line basis over the period of the lease unless another systematic basis is more appropriate.

*Lessee*

Operating lease rentals payable are recognised as an expense in the Income Statement on a straight line basis over the lease term unless another systematic basis is more appropriate.

## ACCOUNTING POLICIES (continued)

### 1.28 Shareholders' Equity

Issued financial instruments, or their components, are classified as equity where they meet the definition of equity and confer on the holder a residual interest in the assets of the Group. Incremental costs directly attributable to the issue of an equity instrument are deducted from the initial measurement of the equity instrument.

*Ordinary share capital*
Ordinary share capital represents funds raised by issuing shares in return for cash or other consideration. Share capital comprises ordinary shares, convertible non-voting shares and preference shares of the entity.

*Dividends and distributions*
Dividends on ordinary shares are recognised in equity in the period in which they are approved by the Company's shareholders or in the case of the interim dividend when it has been approved for payment by the Board of Directors.

*Available-for-sale reserves*
Available-for-sale securities reserves represent the net unrealised gain or loss, net of tax, arising from the recognition in the Statement of Financial Position of financial investments available-for-sale at fair value.

*Cash flow hedge reserves*
Cash flow hedge reserves represent the net gains or losses, net of tax, on effective cash flow hedging instruments that will be reclassified to the income statement when the hedged transaction affects profit or loss.

*Capital contribution*
Capital contribution represents the initial principal amount net of costs of a promissory note issued by the Minister for Finance to EBS Group.

*General reserves*
General reserves represent retained earnings of the parent company and subsidiaries. It is shown net of the cumulative deficit within the defined benefit pension schemes and other appropriate adjustments.

### 1.29 Segment Reporting

An operating segment is a component of the Group that engages in business activities from which it earns revenues and incurs expenses. For management and reporting purposes the Group's activities are organised into one reportable segment based on the internal reports that are regularly reviewed by the Chief Operating Decision Maker ('CODM'). The Board of Directors is considered to be the CODM.

The Group operates solely in the Republic of Ireland.

### 1.30 Cash and Cash Equivalents

For the purposes of the Cash Flow Statement, cash comprises cash on hand and demand deposits, and cash equivalents which are comprised highly liquid investments that are convertible into cash with an insignificant risk of changes in value and with original maturities of less than three months.

### 1.31 Prospective Accounting Changes

The following new accounting standards and amendments to existing standards approved by the IASB, but not early adopted by the Group, will impact the Group's financial reporting in future periods. The Group is currently considering the impacts of these amendments. The new accounting standards and amendments which are more relevant to the Group are detailed below.

| Pronouncement | Nature of change | IASB effective date |
|---|---|---|
| Amendments to IAS 32 Financial instruments: Presentation on Offsetting Financial Assets and Financial Liabilities | The amendments to IAS 32 Financial Instruments: Presentation clarifies that the right of set-off must be currently available and legally enforceable for all counterparties in the normal course of business, as well as in the event of default, insolvency or bankruptcy. | IAS 32: Annual periods beginning on or after 1 January 2014 |

## ACCOUNTING POLICIES (continued)

### 1.31 Prospective Accounting Changes (continued)

| Pronouncement | Nature of change | IASB effective date |
|---|---|---|
| Amendments to IFRS 10 Consolidated Financial Statements, IFRS 12 Disclosure of Interests in Other Entities and IAS 27 Separate Financial Statements on Investment Entities | In October 2012, the IASB issued Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27). The amendments provide an exception for investment entities to consolidate particular subsidiaries. These subsidiaries should be measured at fair value through profit and loss. The amendments also set out the disclosure requirements for investment entities. | Annual periods beginning on or after 1 January 2014 |
| Amendments to IAS 36 Impairment of Assets on Recoverable Amount Disclosures for Non-Financial Assets | As part of the development of IFRS 13 Fair Value Measurement, the IASB amended IAS 36 to require disclosures about the recoverable amount of impaired assets. The amendments published in May 2013 clarify that the scope of these disclosures is limited to the recoverable amount of impaired assets that is based on fair value less costs of disposal. The amendments require an entity to disclose:<br>– the level of the fair value hierarchy within which the fair value of the asset is categorised;<br>– a description of the valuation technique(s) used to measure the fair value less costs of disposal, where the fair value measurement is categorised within Level 2 or Level 3 of the fair value hierarchy;<br>– the key assumptions which management has based its determination of fair value less costs of disposal, where the fair value measurement is categorised within Level 2 or Level 3 of the fair value hierarchy; and<br>– the discount rates used to determine current and previous impairments where the recoverable amount of impaired assets, based on fair value less costs of disposal, was measured using a present value technique.<br><br>The amendment is still subject to EU endorsement. | Annual periods beginning on or after 1 January 2014 |

## ACCOUNTING POLICIES (continued)

### 1.31 Prospective Accounting Changes (continued)

| Pronouncement | Nature of change | IASB effective date |
|---|---|---|
| Amendments to IAS 39 Financial Instruments: Recognition and Measurement on Novation of Derivatives and Continuation of Hedge Accounting | The amendment to IAS 39 Financial Instruments: Recognition and Measurement provides an exception to the requirement to discontinue hedge accounting where a hedging derivative is novated, provided certain criteria are met. The amendment applies to novations:<br>– which arise due to laws or regulations, or the introduction of laws or regulations;<br>– where the parties to the hedging instrument agree that one or more clearing counterparties replace their original counterparty to become the new counterparty to each of the parties; and<br>- that did not result in changes to the terms of the original derivative except the changes directly attributable to the change in counterparty to achieve clearing.<br><br>All of the above criteria must be met to continue hedge accounting under this exception.<br><br>The amendment is still subject to EU endorsement. | Annual periods beginning on or after 1 January 2014 |
| Annual improvements to IFRSs 2010–2012 cycle | In December 2013, the IASB issued Annual Improvements to IFRSs 2010 – 2012 Cycle. The amendments to standards under the annual improvements process are primarily to remove inconsistencies and clarify wording.<br><br>The amendments are to seven International Financial Reporting Standards. The more relevant amendments are:<br><br>*IFRS 2 Share-based payments*<br>The amendment clarifies the definition of ‘vesting conditions’ by defining a ‘performance condition’ and a ‘service condition’.<br><br>*IFRS3 Business Combinations*<br>The amendments clarify that:<br>– a contingent consideration is assessed as either a liability or an equity instrument only on the basis of IAS 32 Financial Instruments: Presentation;<br>– contingent consideration that is within the scope of IAS 39 Financial Instruments: Recognition and Measurement is measured at fair value at each reporting date and changes in fair value are recognised in profit or loss in accordance with IAS 39; and<br>– contingent consideration that is not within the scope of IAS 39 Financial Instruments: Recognition and Measurement is measured at fair value at each reporting date and changes in fair value recognised in profit or loss. | Annual periods beginning on or after 1 July 2014 |

# ACCOUNTING POLICIES (continued)

## 1.31 Prospective Accounting Changes (continued)

| Pronouncement | Nature of change | IASB effective date |
| --- | --- | --- |
| Annual improvements to IFRSs 2010–2012 cycle (continued) | *IFRS 8 Operating Segments*<br>The amendment requires an entity to disclose the judgements made by management to identify the entity's reportable segments when operating segments are aggregated.<br><br>The amendment clarifies that a reconciliation of the total of the reportable segments' assets to the entity's assets should be disclosed, if that amount is regularly provided to the chief operating decision maker.<br><br>*IFRS 13 Fair Value Measurement*<br>The amendment clarifies that amendments to IFRS 9 | Annual periods beginning on or after 1 July 2014 |
| | Financial Instruments and IAS 39 Financial Instruments: Recognition and Measurement by IFRS 13 did not remove the ability to measure short - term receivables and payables with no stated interest rate at invoice amounts without discounting, when the effect of not discounting is immaterial.<br><br>None of the above amendments is expected to have a significant impact on reported results or disclosures.<br><br>The amendments are still subject to EU endorsement. | Annual periods beginning on or after 1 July 2014 |
| Annual improvements to IFRSs 2011–2013 cycle | December 2013, the IASB issued Annual Improvements to IFRSs 2011– 2013 Cycle. The amendments to standards under the annual improvements process are primarily to remove inconsistencies and clarify wording. The more relevant amendments to AIB Group are:<br><br>*IFRS 3 Business Combinations*<br>The amendment clarifies that the accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself is not within the scope of IFRS 3.<br><br>*IFRS 13 Fair Value Measurement*<br>The amendment clarifies that the scope of the portfolio exception defined in paragraph 52 of IFRS 13 includes all contracts accounted for within the scope of IAS 39 Financial Instruments: Recognition and Measurement or IFRS 9 Financial Instruments, irrespective of whether they meet the definition of financial assets or financial liabilities as defined in IAS 32 Financial Instruments: Presentation.<br><br>None of the above amendments is expected to have a significant impact on reported results or disclosures.<br><br>The amendments are still subject to EU endorsement. | Annual periods beginning on or after 1 July 2014 |

# ACCOUNTING POLICIES (continued)

## 1.31 Prospective Accounting Changes (continued)

| Pronouncement | Nature of change | IASB effective date |
|---|---|---|
| IFRS 9 Financial Instruments | IFRS 9 will ultimately replace IAS 39 Financial Instruments: Recognition and Measurement. This project consists of three date removed until main phases:<br><br>Phase 1: Classification and measurement<br>In November 2009, the IASB issued IFRS 9 Financial Instruments covering classification and measurement of financial assets. The new standard aims to enhance the ability of investors and other users of financial information to understand the accounting for financial assets and to reduce complexity. IFRS 9 uses a single approach to determine whether a financial asset is measured at amortised cost or fair value. The basis of classification depends on how an entity manages its financial instruments (its business model) and the contractual cash flow characteristics of the financial assets.<br><br>The IASB reissued IFRS 9 in October 2010. The revised standard incorporated new requirements on accounting for financial liabilities, and carried over the requirements for derecognition of Financial Assets and Liabilities from IAS 39.<br><br>Phase 2: Impairment methodology<br>The IASB published the Exposure Draft Financial Instruments: Expected Credit Losses in March 2013. The comment period closed on 5 July 2013 and redeliberations are on-going.<br><br>Phase 3: Hedge accounting<br>In November 2013, the IASB issued an update to IFRS 9 Financial Instruments (Hedge Accounting and amendments to IFRS 9, IFRS 7 and IAS 39). This includes new hedge accounting requirements and some related amendments to IAS 39 Financial Instruments: Recognition and Measurement and IFRS 7 Financial Instruments: Disclosures.<br><br>This phase replaces the rule based hedge accounting requirements in IAS 39 Financial Instruments: Recognition and Measurement to more closely align the accounting with risk management activities. The objective of this phase is to improve the ability of investors to understand risk management activities and to assess the amounts, timing and uncertainty of future cash flows. This update to IFRS 9 does not deal with macro hedging which is scheduled for a Discussion Paper in 2014. | Mandatory effective date removed until completion of the impairment phase of the project |

## ACCOUNTING POLICIES (continued)

### 1.31 Prospective Accounting Changes (continued)

| Pronouncement | Nature of change | IASB effective date |
|---|---|---|
| IFRS 9 Financial Instruments (continued) | The main areas of change to hedge accounting are as follows:<br>– Risk component – This may be designated as the hedged item, for both financial and non-financial items, if the risk component is separately identifiable and reliably measurable;<br>– Hedge effectiveness testing – the 80-125% range is replaced by an objectives-based test which focuses on the economic relationship between the hedged item and the hedging instrument and the effect of credit risk on the economic relationship;<br>– Costs of hedging – the time value of an option, the forward element of a forward contract and any foreign currency basis spread may be excluded from the designation of a financial instrument as the hedging instrument and accounted for as costs of hedging;<br>– Groups of items – more designations of groups of items as the hedged item are possible;<br>– Disclosures – more extensive disclosures are required.<br><br>IFRS 9 (2013) also includes two changes resulting from other phases of the IASB's financial instruments project:<br>– IFRS 9 requires that changes in the fair value of an entity's own debt caused by changes in its own credit quality to be recognised in other comprehensive income rather than in profit or loss. Under a 'fast-track' option, entities can apply these requirements of IFRS 9 early without applying the other IFRS 9 requirements at the same time;<br>– IFRS 9 (2013) does not have a mandatory effective date. The IASB decided to remove the mandatory effective date until the completion of the impairment phase of the project.<br><br>Since some significant aspects of the standard have yet to be finalised, namely, impairment and macro hedging, it is impracticable for the Group to quantify the impact of IFRS 9 at this stage. However, the implementation and the impact of the standard are likely to be significant.<br><br>The new standard is subject to EU endorsement. | Mandatory effective date removed until completion of the impairment phase of the project |
| Amendments to IAS 19 Employee Benefits | In November 2013, the IASB issued amendments to IAS 19 dealing with 'Defined Benefit Plans-Employee Contributions'. These amendments will not impact AIB Group as all the defined benefit schemes were closed to future accrual with effect from 31 December 2013. | Annual periods beginning on or after 1 July 2014 |

## Consolidated Income Statement

For the year ended 31 December 2013

| | Note | 2013 €m | Restated* 2012 €m |
|---|---|---|---|
| Interest income and similar income | 2 | 621 | 701 |
| Interest expense and similar charges | 2 | (449) | (558) |
| **Net Interest Income** | | **172** | **143** |
| Net fees and commissions income | 3 | 14 | 13 |
| Net trading income | 4 | 2 | 3 |
| Gain on transfer of loans and advances held-for-sale to NAMA | 8 | - | 1 |
| Other operating income/(loss) | 5 | 15 | (671) |
| **Total Other Income/(Loss)** | | **31** | **(654)** |
| **Total Operating Income/(Loss)** | | **203** | **(511)** |
| Administrative expenses | 6 | (65) | (75) |
| Amortisation of intangible assets | 17 | (5) | (5) |
| Impairment and depreciation of property, plant and equipment | 16 | (4) | (5) |
| **Total Operating Expenses** | **6** | **(74)** | **(85)** |
| **Operating profit/(loss) before impairment losses and taxation** | | **129** | **(596)** |
| Provisions for impairment of available-for-sale financial assets | 11 | - | (3) |
| Provisions for impairment of loans and advances to customers | 14 | (401) | (229) |
| **Total Impairment losses** | | **(401)** | **(232)** |
| **Operating loss before taxation** | | **(272)** | **(828)** |
| Taxation | 7 | 29 | 104 |
| **Loss for the year** | | **(243)** | **(724)** |

The loss for the year is wholly attributable to the equity holders of EBS.
*Restated due to change in accounting policy for employee benefits (note 36)

Desmond Fitzgerald, Managing Director

Catherine Woods, Non-Executive Director

James O'Hara, Non-Executive Director

Sarah McLaughlin, Company Secretary

## Consolidated Statement of Comprehensive Income

For the year ended 31 December 2013

| | Note | 2013 €m | Restated* 2012 €m |
|---|---|---|---|
| **Loss for the year** | | **(243)** | **(724)** |
| **Comprehensive gain/profit, net of taxation** | | | |
| ***Items that will not be reclassified to profit and loss:*** | | | |
| Net actuarial movement in retirement benefits | 7 | 11 | (33) |
| | | 11 | (33) |
| ***Items that may be reclassified subsequently to profit and loss:*** | | | |
| Net movement in cash flow hedge reserve | 7 | 4 | 19 |
| Net movement in available-for-sale reserve | 7 | (10) | 189 |
| Comprehensive gain/profit for the year, net of taxation | | (6) | 208 |
| **Total comprehensive loss for the year** | | **(238)** | **(549)** |

*Restated due to change in accounting policy for employee benefits (note 36)

Desmond Fitzgerald, Managing Director

Catherine Woods, Non-Executive Director

James O’Hara, Non-Executive Director

Sarah McLaughlin, Company Secretary

## Group and Company Statement of Financial Position

As at 31 December 2013

| Company 2013 €m | Restated* Company 2012 €m | | Note | Group 2013 €m | Restated* Group 2012 €m |
|---|---|---|---|---|---|
| | | **Assets** | | | |
| 73 | 8 | Cash and balances at central banks | 9 | **74** | 8 |
| 153 | 226 | Derivative financial instruments | 30 | **120** | 190 |
| 3,009 | 4,545 | Available-for-sale financial assets | 11 | **217** | 1,568 |
| - | 305 | NAMA senior bonds | 12 | **-** | 305 |
| 4,079 | 3,906 | Loans and advances to credit institutions | 13 | **1,343** | 883 |
| 5,641 | 5,994 | Loans and advances to customers | 14 | **12,025** | 12,969 |
| 318 | 311 | Deferred taxation | 18 | **279** | 252 |
| 28 | 26 | Other assets | 19 | **9** | 36 |
| 36 | 138 | Prepayments and accrued income | | **24** | 53 |
| 4 | - | Current taxation | | **2** | - |
| 12 | 15 | Intangible assets | 17 | **14** | 17 |
| 612 | 537 | Shares in Group undertakings | 15 | **-** | - |
| 31 | 35 | Property, plant and equipment | 16 | **32** | 36 |
| **13,996** | **16,046** | **Total assets** | | **14,139** | **16,317** |
| | | **Liabilities** | | | |
| 1,694 | 2,756 | Deposits by central bank and banks | 20 | **1,640** | 2,698 |
| 10,073 | 10,983 | Customer accounts | 21 | **9,297** | 10,117 |
| 76 | 180 | Derivative financial instruments | 30 | **80** | 186 |
| 7 | 13 | Provisions for liabilities and commitments | 24 | **7** | 13 |
| 234 | 298 | Accruals and deferred income | | **225** | 269 |
| - | - | Current taxation | | **2** | - |
| 90 | 156 | Other liabilities | 23 | **69** | 101 |
| 1,153 | 1,286 | Debt securities in issue | 22 | **2,001** | 2,182 |
| 37 | 62 | Retirement benefit liability | 25 | **37** | 62 |
| **13,364** | **15,734** | **Total liabilities** | | **13,358** | **15,628** |
| | | **Shareholders' equity** | | | |
| 1,654 | 1,324 | Ordinary share capital | 26 | **1,654** | 1,324 |
| 249 | 249 | Capital contribution | 27 | **249** | 249 |
| (277) | (376) | Reserves | | **(5)** | 1 |
| (994) | (885) | General reserve | | **(1,117)** | (885) |
| 632 | 312 | Shareholders' equity | | **781** | 689 |
| **13,996** | **16,046** | **Total liabilities and shareholders' equity** | | **14,139** | **16,317** |

*Restated due to change in accounting policy for employee benefits (note 36)

Desmond Fitzgerald, Managing Director

Catherine Woods, Non-Executive Director

James O'Hara, Non-Executive Director

Sarah McLaughlin, Company Secretary

## Group and Company Statement of Cash Flows

For the Year Ended 31 December 2013

| Company 2013 €m | Restated* Company 2012 €m | | Note | Group 2013 €m | Restated* Group 2012 €m |
|---|---|---|---|---|---|
| | | **Cash flows from operating activities** | | | |
| (120) | (612) | Loss for the year | | (243) | (724) |
| | | ***Adjustments for:*** | | | |
| 4 | 5 | Impairment and depreciation of property, plant and equipment | 16 | 4 | 5 |
| 4 | 3 | Amortisation of intangibles | 17 | 5 | 5 |
| 222 | 122 | Provisions for impairment of financial assets | 14 | 401 | 232 |
| - | (1) | Gain on disposal of loans and advances held-for-sale to NAMA | 8 | - | (1) |
| (9) | 1 | Pension expense | | (9) | 1 |
| 2 | (31) | Fair value movement on hedging derivatives | | (2) | (5) |
| (45) | (49) | Fair value movement on hedged items | | (46) | (47) |
| - | 516 | Loss on disposal of loans | | - | 668 |
| (18) | 90 | Income tax credit | 7 | (29) | (106) |
| **40** | **44** | **Operating Income before changes in working capital and provisions** | | **81** | **28** |
| 201 | (105) | Net decrease /(increase) in loans and advances to credit institutions | | (296) | (466) |
| (2) | 3 | Net (increase)/ decrease in mandatory reserve balance | | (2) | 3 |
| 131 | 955 | Net decrease (increase) in loans and advances to customers | | 543 | 1,507 |
| 100 | 1 | Net decrease in other assets | | 55 | 30 |
| (1,062) | (2,552) | Net (decrease) increase in deposits from Central Bank of Ireland and banks | | (1,058) | (2,594) |
| (910) | 1,524 | Net (decrease)/increase in amounts due to customers | | (820) | 1,576 |
| (134) | (77) | Net (decrease)/increase in other liabilities | | (85) | 104 |
| - | 1 | Effect of exchange translations and other adjustments | | - | 1 |
| **(1,636)** | **(206)** | **Cash generated from (used in) operations before taxation** | | **(1,582)** | **189** |
| - | 4 | Income taxes refunded | | - | 3 |
| **(1,636)** | **(202)** | **Net cash generated from (used in) operating activities** | | **(1, 582)** | **192** |
| | | **Cash flows from investing activities** | | | |
| - | - | Purchase of property, plant and equipment | 16 | - | (1) |
| (1) | (2) | Purchase of intangible assets | 17 | (1) | (2) |
| (75) | - | Investment in subsidiaries | 15 | - | - |
| 1,936 | (220) | Net (increase) decrease in available-for-sale financial assets | | 1,646 | 376 |
| **1,860** | **(222)** | **Net cash (outflow) inflow from investing activities** | | **1,645** | **373** |
| | | **Cash flows from financing activities** | | | |
| 330 | 400 | Issuance of ordinary share capital | | 330 | 400 |
| (117) | (82) | Redemption of debt securities | | (165) | (1,127) |
| - | (1) | Interest expense on subordinated liabilities | | - | (1) |
| **213** | **317** | **Net cash outflow from financing activities** | | **165** | **(728)** |
| **437** | **(107)** | **Net increase (decrease) in cash and cash equivalents** | | **228** | **(163)** |
| 3,715 | 3,822 | Cash and cash equivalents at 1 January | | 76 | 239 |
| **4,152** | **3,715** | **Cash and cash equivalents at 31 December** | **10** | **304** | **76** |

*Restated due to change in accounting policy for employee benefits (note 36)

# Consolidated Statement of Changes in Shareholders' Equity

## Group

At 31 December 2013

| | Ordinary Share Capital | Capital Contribution | General Reserve | Available-for-Sale Reserve | Cash Flow Hedge Reserve | Total Shareholders' Equity |
|---|---|---|---|---|---|---|
| | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** |
| **At 1 January 2012** | **924** | **249** | **(128)** | **(178)** | **(29)** | **838** |
| Total comprehensive income for the period | - | - | (757) | 189 | 19 | **(549)** |
| Issue of ordinary shares | 400 | - | - | - | - | **400** |
| **At 31 December 2012 (Restated)*** | **1,324** | **249** | **(885)** | **11** | **(10)** | **689** |
| Total comprehensive income for the year | - | - | (232) | (10) | 4 | **(238)** |
| Issue of ordinary shares | 330 | - | - | - | - | **330** |
| **At 31 December 2013** | **1,654** | **249** | **(1,117)** | **1** | **(6)** | **781** |

*Restated due to change in accounting policy for employee benefits (note 36)

## Statement of Changes in Shareholders' Equity

### Company

At 31 December 2013

| | Ordinary Share Capital | Capital Contribution | General Reserve | Available-for-Sale Reserve | Cash Flow Hedge Reserve | Total Shareholders' Equity |
|---|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m | €m |
| **At 1 January 2012** | **924** | **249** | **(240)** | **(527)** | **(29)** | **377** |
| Total comprehensive income for the period | - | - | (645) | 161 | 19 | **(465)** |
| Issue of ordinary shares | 400 | - | - | - | - | **400** |
| **At 31 December 2012 (Restated)*** | **1,324** | **249** | **(885)** | **(366)** | **(10)** | **312** |
| Total comprehensive income for the year | - | - | (109) | 95 | 4 | **(10)** |
| Issue of ordinary shares | 330 | - | - | - | - | **330** |
| **At 31 December 2013** | **1,654** | **249** | **(994)** | **(271)** | **(6)** | **632** |

*Restated due to change in accounting policy for employee benefits (note 36)

# NOTES TO THE FINANCIAL STATEMENTS

## 1. REPORTING BY BUSINESS SEGMENTS AND GEOGRAPHICAL LOCATION

For management and reporting purposes the Group's activities are organised in one reportable segment based on the information provided internally to the chief operating decision maker. The chief operating decision maker is considered to be the Board of Directors. The principal activities of the Group involve the provision of mortgage lending, savings, investments and insurance arrangement services to customers.

For management reporting purposes AIB Group includes EBS across Domestic Core Bank, Financial Services Group and Group segments.

## 2. NET INTEREST INCOME

| | For the year ended 31 December 2013 €m | For the year ended 31 December 2012 €m |
|---|---|---|
| **Interest Income and Similar Income** | | |
| Other interest income | 21 | 39 |
| Interest received from Parent company | 77 | 43 |
| Available-for-sale financial assets | 40 | 63 |
| Interest on loans and receivables to banks | 1 | 2 |
| Interest on loans and receivables to customers | 482 | 554 |
| **Total Interest Income and Similar Income** | **621** | **701** |
| **Interest Expense and Similar Charges** | | |
| Interest on deposits by banks | (10) | (32) |
| Interest on customer accounts | (322) | (377) |
| Interest on debt securities in issue | (55) | (97) |
| Interest paid to Parent company | (29) | (3) |
| Other | (33) | (49) |
| **Total Interest Expense and Similar Charges** | **(449)** | **(558)** |
| **Net Interest Income** | **172** | **143** |

Interest expense includes €47m (2012: €55m) in respect of charges payable under the Credit Institutions (Eligible Liabilities Guarantee) scheme. The cost of this scheme is directly attributable to the issuance of specific funding and is therefore included in interest expense. On 26 February 2013, the Irish Government announced that the ELG would end at midnight on 28 March 2013. After that date any new liabilities were not covered by the ELG. Liabilities incurred since January 2010 and before the scheme's end continue to be guaranteed until maturity date.

Included within various captions under interest income for the year ended 31 December 2013 is a total of €100m (2012: €97m) accrued on impaired financial assets.

Included within loans and advances to customers under interest income for the year ended 31 December 2013 is a credit of Nil for the Group (2012: €13m) due to a change in the accounting estimate of the average expected life of mortgages.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### 3. NET FEES AND COMMISSIONS

| | For the year ended 31 December 2013 €m | For the year ended 31 December 2012 €m |
|---|---|---|
| **Fees and Commission Income** | | |
| Fees and commissions receivable | 18 | 15 |
| Fees and commissions receivable from Group companies | - | 3 |
| **Fees and Commission Income** | **18** | **18** |
| **Fees and Commissions Expense** | | |
| Fees and commissions payable | (4) | (4) |
| Fees and commissions payable to Group companies | - | (1) |
| **Fee and Commission Expense** | **(4)** | **(5)** |
| **Net Fees and Commission Income** | **14** | **13** |

Commission income relates to fees earned by the Group on insurance and investment advisory services provided to its customers.

### 4. NET TRADING INCOME

| | For the year ended 31 December 2013 €m | For the year ended 31 December 2012 €m |
|---|---|---|
| **Net Trading Income/(Loss)** | | |
| Debt securities and interest rate contracts | 1 | 4 |
| Equity securities and index contracts | 1 | (1) |
| **Net Trading Income/(Loss)** | **2** | **3** |

The total hedging ineffectiveness on cash flow hedges reflected in net trading income amounted to a credit of €1m (2012: €1m).

### 5. OTHER OPERATING PROFIT

| | For the year ended 31 December 2013 €m | For the year ended 31 December 2012 €m |
|---|---|---|
| Gain/ (Loss) on disposal of financial instruments | 33 | (3) |
| Loss on disposals of loans and advances to customers | - | (668) |
| Foreign exchange gains | 1 | - |
| Miscellaneous operating income | (19) | - |
| | **15** | **(671)** |

During 2013 a significant part of the EBS portfolio of available-for-sale securities were sold to AIB p.l.c giving rise to a gain of €33m (2012: loss of €3m).

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 6. TOTAL OPERATING EXPENSES

| | For the year ended 31 December 2013 €m | For the year ended 31 December 2012 €m Restated* |
|---|---|---|
| Personnel expenses | 25 | 36 |
| Other Administrative expenses | 40 | 39 |
| Total Administrative expenses | 65 | 75 |
| Amortisation of intangibles (note 17) | 5 | 5 |
| Impairment and depreciation of property, plant and equipment (note 16) | 4 | 5 |
| **Total Operating Expenses** | **74** | **85** |

| | For the year ended 31 December 2013 €m | For the year ended 31 December 2012 €m Restated* |
|---|---|---|
| ***Personnel expenses comprise:*** | | |
| Wages and salaries | 26 | 30 |
| Voluntary Severance | 4 | - |
| Social welfare costs and health insurance | 3 | 4 |
| Retirement benefits (note 25) | (8) | 4 |
| Other indirect staff costs | - | (2) |
| | **25** | **36** |

The average number of full time equivalents employed by EBS in the financial year was 503 (2012: 619).

Full details of directors' remuneration are given in the related party transaction note (note 33).

An analysis of the auditor's fees is set out below:

**Auditors' remuneration**

| | For the year ended 31 December 2013 €'000 | For the year ended 31 December 2012* €'000 |
|---|---|---|
| **Fees & expenses paid to our statutory auditors are analysed as follows:** | | |
| Audit of individual and Group financial statements(1) | 200 | 200 |
| Other assurance services | - | - |
| Tax advisory services | - | - |
| Other non-audit services | 26 | 100 |
| | **226** | **300** |

(1) 2012 audit fees paid to KPMG

Auditors' remuneration (including value added tax) in 2013 for audit services is €200k (2012: €200k) and for non audit services is €26k (2012: €100k). Fees for non audit services consist primarily of fees in connection with letters of comfort and advice on technical accounting matters.

The Board and Audit Committee reviews, on an on-going basis, the level of fees and is satisfied that it has not affected the independence of the auditors.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 6. TOTAL OPERATING EXPENSES (continued)

**Auditors' remuneration (continued)**
On 30th July 2013, KPMG Ireland resigned as Auditor of the EBS Group, and on 30th July 2013, Deloitte and Touche was appointed.

## 7. TAXATION

The taxation credit for the year is as follows:

| | For the year ended 31 December 2013 €m | For the year ended 31 December 2012 €m Restated* |
|---|---|---|
| The taxation credit for the year is as follows: | | |
| Deferred tax credit | (33) | (104) |
| Under accrual in respect of prior year | 4 | - |
| | **(29)** | **(104)** |

The reconciliation of total tax on income at the standard Irish corporation tax rate to the Group's actual tax charge is analysed as follows:

| | | |
|---|---|---|
| Loss before tax at 12.5% | (34) | (104) |
| **Adjustments:** | | |
| Under accrual in respect of prior year | 4 | - |
| Income taxed at higher rates | 1 | - |
| **Total tax credit (effective tax rate 10.7% (2012: 12.5%))** | **(29)** | **(104)** |

**Income tax recognised in other comprehensive income**

| | 2013 Before Tax €m | 2013 Tax benefit (expense) €m | 2013 Net of Tax €m | 2012 Before Tax €m | 2012 Tax benefit (expense) €m | 2012 Net of Tax €m |
|---|---|---|---|---|---|---|
| Net movement in cash flow hedge reserve | 5 | 1 | 4 | 22 | (3) | 19 |
| Net movement in available-for-sale reserve | (11) | (1) | (10) | 216 | (27) | 189 |
| Net actuarial gain/(loss) on retirement benefits | 13 | 2 | 11 | (37) | 4 | (33) |
| | **7** | **2** | **5** | **201** | **(26)** | **175** |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 8. GAIN ON TRANSFER OF LOANS AND ADVANCES HELD-FOR-SALE TO NAMA

**Analysis of gain on transfer of assets to NAMA**

| | For the year ended 31 December 2013 €m | For the year ended 31 December 2012 €m |
|---|---|---|
| Nominal amount of loans transferred to NAMA | - | - |
| Impairment provisions utilised | - | - |
| Carrying value of assets transferred to NAMA | - | - |
| Nominal amount of consideration received | - | - |
| Increase in Tranche 4 and 5 valuations | - | - |
| Reversal of prior period loss – loans returned from NAMA | - | (1) |
| Costs associated with transfer and fair value adjustments on securities received | - | - |
| **Gain on transfer of assets to NAMA** | **-** | **(1)** |

## 9. CASH AND BALANCES AT CENTRAL BANKS

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Cash in hand | 6 | 4 | 6 | 4 |
| Balances with Central Bank of Ireland other than mandatory reserve deposits | 67 | 4 | 68 | 4 |
| **Total cash and balances at Central Bank** | **73** | **8** | **74** | **8** |

## 10. CASH AND CASH EQUIVALENTS

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| **For the purposes of the cash flow statement the cash and cash equivalents comprise the following:** | | | | |
| Cash and balances with Central Bank of Ireland | 73 | 8 | 74 | 8 |
| Loans and receivables to credit institutions | 30 | 49 | 230 | 68 |
| Loans and advances to credit institutions (Group Undertakings) | 4,049 | 3,658 | - | - |
| | **4,152** | **3,715** | **304** | **76** |

Cash and cash equivalents include balances with original maturities of less than 3 months and balances with CBI exclude the mandatory reserve deposits.

Restricted cash in the Company and the Group is included in note 13.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 11. AVAILABLE-FOR-SALE FINANCIAL ASSETS

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Irish Government Securities | 214 | 416 | 214 | 416 |
| Euro Bank Securities | 2,792 | 3,894 | - | 917 |
| Non Euro Bank Securities | - | 35 | - | 35 |
| Other Investments | - | 198 | - | 198 |
| Equity securities - NAMA subordinated bonds | 3 | 2 | 3 | 2 |
| | **3,009** | 4,545 | **217** | 1,568 |

During 2013 the Bank sold the majority of its available for sale financial assets to AIB p.l.c to facilitate the further integration of EBS and AIB Treasury functions. The transfer happened at fair value and all risks and rewards transferred to AIB p.l.c.

**Available-for-sale financial assets – contractual maturity analysis**

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Maturing within three months | - | 147 | - | 147 |
| Maturing between three months and one year | 836 | 812 | - | 366 |
| Maturing between one and five years | 1,624 | 3,104 | - | 811 |
| Maturing after 5 years | 546 | 480 | 214 | 242 |
| | **3,006** | **4,543** | **214** | **1,566** |

At 31 December 2013, no impairment charge on available for sale financial assets was recognised (2012: €3m). As equity securities have no contractual maturity date they are not included in the table above.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### 11. AVAILABLE-FOR-SALE FINANCIAL ASSETS (continued)

| | Fair value | Unrealised gross gains | Unrealised gross losses | Net unrealised gains/(losses) |
|---|---|---|---|---|
| | €m | €m | €m | €m |
| **Group – 31 December 2013** | | | | |
| **Debt securities** | | | | |
| Irish Government Securities | 214 | - | - | - |
| **Total Debt Securities** | **214** | **-** | **-** | **-** |
| **Equity Securities** | | | | |
| Equity securities - NAMA subordinated bonds | 3 | 1 | - | 1 |
| **Total Equity Securities** | **3** | **1** | **-** | **1** |
| **Total financial investments available for sale** | **217** | **1** | **-** | **1** |
| **Company – 31 December 2013** | | | | |
| **Debt securities** | | | | |
| Irish Government Securities | 214 | - | - | - |
| Euro Bank Securities | 2,792 | 10 | (569) | (559) |
| **Total Debt Securities** | **3,006** | **10** | **(569)** | **(559)** |
| **Equity Securities** | | | | |
| Equity securities - NAMA subordinated bonds | 3 | 1 | - | 1 |
| **Total Equity Securities** | **3** | **1** | **-** | **1** |
| **Total financial investments available for sale** | **3,009** | **11** | **(569)** | **(558)** |
| **Group – 31 December 2012** | | | | |
| **Debt securities** | | | | |
| Irish Government Securities | 416 | 26 | - | 26 |
| Euro Bank Securities | 917 | 23 | (36) | (13) |
| Non Euro Bank Securities | 35 | - | (3) | (3) |
| Other Investments | 198 | 3 | - | 3 |
| **Total Debt Securities** | 1,566 | 52 | (39) | 13 |
| **Equity Securities** | | | | |
| Equity securities - NAMA subordinated bonds | 2 | - | - | - |
| **Total Equity Securities** | 2 | - | - | - |
| **Total financial investments available for sale** | 1,568 | 52 | (39) | 13 |
| **Company – 31 December 2012** | | | | |
| **Debt securities** | | | | |
| Irish Government Securities | 416 | 26 | - | 26 |
| Euro Bank Securities | 3,894 | 56 | (501) | (445) |
| Non Euro Bank Securities | 35 | - | (3) | (3) |
| Other Investments | 198 | 3 | - | 3 |
| **Total Debt Securities** | 4,543 | 85 | (504) | (419) |
| **Equity Securities** | | | | |
| Equity securities - NAMA subordinated bonds | 2 | - | - | - |
| **Total Equity Securities** | 2 | - | - | - |
| **Total financial investments available for sale** | 4,545 | 85 | (504) | (419) |

Unrealised gains/losses are recognised through other comprehensive income.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 12. NAMA SENIOR BONDS

| *Group and Company* | 2013 €m | 2012 €m |
|---|---|---|
| At 1 January | 305 | 347 |
| Amortisation of discount | 1 | 1 |
| Sale of NAMA bonds to AIB p.l.c | (279) | - |
| Redemption of bonds | (27) | (43) |
| **NAMA senior bonds** | **-** | **305** |

EBS received, as consideration for assets transferred to NAMA, a combination of Government guaranteed bonds ('NAMA senior bonds'), issued by NAMA and guaranteed by the Minister for Finance (amounting to 95% of the nominal consideration), and non-guaranteed subordinated bonds issued by NAMA (amounting to 5% of the nominal consideration). The NAMA subordinated bonds are classified as equity instruments within available-for-sale financial assets.

The basis for measurement, impairment and interest recognition are the same as those for loans and advances as set out in the accounting policies 1.9, 1.17, 1.19 and 1.20.

During 2013, NAMA redeemed €27m bonds at par (2012: €43m). In Q4 2013, EBS sold the remaining holding of the NAMA Senior Bonds which had a fair value of €279m to AIB Plc.

## 13. LOANS AND ADVANCES TO CREDIT INSTITUTIONS

| **Analysed by remaining maturity:** | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Repayable on demand | 4,079 | 3,639 | 1,343 | 616 |
| 3 months or less | - | 150 | - | 150 |
| 1 year or less but over 3 months | - | 104 | - | 104 |
| 5 years or less but over 1 year | - | 13 | - | 13 |
| | **4,079** | **3,906** | **1,343** | **883** |

Mandatory reserve deposits are not available for use in the Group's day-to-day operations.

At 31 December 2013, in addition to the mandatory reserve deposits, the Group has €222m (2012: €484m) included in loans and advances to credit institutions which is not available for its own use. This amount relates to funds held on behalf of EBS Mortgage Finance, Emerald Mortgages No.4 plc, Emerald Mortgages No.5 plc. Mespil 1 RMBS Limited and credit support annex's (CSA's).

At 31 December 2013, in addition to the mandatory reserve deposits, EBS Ltd had €222m (2012: €299m) included in loans and advances to credit institutions which is not available for its own use. This amount relates to funds held on behalf of Emerald Mortgages No. 4 plc, EBS Mortgage Finance and CSA's. The Company collects repayments from borrowers on behalf of Emerald 4 and EBS Mortgage Finance. These funds are transferred to designated bank accounts in the name of EBS over which these entities have a legal charge.

At 31 December 2013 loans outstanding between the Company and its subsidiary, EBS Mortgage Finance, amounted to €2,979m (2012: €3,254m).

At 31 December 2013 loans restricted between EBS Group and AIB p.l.c are €1,091m (2012: € 606m). At 31 December 2013 loans restricted between EBS Company and AIB p.l.c. and €1,068m (2012: €597m).

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 14. LOANS AND ADVANCES TO CUSTOMERS

### LOANS AND ADVANCES TO CUSTOMERS – ANALYSIS BY SECTOR

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Loans and receivables to customers | 5,732 | 5,903 | 13,377 | 13,903 |
| Loans to subsidiaries and special purpose vehicles | 724 | 673 | - | - |
| Total loans and advances to customers before provisions | 6,456 | 6,576 | 13,377 | 13,903 |
| Less provision for loan impairments | (815) | (582) | (1,352) | (934) |
| **Total loans and advances to customers after provisions** | **5,641** | **5,994** | **12,025** | **12,969** |

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Repayable on demand | 2,609 | 1,904 | 3,337 | 3,011 |
| Repayable in less than three months | 4 | 4 | 9 | 6 |
| Repayable in more than three months but less than one year | 8 | 6 | 24 | 10 |
| Repayable in more than one but less than five years | 81 | 562 | 219 | 182 |
| Repayable in more than five years | 3,754 | 4,100 | 9,788 | 10,694 |
| Total loans and advances to customers before provisions | 6,456 | 6,576 | 13,377 | 13,903 |
| Less provision for loan impairments | (815) | (582) | (1,352) | (934) |
| **Total loans and advances to customers after provisions** | **5,641** | **5,994** | **12,025** | **12,969** |

Included in Group loans and advances to customers is €6,543m (2012: €6,859m) of loans in the covered bond bank, EBS Mortgage Finance, €3,457m (2012: €3,539m) of loans held through securitisation vehicles Emerald Mortgages No.4 plc., Emerald Mortgages No.5 plc. and Mespil 1 RMBS Limited and nil (2012: nil) collateral pledged under the mortgage backed promissory note programme (refer to note 34). Unencumbered loans available as collateral for repo purposes, as at 31 December 2013, were €87m (2012: €59m). Loans to directors are disclosed in Note 33.

Fair value of the collateral held for Residential Mortgages is €11,323m at 31 December 2013 (2012: €11,366m) based on the CSO house price index.

Fair value of the collateral held for Commercial Mortgages is €248m at 31 December 2013 (2012: €261m) based on the property valuations at origination and applying the CSO (Ireland) index to these values to take account of price movements in the interim or valuation based on management's judgement.

### PROVISION FOR LOAN IMPAIRMENTS

**Group**

| | | Group 2013 €m | | Group 2012 €m |
|---|---|---|---|---|
| **Specific provision for loan impairments** | | | | |
| At 1 January | | 716 | | 757 |
| **Charge for impairment losses** | | | | |
| Commercial assets | 3 | | 6 | |
| Residential assets | 348 | | 187 | |
| Total charge for impairment losses | 351 | 351 | 193 | 193 |
| Impairment provision utilised on deleverage | | - | | (234) |
| At 31 December | | 1,067 | | 716 |

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### 14. LOANS AND ADVANCES TO CUSTOMERS (continued)

**PROVISION FOR LOAN IMPAIRMENTS (continued)**

**Group (continued)**

| | | | | |
|---|---|---|---|---|
| **Collective provision for loan impairments** | | | | |
| At 1 January | | 218 | | 192 |
| **Charge for impairment losses** | | | | |
| Commercial assets | 12 | | (21) | |
| Residential assets | 55 | | 70 | |
| Total charge for impairment losses | 67 | 67 | 49 | 49 |
| Impairment provision utilised on deleverage | | - | | (23) |
| At 31 December | | 285 | | 218 |
| **Total provision for loan impairments at 31 December** | | **1,352** | | **934** |

The impairment charge recognised in the Income Statement has increased to €401m (2012: €229m). This is described in detail in the Directors' Report on page 6.

Commercial consists of commercial term debt loans and residential consists of home loans, retail and commercial buy-to-let loans.

The impairment charge recognised in the Group income statement for loans and advances to customers of €401m (2012: €229m) is based on total charges above of €418m (2012: €242m) net of €20m (2012: €13m) settlement received from Genworth in respect of mortgage indemnity insurance on a pool of loans which were greater than 6 months in arrears & write offs of €3m.

**Company**

| | | **Company 2013 €m** | | **Company 2012 €m** |
|---|---|---|---|---|
| **Specific provision for loan impairments** | | | | |
| At 1 January | | 428 | | 514 |
| **Charge for impairment losses** | | | | |
| Commercial assets | 3 | | 6 | |
| Residential assets | 192 | | 120 | |
| Total charge for impairment losses | 195 | 195 | 126 | 126 |
| Impairment provision utilised on deleverage | | - | | (212) |
| At 31 December | | 623 | | 428 |
| **Collective provision for loan impairments** | | | | |
| At 1 January | | 154 | | 174 |
| **Charge (credit) for impairment losses** | | | | |
| Commercial assets | 12 | | (21) | |
| Residential assets | 26 | | 20 | |
| Total charge for impairment losses | 38 | 38 | (1) | (1) |
| Impairment provision utilised on deleverage | | - | | (19) |
| At 31 December | | 192 | | 154 |
| **Total provision for loan impairments at 31 December** | | **815** | | **582** |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 14. LOANS AND ADVANCES TO CUSTOMERS (continued)

Under the terms of the securitisation, the rights of the providers of the related funds are limited to the loans in the securitised portfolios and any related income generated by the portfolios, without recourse to EBS.

The impairment charge recognised in the Company Income Statement was €222m (2012: €117m).

Commercial consists of commercial term debt loans and residential consists of home loans, retail and commercial buy-to-let loans.

The impairment charge recognised in the company income statement for loans and advances to customers of €222m (2012: €117m) is based on total charges above of €233m (2012: €125m) net of €11m (2012: €8m) settlement received from Genworth in respect of mortgage indemnity insurance on a pool of loans which were greater than 6 months in arrears.

### CONTINUING INVOLVEMENT IN SECURITISED ASSETS

At 31 December 2013 the Group and EBS had advances secured on residential property subject to non-recourse funding. These loans, which have not been de-recognised, are shown within loans and advances to customers and the non-recourse funding is shown within debt securities in issue within the Group. In the Company the non recourse funding, in the form of loan notes, is shown in customer accounts.

### Emerald Mortgages No.4 plc

The total carrying amount of the original residential property transferred by EBS to Emerald Mortgages No.4 plc (‘Emerald 4’) as part of the securitisation amounted to €1,500m (2012: €1,500m). The amount of transferred secured loans that the Group continues to recognise at 31 December 2013 is €823m (2012: €868m). The carrying amount of the bonds issued by Emerald 4 to third party investors amounts to €816m (2012: €846m) and is also disclosed in note 22. The fair value of the transferred loans and external bonds at 31 December 2013 was €811m and €649m respectively. The carrying amount of the loan note in EBS issued to Emerald 4 amounts to €827m (2012: €872m) and is also disclosed in note 22.

EBS participates in the securitisation through the provision of administration services and unsecured loan financing of €17m (2012: €17m), which is subordinated to the interest of the bond holders.

### Emerald Mortgages No.5

The total carrying amount of the original residential property transferred by EBS to Emerald Mortgages No.5 (‘Emerald 5’) as part of the securitisation amounted to €2,500m (2012: €2,500m). The amount of transferred secured loans that the Group continues to recognise at 31 December 2013 is €1,708 (2012: €1,716m). The fair value of these of these loans at 31 December 2013 was €1,633m. Bonds were issued by Emerald 5 to EBS but these are not shown on the Group or Company statement of financial position as these bonds are eliminated on consolidation under IAS 39 (‘Financial Instruments: Recognition and Measurement’) in EBS and under IFRS10 ‘Consolidated Financial Statements’.

### Mespil 1 RMBS Limited

The total carrying amount of the original residential property transferred by EBS and Haven Mortgages Limited to Mespil 1 RMBS Limited (‘Mespil’) as part of the securitisation amounted to €1,000m (EBS €290m; Haven Mortgages Limited €710m).

The amount of transferred secured loans that the Group continues to recognise as at 31 December 2013 is €926m (2012: €955m) in relation to the transfers from EBS and Haven Mortgages Limited. The fair value of these of these loans at 31 December 2013 was €855m.

Bonds issued by Mespil to EBS are not shown on the Group or Company statement of financial position as these bonds are eliminated on consolidation under IAS 39 (‘Financial Instruments: Recognition and Measurement’) in EBS and under IFRS10 ‘Consolidated Financial Statements’.

EBS participates in the securitisation through the provision of administration services and unsecured loan financing of €11m (2012: €10m), which is subordinated to the interest of the bond holders.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 15. SHARES IN GROUP UNDERTAKINGS

| *Company* | 2013 €m | 2012 €m |
|---|---|---|
| At 1 January | 537 | 537 |
| Investment in subsidiary | 75 | - |
| **At 31 December** | **612** | **537** |

**Principal subsidiary undertakings**:
All subsidiaries are 100% wholly owned unless otherwise stated.

(i) EBS indirectly holds 100% of the ordinary share capital in Hinsona Limited, incorporated in the Republic of Ireland. The company leases a property on behalf of the Group. The registered address of the company is Bankcentre, Ballsbridge, Dublin 4.

(ii) EBS holds 1 €1 ordinary share (100%) in Haven Mortgages Limited, incorporated in the Republic of Ireland. The company trades as a mortgage lender. The registered address of the company is 2 Burlington Road, Dublin 4.

(iii) EBS holds 551,540,000 (2012: 476,540,000) €1 ordinary shares (100%) in EBS Mortgage Finance incorporated in the Republic of Ireland on 30 October 2008 and regulated as a designated credit institution. EBS Mortgage Finance does not sell mortgage loans directly to the public. Instead it has an origination agreement with EBS whereby EBS continues to sell mortgage loans directly to the public and subsequently sells these loans to EBS Mortgage Finance for an appropriate consideration. The registered address of the company is 2 Burlington Road, Dublin 4.

On 20 December 2013, EBS Mortgage Finance issued 75,000,000 €1 ordinary shares at par.

The shares were issued to ensure that EBS Mortgage Finance would continue to exceed its regulatory capital requirement.
The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of EBS Mortgage Finance. All shares rank equally with regard to EBS Mortgage Finances' residual assets.

EBS assessed its investments in Group undertakings for impairment at 31 December 2013 in accordance with IAS 36 - Impairment of Assets. The carrying value is compared to the recoverable amount, which is the higher of value in use or fair value less costs to sell. The value in use being EBS' share of the future cash flows expected to be generated exceeds the carrying value for each investment.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### 16. PROPERTY, PLANT AND EQUIPMENT

**Group**

| | 2013 | | | | | 2012 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Free-hold €m | Long Leasehold €m | Short Leasehold €m | Fixtures & Fittings computer equipment & motor vehicles €m | Total €m | Free-hold €m | Long Leasehold €m | Short Leasehold €m | Fixtures & Fittings computer equipment & motor vehicles €m | Total €m |
| **Cost** | | | | | | | | | | |
| At 1 January | 29 | 10 | 19 | 23 | **81** | 30 | 10 | 19 | 23 | **82** |
| Additions | - | - | - | - | **-** | - | - | - | 1 | **1** |
| Disposals | (1) | - | (5) | (13) | **(19)** | - | - | - | (1) | **(1)** |
| Impairment | (1) | - | - | - | **(1)** | (1) | - | - | - | **(1)** |
| **At 31 December** | **27** | **10** | **14** | **10** | **61** | **29** | **10** | **19** | **23** | **81** |
| **Depreciation and impairment** | | | | | | | | | | |
| At 1 January | 7 | 4 | 16 | 18 | **45** | 7 | 3 | 14 | 18 | **42** |
| Charge for year | 1 | - | 1 | 1 | **3** | 1 | 1 | 2 | 1 | **5** |
| Disposals | (1) | - | (5) | (12) | **(18)** | - | - | - | (1) | **(1)** |
| Impairment charge | (1) | - | - | - | **(1)** | (1) | - | - | - | **(1)** |
| **At 31 December** | **6** | **4** | **12** | **7** | **29** | **7** | **4** | **16** | **18** | **45** |
| **Carrying value at 31 December** | **21** | **6** | **2** | **3** | **32** | **22** | **6** | **3** | **5** | **36** |

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### 16. PROPERTY, PLANT AND EQUIPMENT (continued)

**Company**

| | 2013 | | | | | 2012 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Free-hold €m | Long Leasehold €m | Short Leasehold €m | Fixtures & Fittings computer equip & motor vehicles €m | Total €m | Free-hold €m | Long Leasehold €m | Short Leasehold €m | Fixtures & Fittings computer equip & motor vehicles €m | Total €m |
| **Cost** | | | | | | | | | | |
| At 1 January | 29 | 10 | 19 | 23 | **81** | 30 | 10 | 19 | 22 | **81** |
| Additions | - | - | - | - | **-** | - | - | - | - | **-** |
| Reclassification | - | - | - | - | **-** | (1) | - | - | - | **(1)** |
| Disposals | (1) | - | (5) | (13) | **(19)** | **-** | - | - | (1) | (1) |
| Impairments | (1) | - | - | - | **(1)** | - | - | - | - | **-** |
| **At 31 December** | **27** | **10** | **14** | **10** | **61** | **29** | **10** | **19** | **21** | **79** |
| **Depreciation and impairment** | | | | | | | | | | |
| At 1 January | 7 | 4 | 16 | 18 | **45** | 7 | 3 | 14 | 17 | **41** |
| Charge for year | 1 | - | 1 | 1 | **3** | 1 | 1 | 2 | 1 | **5** |
| Reclassification | - | - | - | - | **-** | (1) | - | - | - | **(1)** |
| Disposals | (1) | - | (5) | (13) | **(19)** | - | - | - | (1) | **(1)** |
| Impairment charge | 1 | - | - | - | **1** | - | - | - | - | **-** |
| **At 31 December** | **8** | **4** | **12** | **6** | **30** | **7** | **4** | **16** | **17** | **44** |
| **Carrying value at 31 December** | **19** | **6** | **2** | **4** | **31** | **22** | **6** | **3** | **4** | **35** |

Land and buildings to the value of €32m (2012: €36m) are occupied by the Group for its own activities. The carrying value of land and buildings comprises Freeholds of €20m (2012: €22m), Long Leaseholds of €6m (2012: €6m) and Short Leaseholds of €2m (2012: €3m). The value of land and buildings under the historical cost basis are consistent with market values at year end.

At 31 December 2013, the Directors' reviewed property, plant and equipment for impairment in accordance with IAS 36 and concluded that impairment provisions were not required for 2013.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 17. INTANGIBLE ASSETS

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| **Computer software (and development costs)** | | | | |
| ***Cost*** | | | | |
| At 1 January | 72 | 70 | 78 | 76 |
| Additions - internally generated | 1 | 2 | 1 | 2 |
| Write offs | (40) | - | (40) | - |
| Reclassification (including AUC) | - | - | 1 | - |
| **At 31 December** | **33** | **72** | **40** | **78** |
| ***Amortisation*** | | | | |
| At 1 January | 57 | 54 | 61 | 56 |
| Charge for year | 4 | 3 | 5 | 5 |
| Write offs | (40) | - | (40) | - |
| **At 31 December** | **21** | **57** | **26** | **61** |
| **Carrying value at 31 December** | **12** | **15** | **14** | **17** |

Computer software costs are amortised on a straight line basis over a period not exceeding ten years and all are in use at 31 December 2013.

## 18. DEFERRED TAXATION

| | Company 2013 €m | Company 2012 €m Restated* | Group 2013 €m | Group 2012 €m Restated* |
|---|---|---|---|---|
| At 1 January | 311 | 196 | 252 | 172 |
| Current year tax losses | 18 | 88 | 29 | 104 |
| Deferred tax through equity | (11) | 27 | (2) | (24) |
| **At 31 December** | **318** | **311** | **279** | **252** |
| The amounts provided in relation to deferred taxation are as follows: | | | | |
| Retirement benefits | 5 | 8 | 5 | 8 |
| Amortised income | - | - | 16 | 1 |
| Available-for-sale financial assets | 47 | 51 | - | (2) |
| Unutilised tax losses | 265 | 251 | 291 | 277 |
| Other | 1 | 1 | - | 3 |
| Assets used in business | - | - | (8) | (8) |
| Other deferred tax liabilities | - | - | (25) | (27) |
| | **318** | **311** | **279** | **252** |

Comments on the basis of recognition of deferred tax assets on unused tax losses are included in critical accounting policies.

At 31 December 2013 recognised deferred tax assets on tax losses and other temporary differences, net of deferred tax liabilities, totalled €279m (2012: €252m). Net deferred tax assets of €264m (2012: €252m) are expected to be recovered after more than 12 months. The tax losses arise in the Irish tax jurisdiction and their utilisation is dependent on the generation of future taxable profits.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 18. DEFERRED TAXATION (continued)

Temporary differences recognised in other comprehensive income consist of deferred tax on available-for-sale securities, cash flow hedges and actuarial gain/loss on retirement benefit schemes. Temporary differences recognised in the income statement consist of provision for impairment of loans and advances, amortised income and assets used in the course of business.

## 19. OTHER ASSETS

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Items in transit - debit | (2) | 24 | - | 26 |
| Sundry debtors | 30 | 2 | 9 | 10 |
| | **28** | **26** | **9** | **36** |

## 20. DEPOSITS BY CENTRAL BANK AND BANKS

**Deposits by Central Bank and Banks –Analysis by Counterparty**

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| ECB repurchase agreements | 975 | 2,460 | 975 | 2,460 |
| Due to other banks | 54 | 222 | - | 222 |
| Due to Group undertaking | - | 58 | - | - |
| Due to AIB p.l.c | 665 | 16 | 665 | 16 |
| | **1,694** | **2,756** | **1,640** | **2,698** |
| **Balances placed by monetary authorities** | | | | |
| ECB repurchase agreements – average | 1,624 | 3,176 | 1,624 | 3,176 |
| ECB repurchase agreements – maximum | 2,490 | 4,515 | 2,490 | 4,515 |

**CONTRACTUAL MATURITY ANALYSIS**

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Repayable on Demand | 15 | 68 | - | 10 |
| 3 months or less | 1,040 | 2,088 | 1,040 | 2,088 |
| 5 years or less but over 1 year | 600 | 600 | 600 | 600 |
| Over 5 years | 39 | - | - | - |
| | **1,694** | **2,756** | **1,640** | **2,698** |

Borrowings from the ECB fell from the levels seen throughout 2012 as improved customer funding permitted repayments to the ECB. All borrowings from Central Bank of Ireland are fully collateralised. Further information on collateral provided is included in note 32.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 21. CUSTOMER ACCOUNTS

### CUSTOMER ACCOUNTS – CONTRACTUAL MATURITY ANALYSIS

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Repayable on demand | 2,183 | 1,428 | 1,406 | 1,428 |
| Repayable in less than three months but not on demand | 2,074 | 3,130 | 2,074 | 3,136 |
| Repayable in more than three months but less than one year | 3,959 | 3,518 | 3,960 | 3,518 |
| Repayable in more than one year but less than five years | 1,857 | 1,908 | 1,857 | 1,908 |
| Repayable in more than five years | - | 999 | - | 127 |
| | **10,073** | **10,983** | **9,297** | **10,117** |

### Customer Accounts – Analysis by Sector

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Retail | 6,483 | 7,431 | 6,484 | 7,431 |
| Corporate | 2,813 | 2,680 | 2,813 | 2,686 |
| Securitisation | 777 | 872 | - | - |
| | **10,073** | **10,983** | **9,297** | **10,117** |

The securitisation balances in the Company relate to loan notes issued to Emerald No.4 plc, secured on residential property, which are eliminated on consolidation. These are also referred to in note 14.

## 22. DEBT SECURITIES IN ISSUE

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Bonds and medium term notes | 1,153 | 1,252 | 2,001 | 2,148 |
| Commercial certificates of deposit | - | 34 | - | 34 |
| | **1,153** | **1,286** | **2,001** | **2,182** |
| **Maturity Profile – Debt Securities in Issue:** | | | | |
| Repayable in 3 months or less | 64 | 48 | 64 | 48 |
| Repayable in no more than 1 year but over 3 months | 25 | 31 | 75 | 31 |
| Repayable in more than 2 years but not more than 5 years | 1,064 | 1,207 | 1,064 | 1,257 |
| Repayable in more than 5 years | - | - | 798 | 846 |
| | **1,153** | **1,286** | **2,001** | **2,182** |

**Details of Debt Securities in Issue by currency are as follows:**

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| EURO | 1,153 | 1,245 | 2,001 | 2,141 |
| GBP | - | 41 | - | 41 |
| | **1,153** | **1,286** | **2,001** | **2,182** |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 22. DEBT SECURITIES IN ISSUE (CONTINUED)

**Debt securities in issue by geographical area**

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Republic of Ireland | 1,153 | 1,286 | 2,001 | 2,182 |
| | 1,153 | 1,286 | 2,001 | 2,182 |

The securitised bonds in the Group relate to bonds issued from Emerald Mortgages No. 4 plc, a securitisation vehicle, to third party investors. These are also referred to in Note 14.

During the year ended 31 December 2013 and 31 December 2012 no new debt securities were issued by the Group.

## 23. OTHER LIABILITIES

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Funding liabilities fair value hedge | 23 | 48 | 23 | 48 |
| Items in transit | 30 | 33 | 30 | 33 |
| Other liabilities | 37 | 75 | 16 | 20 |
| | **90** | **156** | **69** | **101** |

Other liabilities comprise Government guarantee scheme charges and trade creditors.

## 24. PROVISIONS FOR LIABILITIES AND COMMITMENTS

| | Company 2013 €m | Company 2012 €m Restated* | Group 2013 €m | Group 2012 €m Restated* |
|---|---|---|---|---|
| **Provisions** | | | | |
| At 1 January | 13 | 13 | 13 | 13 |
| Amounts charged to income statement | 7 | 7 | 7 | 7 |
| Amounts written back to income statement | (4) | (5) | (4) | (5) |
| Provisions utilised | (9) | (2) | (9) | (2) |
| **At 31 December** | **7** | **13** | **7** | **13** |

Provisions recognised include amounts in respect of voluntary severance scheme, onerous leases, customer repayments in respect of PPI and legal claims. The total expected to be settled within one year amounts to €7m (2012: €16m) for the Group and company.

In January 2013 EBS launched a voluntary severance programme which was made available to all staff, €14m was provided in relation to this.

## 25. RETIREMENT BENEFITS LIABILITY

The Company provides three funded defined benefit pension schemes, as well as one defined contribution scheme. These schemes were closed to future accrual and future contributions from 31 December 2013, and future pension provision for current employees is to be provided through the EBS Group Defined Contribution Scheme.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 25. RETIREMENT BENEFITS LIABILITY (CONTINUED)

**Defined benefit schemes**
Of the three defined benefit schemes, the two of most significance are the EBS Defined Benefit Pension Plan (the main Staff Plan) and EBS Pension Plan for Senior Management (the Senior Managers Plan).
Following the changes to the schemes at 31 December 2013, retirement benefits for active employees at that date are calculated by reference to service and Final Pensionable Salary at 31 December 2013. This calculation of benefit for each staff member will revalue between 1 January 2014 and retirement date in line with the statutory requirement to revalue deferred benefits. There is no link to any future changes in salaries, as was previously the case. This change gave rise to a negative past service cost of €13.1 million during 2013 – the Company has recognised this in the income statement and the gain is reflected in the benefit obligation at 31 December 2013. As part of the changes, the Company has given a commitment that the three defined benefit schemes will not be wound up before 30th June 2015 without the agreement of the trustees.

**Voluntary Severance Programme**
During 2013, 60 employees left EBS under the terms of a voluntary severance programme. No early retirement programme was provided - all of these leavers left with standard pension benefits. The Company has recognised a negative past service cost in the income statement and a reduction in the benefit obligation of €1.6 million as a result of these 60 leavers.

**Contributions**
Prior to the changes introduced in 2013, contributions were determined in accordance with an actuarial valuation carried out by Mercer, using the projected unit credit method. The most recent valuations were carried out as of 1 January 2011 and showed that the actuarial value of the schemes' assets represented 72% of the benefits that had accrued to members after allowing for expected future increases in earnings. The actuarial reports are available for inspection by members of the scheme and are not available for public inspection.

Following the 2013 changes, the Company contributions will be set out in the 6-year funding plan to be submitted to the Pensions Board. It is expected that this will result in Company contributions of €3.4 million for 2014 and €1.4 million per annum for subsequent years.

**Regulatory framework**
In Ireland, the Pensions Act provisions set out the requirement for a defined benefit scheme that fails the Minimum Funding Standard ('MFS') to have a funding plan in place and approved by the Pensions Board. The objective of an MFS funding plan is to set out the necessary corrective action to restore the funding of the scheme over a reasonable time period and enable the scheme to meet the MFS standard at a future date.

A funding plan is required in respect of all 3 defined benefit schemes. Negotiations are ongoing between the company and the trustees of each scheme with a view to submitting a 6-year funding plan to the Pensions Board.

**Responsibilities for governance**
The Trustees of each Company pension scheme are ultimately responsible for the governance of the schemes.

**Risks**
Pension risk is the risk that the funding position of the Company's defined benefit schemes would deteriorate to such an extent that the Company would be required to make additional contributions to cover its pension obligations towards current and former employees. Furthermore, for EBS, IAS pension deficits are now a deduction from capital under CRD IV which came into force on 1 January 2014.

While the Company has taken certain risk mitigating actions, a level of volatility associated with pension funding remains due to financial market fluctuations and changes to pension and accounting regulations. This volatility can be classified as market risk and actuarial risk. Market risk arises because the estimated market value of the pension scheme assets may decline or their investment returns may reduce due to market movements. Actuarial risk arises due to the risk that the estimated value of the pension scheme liabilities may increase due to changes in actuarial assumptions. The ability of the pension schemes to meet the projected pension payments is managed by the Trustees through the dynamic diversification of the investment portfolios across geographies and asset classes.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 25. RETIREMENT BENEFITS LIABILITY (CONTINUED)

**Maturity profile of the defined benefit obligation**
The following table shows the maturity profile of the defined benefit obligation and the weighted average duration of the defined benefit obligation

| | €m |
|---|---:|
| **Expected total benefit payments as at 31 December 2013 for the following years:** | |
| Year 1 | 3 |
| Year 2 | 3 |
| Year 3 | 3 |
| Year 4 | 4 |
| Year 5 | 4 |
| Next 5 years | 26 |
| **Weighted average duration of the defined benefit obligation (in years):** | **21** |

**Asset liability matching strategies**
The 6-year funding plan to be submitted to the Pensions Board will allow for a process of de-risking the investment strategy to reduce market risk – under Pensions Board guidelines there is a requirement for the investment strategy to take account of the liabilities by completion of the funding plan. The amounts recognised in the statement of financial position are determined as follows:

| | 2013 €m | 2012 €m Restated* |
|---|---:|---:|
| Present value of pension obligations | (179) | (197) |
| Fair value of plan assets | 142 | 135 |
| **Liability in the statement of financial position** | **(37)** | **(62)** |
| **Movement in the present value of pension obligations:** | | |
| At 1 January | (197) | (143) |
| Current service costs | (3) | (2) |
| Interest cost | (8) | (7) |
| Participants' contributions | (2) | (2) |
| Changes in demographic assumptions | 5 | - |
| Changes in financial assumptions | (1) | (47) |
| Effect of experience adjustments | 8 | 1 |
| Benefits paid from plan | 4 | 3 |
| Past service cost gain due to ceasing future accrual | 13 | - |
| Past service cost gain due to voluntary severance programme | 2 | - |
| **At 31 December** | **(179)** | **(197)** |
| **Movement in the fair value of plan assets:** | | |
| At 1 January | 135 | 115 |
| Expected return on plan assets | 5 | 6 |
| Employer contributions | 3 | 6 |
| Participants' contributions | 2 | 2 |
| Administrative Expenses | - | - |
| Return on scheme assets excluding interest income | 1 | 9 |
| Benefits paid from plan | (4) | (3) |
| **At 31 December** | **142** | **135** |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 25. RETIREMENT BENEFITS LIABILITY (CONTINUED)

**Asset liability matching strategies (continued)**

| | 2013 €m | 2012 €m Restated* |
|---|---|---|
| **The amounts recognised in the income statement are as follows:** | | |
| *Defined Benefit Schemes* | | |
| Current service costs | (3) | (2) |
| Interest cost | (8) | (8) |
| Past service cost gain due to voluntary severance programme | 2 | - |
| Past service cost gain due to ceasing future accrual | 13 | - |
| Administrative Expense | - | - |
| Future expected return on plan assets | 5 | 6 |
| **Total expenses (included in staff costs)** | **9** | **(4)** |

**Pension Plan Assets as at 31 December**
The following tables set out an analysis of the scheme assets at 31 December 2013 and 2012.

| | 2013 | 2012 Restated* |
|---|---|---|
| **Asset Category** | | |
| Cash and cash equivalents | - | - |
| Equities | - | - |
| Debt Instruments | - | - |
| Real Estate | - | - |
| Derivatives | - | - |
| Investment Funds | 142 | 135 |
| Asset backed securities | - | - |
| Structured debt | - | - |
| **Fair value of scheme assets as at 31 December** | **142** | **135** |

| | 2013 | 2012 Restated* |
|---|---|---|
| **Investment Funds** | | |
| Equity | 69 | 76 |
| Fixed Interest | 60 | 47 |
| Alternatives | | |
| - Quoted | 13 | 11 |
| - Unquoted | - | - |
| Cash | - | - |
| Property | - | 1 |
| **Total Investment funds** | **142** | **135** |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 25. RETIREMENT BENEFITS LIABILITY (CONTINUED)

**Pension Plan Assets as at 31 December (continued)**

The principal actuarial assumptions used for calculating the pension obligations were as follows:

| | 2013 | Restated* 2012 |
|---|---|---|
| Rate of inflation | 2.0% | 2.0% |
| Discount rate | 3.9% | 4.0% |
| Future salary increases* | - | 3.5% |
| Future pension increases | 2.0% | 2.0% |

*The rate of increase in salaries is not applicable in 2013, due to the closure of defined benefit schemes to future accrual. In 2012, the rate of increase in salaries included the impact of salary scale improvements.

Contributions are determined in accordance with the advice of Mercer, using the projected unit credit method. The most recent valuations were carried out as of 1 January 2011 and showed that the actuarial value of the schemes assets represented 72% of the benefits that had accrued to members after allowing for expected future increases in earnings. The actuarial reports are available for inspection by members of the scheme and are not available for public inspection.

None of the pension plans assets are invested in the Company's or Group's own financial instruments.

The main post retirement mortality assumptions used at 31 December 2013 were 108% Pensioners, males, Normal, lives. '00' series (PNML00) with no age rating for active, deferred members and pensioners, with future mortality improvements for active and deferred members.

On this basis the life expectancy for a male pensioner aged 65 at 31 December 2013 was 22.7 years (2012: 23.2 years) and for a female pensioner aged 65 years was 24.0 years (2012: 24.6 years). Based on the assumed mortality improvements in 15 years time the life expectancy for a male pensioner aged 65 years will have increased to 24.6 years (2012: 25.2 years) and for a female pensioner then aged 65 years will have increased to 25.7 years (2012: 26.4 years).

The contribution to be paid by the company in 2014 is estimated to be €3.4m and €1.4m per annum in subsequent years. The death in service premiums in 2014 is estimated to be €0.27m.

EBS funded payment of the Pension Levy in 2013. Further consideration is being given to whether the cost of the Pension Levy will be absorbed by EBS or the individual Defined Benefit pension plans.

**Sensitivity Analysis**

There are inherent uncertainties around the financial assumptions adopted in calculating the actuarial valuation of the pension schemes.

An increase or decrease in the discount rate of 25 basis points would reduce or increase the scheme liabilities by 5.4%.

An increase or decrease in the inflation rate of 25 basis points would reduce or increase the scheme liabilities by 3.9%.

The addition of a one year age offset to the mortality table in use would increase the scheme liabilities by 2.7%.

The sensitivity analysis has been prepared using the same methodology and limitations that are used in the calculation of the defined benefit obligation. There are no changes to the methods and assumptions used in preparing the sensitivity analysis from last year to this year.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 26. ORDINARY SHARE CAPITAL

**Group and Company**

| | 2013<br>€ | 2012<br>€ |
|---|---|---|
| Authorised: | | |
| 2,000,000,000 ordinary shares of €1 each | 2,000,000,000 | 2,000,000,000 |
| Issued and fully paid: | | |
| 1,655,000,000 ordinary shares of €1 each | 1,655,000,000 | 1,325,000,000 |

On 1 July 2011 EBS converted the special investment shares held by the Minister for Finance to ordinary shares following the conversion of EBS from a building society to a limited company. There were 1,000,000,000 ordinary shares authorised in €1 denominations and 625,000,000 €1 shares acquired by AIB p.l.c. directly from the Minister for Finance. Costs of €1.3m relating to the issuance of the special investment shares were transferred to ordinary share capital. Further information on the demutualisation of EBS and the issuance of special investment shares is set out in the accounting policies section.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of EBS. AIB p.l.c. is the sole holder of the issued share capital.

On 19th December 2013 EBS issued a further 330,000,000 €1 ordinary shares at par for cash to AIB p.l.c. These shares rank pari passu with the other ordinary shares issued. The shares were issued to ensure that the Bank continued to exceed its regulatory capital requirements.

On 27th July 2012 EBS issued 400,000,000 €1 ordinary shares at par for cash to AIB p.l.c. These shares rank pari passu with the other ordinary shares issued. The shares were issued to ensure that the Bank continued to exceed its regulatory capital requirements.

**Group and Company**

| | 2013<br>€m | 2012<br>€m |
|---|---|---|
| At 1 January | 1,324 | 924 |
| Issue of ordinary share capital | 330 | 400 |
| **At 31 December** | **1,654** | **1,324** |

## 27. CAPITAL CONTRIBUTION

**Group and Company**

| | 2013<br>€m | 2012<br>€m |
|---|---|---|
| Capital contribution | 249 | 249 |
| **At 31 December** | **249** | **249** |

A Promissory Note in the initial principal amount of €250m was issued by the Minister for Finance to EBS on 17 June 2010 pursuant to the Minister's powers under the Credit Institutions (Financial Support) Act, 2008. The Promissory Note is an unconditional promise in writing on behalf of the Minister for Finance to pay a defined sum of money to EBS on each instalment date as requested by EBS.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 27. CAPITAL CONTRIBUTION (continued)

**Group and Company (continued)**

On each adjustment date, being, if specified by the Minister, the date on which NAMA serves a completion notice or such other date as the Minister may specify, or if earlier the date of completion of a corporate transaction (i.e. a merger or sale) the Promissory Note may be adjusted to enable EBS meet its target core tier 1 and total capital ratios. In the case of an adjustment, the Promissory Note may be changed by the Minister to provide for that adjustment. The Promissory Note is payable in instalments of 10% of the principal outstanding amount per annum. Interest accrues on the Promissory Note at an agreed coupon rate and may be adjusted by the Minister at any time. No dividends can be paid by EBS during the term of the Promissory Note.

The Promissory Note is recognised as an available-for-sale financial asset in the Statement of Financial Position at its fair value (note 11).

The related capital arising on recognition of the Promissory Note is recognised as a capital contribution in shareholders' equity. Under the Promissory Note there is no obligation on EBS to make any repayments, returns or distributions on the capital contribution received.

There was no change to the terms of the Promissory Note on the acquisition of EBS by AIB p.l.c.

## 28. LEASING COMMITMENTS

**Group and Company**

| | 2013<br>€m | 2012<br>€m |
|---|---|---|
| At 31 December, future minimum payments under non cancellable operating leases relating to land and buildings are as follows: | | |
| Payments to be made in: | | |
| Less than one year | 7 | 7 |
| Between one and five years | 17 | 22 |
| After five years | 10 | 12 |
| | **34** | **41** |

These leases have average lives of between 25 and 35 years with renewal options included in the contracts.
The actual amount incurred on operating lease charges in 2013 was €7m (2012: €7m).

## 29. CAPITAL COMMITMENTS

**Group and Company**

| | 2013<br>€m | 2012<br>€m |
|---|---|---|
| Capital expenditure contracted but not provided for | - | - |
| Capital expenditure authorised but not contracted | - | 1 |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 30. DERIVATIVE FINANCIAL INSTRUMENTS

**Group**

Group operations are exposed to the risk of interest rate fluctuations to the extent that assets and liabilities mature or re-price at different times or in differing amounts. Derivatives allow the Group to modify the re-pricing characteristics of assets and liabilities in a cost efficient manner. This flexibility helps the Group to achieve liquidity and risk management objectives.

Derivatives fluctuate in value as interest or exchange rates rise or fall just as all assets and liabilities fluctuate in value. If the derivatives are purchased or sold as hedges of Statement of Financial Position items, the appreciation or depreciation of the derivatives as interest or exchange rates change, will generally be offset by the unrealised appreciation or depreciation of the hedged items.

To achieve its risk management objectives, the Group uses a combination of derivative financial instruments, particularly interest rate swaps, currency swaps and equity index swaps. The Group only engages in derivative activity for hedging purposes, although all swaps are considered to be effective hedges in economic terms, due to the nature of some it is not possible to establish a ‘Fair Value’ or ‘Cash Flow’ hedging relationships under IAS 39, such swaps are classified as ‘Held at fair value through the Income Statement’.

Derivative instruments are contractual agreements whose value is derived from the price movements in underlying assets, interest rates, exchange rates or indices.
Derivatives are an efficient and cost effective means of managing market risk and limiting counterparty exposure. The Board approves policy with respect to credit risk, market risk and liquidity risk and has delegated its monitoring and control responsibilities to the Group Asset and Liability Committee. However the Board continues to retain ultimate responsibility for these risks. Membership of the Group Asset and Liability Committee consists of senior management as well as management team members.

During 2013 the Bank novated the majority of derivatives (both by value and numbers) with external counterparties to AIB p.l.c, replacing them with identical swaps with AIB p.l.c. as counterparty. Hedge accounting was not discontinued where replacement swaps were booked on the same terms as the novated swaps.

**Fair value hedges**

The Group hedges part of its existing interest rate and foreign currency risk resulting from any potential movement in the fair value of fixed rate assets or liabilities and movement in fair value of assets and liabilities denominated in foreign currencies using interest rate and cross-currency interest rate swaps. The fair value excluding accrued interest of these swaps at 31 December 2013 was €23m (2012: €11m).

**Cash flow hedges**

The Group also hedges part of its existing interest rate risk from any potential movement in variable cash flows using interest rate swaps. The fair value excluding accrued interest of these swaps at 31 December 2013 was €9m (2012: €18m).

The weighted average remaining term of the Group's cash flow hedges is 3.9 years (2012: 2.3 years). The maximum remaining term of any individual cash flow hedge is 7.2 years (2012: 8.2 years).

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 30. DERIVATIVE FINANCIAL INSTRUMENTS (continued)

**Cash flow hedges (continued)**

**Group**

| | 2013 | | | 2012 | | |
|---|---|---|---|---|---|---|
| | Notional amount | Fair values | | Notional amount | Fair values | |
| | | Assets | Liabilities | | Assets | Liabilities |
| | €m | €m | €m | €m | €m | €m |
| **Derivatives held at fair value through the income statement** | | | | | | |
| Interest rate swaps | 2,013 | 42 | 44 | 3,100 | 64 | 60 |
| Cross currency interest rate swaps | - | - | - | - | - | - |
| **Interest rate contracts total** | **2,013** | **42** | **44** | **3,100** | **64** | **60** |
| Currency swaps | - | - | - | 44 | - | 1 |
| **Foreign exchange derivatives total** | **-** | **-** | **-** | **44** | **-** | **1** |
| Equity index options | - | - | - | 7 | 1 | 1 |
| **Equity index contracts total** | **-** | **-** | **-** | **7** | **1** | **1** |
| **Total contracts at fair value through the income statement** | **2,013** | **42** | **44** | **3,151** | **65** | **62** |
| **Derivatives classified as fair value hedging** | | | | | | |
| Interest rate swaps | 1,181 | 56 | 7 | 1,963 | 85 | 61 |
| **Derivatives classified as cashflow hedges** | | | | | | |
| Interest rate swaps | 7,424 | 22 | 29 | 7,632 | 40 | 63 |
| **Total hedging contracts** | **8,605** | **78** | **36** | **9,595** | **125** | **124** |
| **Total derivative financial instruments** | **10,618** | **120** | **80** | **12,746** | **190** | **186** |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 30. DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

**Company**

| | 2013 | | | 2012 | | |
|---|---|---|---|---|---|---|
| | Notional amount | Fair values Assets | Fair values Liabilities | Notional amount | Fair values Assets | Fair values Liabilities |
| | €m | €m | €m | €m | €m | €m |
| **Derivatives held at fair value through the income statement** | | | | | | |
| Interest rate swaps | 7,762 | 75 | 40 | 8,219 | 100 | 54 |
| Cross currency interest rate swaps | - | - | - | - | - | - |
| **Interest rate contracts total** | **7,762** | **75** | **40** | **8,219** | **100** | **54** |
| Currency swaps | - | - | - | 44 | - | 1 |
| **Foreign exchange derivatives total** | - | - | - | **44** | **-** | **1** |
| Equity index options | - | - | - | 7 | 1 | 1 |
| **Equity index contracts total** | - | - | - | **7** | **1** | **1** |
| **Total contracts at fair value through the income statement** | **7,762** | **75** | **40** | **8,270** | **101** | **56** |
| **Derivatives classified as fair value hedging** | | | | | | |
| Interest rate swaps | 1,181 | 56 | 7 | 1,963 | 85 | 61 |
| **Derivatives classified as cashflow hedges** | | | | | | |
| Interest rate swaps | 7,424 | 22 | 29 | 7,632 | 40 | 63 |
| **Total hedging contracts** | **8,605** | **78** | **36** | **9,595** | **125** | **124** |
| **Total derivative financial instruments** | **16,367** | **153** | **76** | **17,865** | **226** | **180** |

The derivative maturity table on the next page analyses the asset and liability fair value amounts by maturity bucket.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 30. DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

**Derivative Maturity Table – at 31 December 2013**

**Group**

| | Less than 1 year €m | Over 1 year but not more than 5 years €m | Over 5 years €m | Total €m |
|---|---|---|---|---|
| Interest rate contracts | 9 | 111 | - | 120 |
| **Total assets** | **9** | **111** | **-** | **120** |

**Derivative Maturity Table – at 31 December 2012**

**Group**

| | Less than 1 year €m | Over 1 year but not more than 5 years €m | Over 5 years €m | Total €m |
|---|---|---|---|---|
| Interest rate contracts | 72 | 76 | 41 | 189 |
| Foreign exchange contracts | 1 | - | - | 1 |
| **Total assets** | **73** | **76** | **41** | **190** |

**Derivative Maturity Table – at 31 December 2013**

**Company**

| | Less than 1 year €m | Over 1 year but not more than 5 years €m | Over 5 years €m | Total €m |
|---|---|---|---|---|
| Interest rate contracts | 9 | 138 | 6 | 153 |
| **Total assets** | **9** | **138** | **6** | **153** |

**Derivative Maturity Table – at 31 December 2012**

**Company**

| | Less than 1 year €m | Over 1 year but not more than 5 years €m | Over 5 years €m | Total €m |
|---|---|---|---|---|
| Interest rate contracts | 99 | 85 | 41 | 225 |
| Foreign exchange contracts | 1 | - | - | 1 |
| **Total assets** | **100** | **85** | **41** | **226** |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 31. COMMITMENTS AND CONTINGENT LIABILITIES

**Group and Company**

(i) At 31 December 2013 Group and Company loan approvals not advanced, as calculated under the Basel II definition, amount to €59m (2012: €13m) and €42m (2012: €13m) respectively.

(ii) Legal proceedings

EBS in the course of its business is frequently involved in litigation cases. However, it is not, nor has it been involved in, nor are there, so far as the Company is aware, pending or threatened by or against EBS any legal or arbitration proceedings, including governmental proceedings, which may have, or have had during the previous twelve months, a material effect on the financial position, profitability or cashflows of EBS.

(iii) Contingent liability / contingent asset - NAMA

On dissolution or restructuring of NAMA, the Minister may require that a report and accounts be prepared. If NAMA shows that an aggregate loss has been incurred since its establishment which is unlikely to be made good, the Minister may impose a surcharge on the participating institutions. This will involve apportioning the loss on the participating institution, subject to certain restrictions, on the basis of the book value of the assets acquired from that institution in relation to the total book value of assets acquired from all participating institutions.

(iv) TARGET 2 – Gross settlement system

EBS migrated to the TARGET 2 system during 2008. TARGET 2, being the wholesale payment infrastructure for credit institutions across Europe, is a real time gross settlement system for large volume interbank payments in euro. The following disclosures relate to the charges arising as a result of the migration to TARGET 2.

On 15 February 2008, a first floating charge was placed in favour of the Central Bank of Ireland over all EBS' right, title, interest and benefit, present and future, in and to:

(i) the balances now or at any time standing to the credit of EBS' account held as a TARGET 2 participant with the Central Bank of Ireland ('the Charged Property'); and

(ii) certain segregated securities ('the Charged Property') listed in an Eligible Securities Schedule kept by EBS for the purpose of participating in TARGET 2.

These floating charges contain a provision whereby during the subsistence of the security, otherwise than with the prior written consent of the Central Bank of Ireland, EBS shall:

(a) not create or attempt to create or permit to arise or subsist any encumbrance on or over the charged property or any part thereof: or

(b) not, otherwise than in the ordinary course of business, sell, transfer, lend or otherwise dispose of the charged property or any part thereof or attempt or agree to do so whether by means of one or a number of transactions related or not and whether at one time or over a period of time.

## 32. PLEDGED COLLATERAL

| | Company 2013 €m | Company 2012 €m | Group 2013 €m | Group 2012 €m |
|---|---|---|---|---|
| Debt securities | - | 845 | - | 845 |
| Asset backed securities (own issue) | 1,071 | 2,162 | - | - |
| | **1,071** | **3,007** | **-** | **845** |

Pledged collateral can be collateral pledged to the ECB, Central Bank of Ireland (CBI) or to market counterparties. ECB pledged collateral is comprised of financial assets that are pledged to the ECB as part of sale & repurchase (repo) agreements.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 32. PLEDGED COLLATERAL (CONTINUED)

These financial assets are ECB eligible assets in the form of government bonds, treasury bills debt securities issued by monetary financial institutions, asset backed securities (own issue) in the form of Emerald Mortgages No.5, Mespil and covered bonds issued by EBS Mortgage Finance. CBI pledged collateral is comprised of retail homeloan assets in the form of a Mortgage Backed Promissory Note (MBPN) that is pledged to the CBI as part of sale & repurchase (repo) agreements. Market counterparty pledged collateral are financial assets pledged as collateral as part of a sale & repurchase agreement (repo) with other credit institutions as market counterparts. These financial assets are in the form of government bonds and debt securities issued by monetary financial institutions. All of these repos are covered by repo master agreements and are subject to daily repo margin processes.

These transactions are conducted under terms that are usual and customary to standard lending and securities borrowing and lending activities, as well as requirements determined by exchanges where EBS acts as an intermediary.

The transferee has a right by contract or custom to sell or re-pledge the collateral under certain circumstances. These circumstances would arise if EBS breaches the standard securities lending and borrowing agreements.

The Group had €0.3bn (2012: €0.3bn) of unencumbered contingent collateral available at 31 December 2013 comprising residential mortgage assets of €0.1bn (2012: €0.1bn) and debt securities of €0.2bn (2012: €0.2bn).

## 33. RELATED PARTY TRANSACTIONS

**Group**

Details of the principal subsidiary undertakings are shown in Note 15. In accordance with IAS 24 - related party disclosures, transactions or balances between group entities that have been eliminated on consolidation are not reported.

The immediate holding company and controlling party is EBS Limited, with a registered office at 2 Burlington Road, Dublin 4. The ultimate holding entity and controlling party is Allied Irish Banks, p.l.c, with a registered office at Bankcentre, Ballsbridge, Dublin 4. Copies of both EBS Group and AIB Group financial statements are available from the registered office of Allied Irish Banks, p.l.c. The only related party transactions are normal banking transfers to and from EBS.

**The Irish Government and Government related entities**

The Irish Government has taken a range of measures to stabilise the Irish banking system since the commencement of the financial crisis in 2008. These measures have included the injection of equity and preference share capital into AIB p.l.c. As a result of these capital injections, the Irish Government, through the National Pension Reserve Fund Commission, now holds 99.8% of the ordinary shares of AIB p.l.c. and €3.5bn in 2009 Preference Shares. In addition, the Minister for Finance holds €1.6bn of contingent capital notes.

As a result of the various measures taken by the Irish Government (specifically the guarantee schemes, the Direction Order, and the capital injections) the Irish Government is a related party to AIB p.l.c. and therefore EBS. Details regarding these measures, as well as others taken in the context of the Irish banking crisis, are set out below.

The Minister for Finance (the 'Minister') and/or the Central Bank of Ireland has considerable rights and powers over the operations of the AIB Group (and other financial institutions) arising from the various stabilisation measures.

These rights and powers include, inter alia:

- The acquisition of shares in other institutions;
- Maintenance of solvency ratios and compliance with any liquidity and capital ratios that the Central Bank of Ireland, following consultation with the Minister, may direct;
- The appointment of non-executive directors and board changes;
- The appointment of persons to attend meetings of various committees;
- Restructuring of executive management responsibilities, strengthening of management capacity and improvement of governance;
- Declaration of payment dividends;

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 33. RELATED PARTY TRANSACTIONS (CONTINUED)

**The Irish Government and Government related entities (continued)**

- Restrictions on various types of remuneration;
- Buy-backs or redemption of its shares;
- The manner in which the Group extends credit to certain customer groups; and
- Conditions regulating the commercial conduct of AIB p.l.c., having regard to capital ratios, market share and the Group’s balance sheet growth.

**(a) Irish Government Guarantee Schemes:**

EBS and its subsidiary EBS Mortgage Finance are covered institutions under the Government's Credit Institutions (Finance Support) Scheme 2008 (the ‘CIFS Scheme’) which guaranteed covered liabilities raised by covered institutions up to 29 September 2010. Covered liabilities that were covered by the CIFS Scheme were those liabilities in respect of retail and corporate deposits (to the extent not covered by existing deposit protection scheme in Ireland or any other jurisdiction), inter-bank deposits and senior unsecured debt excluding any intra group borrowing and any debt due to the ECB of Ireland arising from Euro system monetary operations. Under the terms of the CIFS Scheme the Central Bank of Ireland in consultation with the Minister regulated the commercial conduct of covered institutions strictly in order to achieve the objectives of this scheme.

EBS is a participating institution under the Government's Credit Institutions (Eligible Liabilities Guarantee) Scheme 2009 which guarantees certain eligible liabilities (including deposits) of up to five years in maturity.

The European Commission approved the extension of the ELG issuance period to the 30 June 2012 in December 2011 and again in June 2012 for the period to 31 December 2012 as six months is the maximum period permitted for state aid approval under the European Commission’s policy on guarantee schemes in the financial sector.

In December 2012, the European Commission further extended the ELG issuance to the 30 June 2013. On 26 February 2013, the Irish Government announced that the ELG would end at midnight on 28 March 2013. After that date no new liabilities were covered by the Eligible Liabilities Guarantee Scheme. Liabilities incurred since January 2010 and before the scheme's end will continue to be guaranteed until their next maturity, which can last for five years.

The total amount of guaranteed deposits and senior unsecured debt raised by EBS as a covered institution under the Government Guarantee ELG scheme at 31 December 2013 amounted to €3,094m (December 2012: €5,487m).

In 2013, €47m was charged to EBS under the ELG scheme (2012: €55m).

**(b) Promissory Note**

On 17 June 2010 a Promissory Note in the initial principal amount of €250m was issued by the Minister for Finance to EBS pursuant to the Minister’s powers under the Credit Institutions (Financial Support) Act, 2008. Further information on the promissory note is included in note 27. Interest earned on the Promissory Note for the year ending 31 December 2013 amounted to €12m (2012: €13m).

The terms and conditions regarding the Promissory Note and Capital Contribution have remained unchanged.

**(c) National Asset Management Agency (NAMA)**

The Irish Government set up an asset relief scheme in 2009 under the auspices of the National Asset Management Agency in Ireland. EBS is a participating institution in NAMA.

Senior unsecured floating rate notes and callable perpetual subordinated fixed rate bonds were received as consideration from NAMA for the transfer of loans and advances. Further information on this is included in notes 8, 11 and 12. Interest earned on these bonds in 2013 amounted to €1m (2012: €4m).

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 33. RELATED PARTY TRANSACTIONS (CONTINUED)

**(d) Credit Institutions (Stabilisation) Act 2010**
The Credit Institutions (Stabilisation) Act 2010 ('the Act') was passed into Irish law on 21 December 2010. The Act provides the legislative basis for the reorganisation and restructuring of the Irish banking system agreed in the joint EU/IMF Programme for Ireland ('the Programme'). This will allow the Minister for Finance ('the Minister') to take the actions required to bring about a domestic retail banking system that is proportionate to and focused on the Irish economy.

The Act provides broad powers to the Minister (in consultation with the Governor of the Central Bank of Ireland) to act on financial stability grounds to effect the restructuring actions and recapitalisation measures envisaged in the Programme. The Act applies to banks which have received financial support from the State, building societies and credit unions. Given the exceptional nature of the powers contained in the Act, the powers are time-limited and were scheduled to expire on 31 December 2012. However, in January 2013, the Minister extended the period of effectiveness of the Act for a further period of two years until 31 December 2014.

The powers provided in the Act allow the Minister to implement key aspects of the agreed Programme for bank restructuring and include the issue of direction orders, special management orders, subordinated liabilities orders and transfer of assets and liabilities orders. In addition, the Act gives the Minister broad powers in relation to directors and officers and their appointment/removal/duties. Various other terms are also imposed on relevant financial institutions as a condition for financial support.

**(e) Funding Support**
EBS received funding from the ECB throughout the year through the ECB Monetary Policy Operation Sale and Repurchase Agreements. This funding amounted to €975m at 31 December 2013 (2012: €2,460m). Other funding supports from the Central Bank of Ireland, which had been in operation at 31 December 2010, were not availed of by EBS from May 2011 onwards.

**(f) Central Bank of Ireland and Credit Institutions (Resolution) Act 2011**
The Central Bank of Ireland and Credit Institutions (Resolution) Act 2011 (the 'Act') was signed into law on 20 October 2011 and became effective on 28 October 2011.

This legislation provides the Central Bank of Ireland with additional powers to achieve an effective and efficient resolution regime for credit institutions that are failing or likely to fail and that is effective in protecting the Exchequer and the stability of the financial system and the economy.

The Act give the Central Bank of Ireland power to take control of banks, appoint managers to run them and remove directors, staff and consultants and to move their deposits and loans to other banks. It provides for the establishment of a Credit Institution Resolution Fund which would provide a source of funding for the resolution of financial instability or in the event of an imminent serious threat to the financial stability of an authorised credit institution. Authorised credit institutions will be obliged to contribute to the resolution fund.

The Act provides for the establishment of 'Bridge-Banks' for the purposes of holding assets or liabilities which have been transferred under a transfer order. Bridge-Banks are only intended to hold such assets or liabilities on a temporary basis pending onward transfer as soon as possible.

The Central Bank of Ireland will also be empowered to make special management orders in relation to an authorised credit institution or in relation to a subsidiary or holding company of the authorised credit institution in certain circumstances. The Act also provides powers to the Central Bank of Ireland regarding the liquidation of authorised credit institutions. Authorised credit institutions may also be directed to prepare a recovery plan setting out actions that could be taken to facilitate the continuation or secure the business or part of the business of that institution.

The legislation is expected to, in due course, replace the provisions of the Credit Institutions (Stabilisation) Act 2010 outlined above which ceases to have effect on 31 December 2014 or at a later date substituted by resolution of both Houses of the Oireachtas.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 33. RELATED PARTY TRANSACTIONS (CONTINUED)

**(g) Government related entities**
As a result of the capital received from Government in 2010 and the participation in the Government guarantee scheme, the Government is recognised as a related party, as defined under the accounting standards.

In the normal course of business the Group has various transactions with the Government, state departments and semi-state bodies and state owned financial institutions including the holding of securities issued by the Government and semi-state bodies of €217m (December 2012: €697m).

At 31 December 2013 deposits by banks and state owned financial institutions included deposits of nil (December 2012: nil) placed by the National Treasury Management Agency (NTMA).

During 2009 and 2010 the Government acquired 100% of shares in Anglo Irish Bank Corporation limited ('Anglo'), acquired a controlling interest in Irish Nationwide Building Society, Allied Irish Bank plc and acquired a significant influence over Bank of Ireland. As the Government also took a controlling interest in the EBS Limited, balances between the Group and each of the other aforementioned institutions are considered to be related party transactions. These institutions are members of the Credit Institutions (Eligible Liabilities Guarantee) Scheme 2009 ('ELG Scheme').

The following table sets out the aggregate balance between the Group and these financial institutions.

| As at 31 December | Available-for-sale financial assets €m | Derivative financial instruments (Assets) €m | Loans and advances to credit institutions €m | Deposits by credit institutions €m | Derivative financial instruments (Liabilities) €m |
|---|---|---|---|---|---|
| 2013 | 224 | 83 | 1,190 | 1,640 | 41 |
| 2012 | 605 | 30 | 606 | 16 | 7 |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 33. RELATED PARTY TRANSACTIONS (CONTINUED)

### (h) Subsidiaries and special purpose vehicles

**Company**
A number of transactions are entered into with subsidiaries and special purpose vehicles in the normal course of business by EBS. Loans to related parties include subsidiaries and securitisation vehicles and deposits from related parties include non-recourse funding from securitisation vehicles. The interest charged to related parties is at normal commercial rates appropriate to the transaction. There is no provision for doubtful debts relating to amounts owed by subsidiaries.

| | 2013<br>€m | 2012<br>€m |
|---|---|---|
| ***Loans to related parties*** | | |
| At 1 January | 3,782 | 4,152 |
| Net movement in loans during the year | (273) | (370) |
| **At 31 December** | 3,509 | 3,782 |
| ***Deposits from related parties*** | | |
| At 1 January | 3,009 | 3,129 |
| Net movement in deposits during the year | (201) | (120) |
| **At 31 December** | 2,808 | 3,009 |
| ***Included in the Income Statement*** | | |
| Interest income on loans | 5 | 5 |
| Interest expense on loans | 114 | 145 |
| Other income | 7 | 41 |
| **Derivative financial instruments with subsidiary (EBS Mortgage Finance)** | | |
| **Interest rate swaps** | | |
| Notional Principal amount | 6,622 | 6,913 |
| Assets (Fair value) | 33 | 35 |
| Liabilities (Fair value) | 33 | 35 |
| Net Trading Income | 5 | 10 |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 33. RELATED PARTY TRANSACTIONS (CONTINUED)

### (i) Transactions with parent company AIB p.l.c.

A number of transactions were also entered into with the ultimate parent, AIB p.l.c., in the normal course of business. These include loans, deposits, derivatives and available-for-sale assets.

| | 2013 €m | 2012 €m |
|---|---|---|
| ***Loans*** | | |
| At 1 January | 598 | 78 |
| Net movement in loans during the year | 503 | 520 |
| **At 31 December** | 1,101 | 598 |
| ***Available-for-sale financial asset*** | | |
| At 1 January | 202 | 238 |
| Net movement in deposits during the year | (202) | (36) |
| **At 31 December** | - | 202 |
| ***Derivative financial instruments (assets fair value)*** | | |
| At 1 January | 30 | 10 |
| Issued in the year | 53 | 20 |
| **At 31 December** | 83 | 30 |
| ***Deposits from related parties*** | | |
| At 1 January | 16 | 1,151 |
| Net movement in deposits during the year | 649 | (1,135) |
| **At 31 December** | 665 | 16 |
| ***Derivative financial instruments (liabilities fair value)*** | | |
| At 1 January | 7 | 8 |
| Issued in the year | 34 | (1) |
| **At 31 December** | 41 | 7 |
| ***Derivative financial instruments*** | | |
| Notional Principal amount | 8,872 | 6,953 |
| ***Included in the Income Statement*** | | |
| Interest income | 73 | 43 |
| Interest expense | (29) | (3) |
| Net Trading Income | 3 | 6 |
| Administrative expenses | - | (1) |

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 33. RELATED PARTY TRANSACTIONS (CONTINUED)

### (j) Transactions with key management personnel

For the purpose of IAS 24 related part disclosures, 'key management personnel' comprises executive and non executive directors.

Loans to the key management personnel are made in the ordinary course of business. No current directors in office during 2012, had loan facilities with EBS Limited and its subsidiaries during the year ended 31 December 2012. The following amounts represent the transactions and outstanding balances with the Group:

| | 2013 €m | 2012 €m |
|---|---|---|
| **Transactions during the period:** | | |
| Loan advances | - | - |
| Loan repayments | - | - |
| Interest on loans | - | - |
| **The savings balances for key management personnel amount to (maximum in 2013: €0.3m (2012: €0.1m)).** | **-** | **-** |

### (k) Compensation of key management personnel:

Total compensation to key management personnel is as follows:

| | 2013 €m | 2012 €m |
|---|---|---|
| Fees | 0.1 | 0.1 |
| Salary and other benefits | 0.3 | 0.5 |
| Pension benefits | 0.1 | 0.2 |
| | **0.5** | **0.8** |

Details of executive directors are as follows:

| | Salary | | Benefits | | Total | |
|---|---|---|---|---|---|---|
| **Executive Directors** | **2013 €m** | **2012 €m** | **2013 €m** | **2012 €'000** | **2013 €m** | **2012 €m** |
| Desmond Fitzgerald (1) | 0.3 | 0.1 | - | - | 0.3 | 0.1 |
| Fergus Murphy (2) | - | 0.3 | - | 0.1 | - | 0.4 |
| | **0.3** | **0.4** | **-** | **0.1** | **0.3** | **0.5** |

(1) Desmond Fitzgerald was appointed a Director of EBS on 16 July 2012.
(2) Fergus Murphy ceased to be a Director of EBS on 21 November 2012.

Benefits provided to the Executive Directors were the provision of car allowances, contributions to health insurance, subsidised home loans and club subscriptions. Subsidised home loans to Executive Directors are on the same terms and conditions as loans to other eligible EBS management and staff. Executive Directors do not receive any additional reward for their work as members of the EBS Board.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 33. RELATED PARTY TRANSACTIONS (CONTINUED)

**(k) Compensation of key management personnel (continued):**
Desmond Fitzgerald has a personal defined contribution pension scheme. In 2013, €68,750 (2012: €38,183 in respect of the period from the date of his appointment as Director) was paid to a defined contribution scheme on behalf of Desmond Fitzgerald. In 2013 no payment (2012: €116,455) was paid to a defined contribution scheme on behalf of Fergus Murphy.

The remuneration of the Independent Non Executive Directors in 2013 is set out below:

| | 2013 €'000 | 2012 €'000 |
|---|---|---|
| Catherine Woods | 29.0 | 29.0 |
| James O'Hara (1) | 29.0 | 14.9 |
| Tom Foley (2) | 29.0 | 3.3 |
| | **87.0** | **47.2** |

(1) James O'Hara was appointed as an Independent Non Executive director on 26 June 2012
(2) Tom Foley was appointed as an Independent Non Executive director on 21 November 2012

At 31 December 2013, the Board of Directors is comprised of Denis O'Callaghan, Bernard Byrne, Catherine Woods, Tom Foley, James O'Hara, Fidelma Clarke and Desmond Fitzgerald.

The remuneration of Group Non Executive Directors (Denis O'Callaghan, Bernard Byrne, and Fidelma Clarke) is borne by the Parent.

**Long term incentive plans**
There were no conditional grants of awards of ordinary shares outstanding to Executive Directors or the Company Secretary at 31 December 2013.

Independent Non-Executive Directors do not participate in long term incentive plans.

Apart from the interests set out above, the Directors and Secretary and their spouses and minor children have no other interests in the shares of Allied Irish Banks, p.l.c.

There were no changes in the Directors' and Secretary's interests between 31 December 2013 and 13 March 2013.

## 34. FAIR VALUE OF FINANCIAL INSTRUMENTS

The term 'financial instruments' includes both financial assets and financial liabilities. The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Bank has access at that date. The Companys' accounting policy for the determination of fair value of financial instruments is set out in accounting policy number 1.18.

Readers of these financial statements are advised to use caution when using the data in the following table to evaluate the Companys' financial position or to make comparisons with other institutions. Fair value information is not provided for items that do not meet the definition of a financial instrument. These items include intangible assets such as the value of the branch network and the long-term relationships with depositors, premises and equipment and shareholders' equity. These items are material and accordingly, the fair value information presented does not purport to represent, nor should it be construed to represent, the underlying value of the Bank as a going concern at 31 December 2013.

The valuation of financial instruments, including loans and advances, involves the application of judgement and estimation. Market and credit risks are key assumptions in the estimation of the fair value of loans and advances. During the year, the Company has continued to observe adverse changes in the credit quality of its borrowers, with increasing delinquencies and defaults across a range of sectors.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 34. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

The volatility in financial markets and the illiquidity that is evident in these markets has reduced the demand for many financial instruments and this creates a difficulty in estimating the fair value for loans to customers. The Company has estimated the fair value of its loans to customers taking into account market risk and the changes in credit quality of its borrowers.

Fair values are based on observable market prices where available, and on valuation models or techniques where the lack of market liquidity means that observable prices are unavailable. The fair values of financial instruments are measured according to the following fair value hierarchy:
**Level 1** – financial assets and liabilities measured using quoted market prices from an active market (unadjusted).
**Level 2** – financial assets and liabilities measured using valuation techniques which use quoted market prices from an active market or measured using quoted market prices unadjusted from an inactive market.
**Level 3** – financial assets and liabilities measured using valuation techniques which use unobservable market data.

All financial instruments are initially recognised at fair value. Financial instruments held for trading and financial instruments in fair value hedge relationships are subsequently measured at fair value through profit or loss. Available for sale securities and cash flow hedge derivatives are subsequently measured at fair value through other comprehensive income.

All valuations are carried out within the Finance function of the Company and valuation methodologies are validated by the independent Risk function within the Bank.

The methods used for calculation of fair value are as follows:

**Financial instruments measured at fair value in the financial statements**

***Derivative financial instruments***
Where derivatives are traded on an exchange, the fair value is based on prices from the exchange. The fair value of over the counter derivative financial instruments is estimated based on standard market discounting and valuation methodologies which use reliable observable inputs including yield curves and market rates. These methodologies are implemented by the Finance function and validate by the Risk function. Where there is uncertainty around the inputs to a derivatives' valuation model, the fair value is estimated using inputs which provide the Companies view of the most likely outcome in a disposal transaction between willing counterparties in a functioning market. Where an unobservable input is material to the outcome of the valuation, a range of potential outcomes from favourable to unfavourable are estimated.

**Financial instruments not measured at fair value but with fair value information presented separately in the notes to the financial statements**

***Loans and advances to credit institutions***
The fair value of loans and advances to credit institutions is estimated using discounted cash flows applying either market rates, where practicable, or rates currently offered by other financial institutions for placings with similar characteristics.

***Loans and advances to customers***
The Bank provides lending facilities of varying rates and maturities to corporate and personal customers. Valuation techniques are used in estimating the fair value of loans, primarily using discounted cash flows and applying market rates where practicable.

In addition to the assumptions set out above under valuation techniques regarding cash flows and discount rates, a key assumption for loans and advances is that the carrying amount of variable rate loans (excluding mortgage products) approximates to market value where there is no significant credit risk of the borrower. The fair value of variable rate mortgage products including tracker mortgages is calculated by discounting expected cash flows using discount rates that reflect the interest rate risk in the portfolio. For fixed rate loans, the fair value is calculated by discounting expected cash flows using discount rates that reflect the interest rate risk in that portfolio.
For the overall loan portfolio, an adjustment is made for credit risk which at 31 December 2013 took account of the Companys' expectations on credit losses over the life of the loans.

# NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

## 34. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

***Deposits by credit institutions***
The fair value of deposit liabilities which are repayable on demand, or which re-price frequently, approximates to their book value. The fair value of all other deposits and other borrowings is estimated using discounted cash flows applying either market rates, where applicable, or interest rates currently offered by the Bank.

***Financial investments available for sale***
The fair value of available for sale debt securities and equities has been estimated based on expected sale proceeds. The expected sale proceeds are based on screen bid prices which have been analysed and compared across multiple sources for reliability. Where screen prices are unavailable, fair values are estimated using valuation techniques using observable market data for similar instruments. Where there is no market data for a directly comparable instrument, management judgement, on an appropriate credit spread to similar or related instruments with market data available, is used within the valuation technique. This is supported by cross referencing other similar or related instruments.

***Debt securities in issue***
The estimated fair value of debt securities in issue, is based on quoted prices where available, or where these are unavailable, are estimated using valuation techniques using observable market data for similar instruments. Where there is no market data for a directly comparable instrument, management judgement on an appropriate credit spread to similar or related instruments with market data available is used within the valuation technique. This is supported by cross referencing other similar or related instruments.

**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**

**34. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)**

The following table sets out the carrying amount and fair value of financial instruments across the three levels of the fair value hierarchy at 31 December 2013.

| Group | Carrying amount in statement of financial position | | | | | | | Fair Value hierarchy | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | At fair value through profit and loss | | At fair value through equity | | At amortised cost | | Total | | | | |
| | Held for trading | Fair value hedge derivatives | Cashflow hedge derivatives | Available for sale securities | Loans and receivables | Other | | Level 1 | Level 2 | Level 3 | Total |
| **Financial assets measured at fair value** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** |
| Cash and balances at central banks | - | - | - | - | - | 74 | 74 | 74 | - | - | 74 |
| Available-for-sale financial asset | | | | | | | | | | | |
| Irish Government Securities | - | - | - | 214 | - | - | 214 | - | 214 | - | 214 |
| Equity – NAMA subordinated | - | - | - | 3 | - | - | 3 | - | - | 3 | 3 |
| Derivative financial instruments | 42 | 56 | 22 | - | - | - | 120 | - | 83 | 37 | 120 |
| **Financial assets not measured at fair value** | | | | | | | | | | | |
| Loans and advances to credit institutions | - | - | - | - | 1,343 | - | 1,343 | 1,343 | - | - | 1,343 |
| Loans and advances to customers | - | - | - | - | 12,025 | - | 12,025 | - | - | 11,329 | 11,329 |
| Other financial assets | - | - | | - | - | 360 | 360 | - | - | 360 | 360 |
| | 42 | 56 | 22 | 217 | 13,368 | 434 | 14,139 | 1,417 | 297 | 11,729 | 13,443 |
| **Financial liabilities measured at fair value** | | | | | | | | | | | |
| Derivative financial instruments | 44 | 7 | 29 | - | - | - | 80 | - | 41 | 39 | 80 |
| **Financial liabilities not measured at fair value** | | | | | | | | | | | |
| Deposits by credit institutions | - | - | - | - | - | 1,640 | 1,640 | 665 | 975 | - | 1,640 |
| Debt securities in issue | - | - | - | - | - | 2,001 | 2,001 | 1,909 | - | - | 1,909 |
| Customer accounts | - | - | - | - | - | 9,297 | 9,297 | - | - | 8,918 | 8,918 |
| Other financial liabilities | - | - | - | - | - | 340 | 340 | - | - | 340 | 340 |
| | 44 | 7 | 29 | - | - | 13,278 | 13,358 | 2,574 | 1,016 | 9,297 | 12,887 |

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

**34. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)**

The following table sets out the carrying amount and fair value of financial instruments across the three levels of the fair value hierarchy at 31 December 2012 (Restated*).

| Group | Carrying amount in statement of financial position | | | | | | | Fair Value hierarchy | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | At fair value through profit and loss | | At fair value through equity | | At amortised cost | | Total | | | | |
| | Held for trading | Fair value hedge derivatives | Cashflow hedge derivatives | Available for sale securities | Loans and receivables | Other | | Level 1 | Level 2 | Level 3 | Total |
| **Financial assets measured at fair value** | €m | €m | €m | €m | €m | €m | €m | €m | €m | €m | €m |
| Cash and balances at central banks | - | - | - | - | - | 8 | 8 | 8 | - | - | 8 |
| Available-for-sale financial asset | | | | | | | | | | | |
| Securities and investments | - | - | - | 1,150 | - | - | 1,150 | 1,150 | - | - | 1,150 |
| Irish Government Securities | - | - | - | 416 | - | - | 416 | 174 | 242 | - | 416 |
| Equity – NAMA subordinated | - | - | - | 2 | - | - | 2 | - | - | 2 | 2 |
| Derivative financial instruments | 65 | 85 | 40 | - | - | - | 190 | - | 190 | - | 190 |
| **Financial assets not measured at fair value** | | | | | | | | | | | |
| Loans and advances to credit institutions | - | - | - | - | 883 | - | 883 | | | | |
| NAMA senior bond | - | - | - | - | - | 305 | 305 | | | | |
| Loans and advances to customers | - | - | - | - | 12,969 | - | 12,969 | | | | |
| Other financial assets | - | - | - | - | - | 394 | 394 | | | | |
| | 65 | 85 | 40 | 1,568 | 13,852 | 707 | 16,317 | 1,332 | 432 | 2 | 1,766 |
| **Financial liabilities measured at fair value** | | | | | | | | | | | |
| Derivative financial instruments | 63 | 60 | 63 | - | - | - | 186 | - | 186 | - | 186 |
| **Financial liabilities not measured at fair value** | | | | | | | | | | | |
| Deposits by credit institutions | - | - | - | - | - | 2,698 | 2,698 | | | | |
| Debt securities in issue | - | - | - | - | - | 2,182 | 2,182 | | | | |
| Customer accounts | - | - | - | - | - | 10,117 | 10,117 | | | | |
| Other financial liabilities | - | - | - | - | - | 445 | 445 | | | | |
| | 63 | 60 | 63 | - | - | 15,442 | 15,628 | - | 186 | - | 186 |

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### 34. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

The following table sets out the carrying amount and fair value of financial instruments across the three levels of the fair value hierarchy at 31 December 2013.

| Company | Carrying amount in statement of financial position | | | | | | | Fair Value hierarchy | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | At fair value through profit and loss | | At fair value through equity | | At amortised cost | | Total | | | | |
| | Held for trading | Fair value hedge derivatives | Cashflow hedge derivatives | Available for sale securities | Loans and receivables | Other | | Level 1 | Level 2 | Level 3 | Total |
| **Financial assets measured at fair value** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** |
| Cash and balances at central banks | - | - | - | - | - | 73 | 73 | 73 | - | - | 73 |
| Available-for-sale financial asset | | | | | | | | | | | |
| Euro Bank Securities | - | - | - | 2,792 | - | - | 2,792 | 2,792 | - | - | 2,792 |
| Irish Government Securities | - | - | - | 214 | - | - | 214 | - | 214 | - | 214 |
| Equity – NAMA subordinated | - | - | - | 3 | - | - | 3 | - | - | 3 | 3 |
| Derivative financial instruments | 75 | 56 | 22 | - | - | - | 153 | - | 116 | 37 | 153 |
| **Financial assets not measured at fair value** | | | | | | | | | | | |
| Loans and advances to credit institutions | - | - | - | - | 4,079 | - | 4,079 | 4,079 | - | - | 4,079 |
| Loans and advances to customers | - | - | - | - | 5,641 | - | 5,641 | - | - | 5,399 | 5,399 |
| Other financial assets | - | - | - | - | - | 1,041 | 1,041 | - | - | 1,041 | 1,041 |
| | 75 | 56 | 22 | 3,009 | 9,720 | 1,114 | 13,996 | 6,944 | 330 | 6,480 | 13,754 |
| **Financial liabilities measured at fair value** | | | | | | | | | | | |
| Derivative financial instruments | 40 | 7 | 29 | - | - | - | 76 | - | 37 | 39 | 76 |
| **Financial liabilities not measured at fair value** | | | | | | | | | | | |
| Deposits by credit institutions | - | - | - | - | - | 1,694 | 1,694 | 719 | 975 | - | 1,694 |
| Debt securities in issue | - | - | - | - | - | 1,153 | 1,153 | 1,179 | - | - | 1,179 |
| Customer accounts | - | - | - | - | - | 10,073 | 10,073 | - | - | 9,694 | 9,694 |
| Other financial liabilities | - | - | - | - | - | 368 | 368 | - | - | 368 | 368 |
| | 40 | 7 | 29 | - | - | 13,288 | 13,364 | 1,898 | 1,012 | 10,101 | 13,011 |

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### 34. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

**Fair Value of Financial Instruments**

The following table sets out the carrying amount and fair value of financial instruments across the three levels of the fair value hierarchy at 31 December 2012 (Restated*).

| Company | Carrying amount in statement of financial position | | | | | | | Fair Value hierarchy | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | At fair value through profit and loss | | At fair value through equity | | At amortised cost | | Total | | | | |
| | Held for trading | Fair value hedge derivatives | Cashflow hedge derivatives | Available for sale securities | Loans and receivables | Other | | Level 1 | Level 2 | Level 3 | Total |
| **Financial assets measured at fair value** | €m | €m | €m | €m | €m | €m | €m | €m | €m | €m | €m |
| Cash and balances at central banks | - | - | - | - | - | 8 | 8 | 8 | - | - | 8 |
| Available-for-sale financial asset | | | | | | | | | | | |
| Securities and investments | - | - | - | 4,127 | - | - | 4,127 | 4,127 | - | - | 4,127 |
| Irish Government Securities | - | - | - | 416 | - | - | 416 | 174 | 242 | - | 416 |
| Equity – NAMA subordinated | - | - | - | 2 | - | - | 2 | - | - | 2 | 2 |
| Derivative financial instruments | 101 | 85 | 40 | - | - | - | 226 | - | 226 | - | 226 |
| **Financial assets not measured at fair value** | | | | | | | | | | | |
| Loans and advances to credit institutions | - | - | - | - | 3,906 | - | 3,906 | | | | |
| NAMA senior bond | - | - | - | - | 305 | - | 305 | | | | |
| Loans and advances to customers | - | - | - | - | 5,994 | - | 5,994 | | | | |
| Other financial assets | - | - | - | - | - | 1,062 | 1,062 | | | | |
| | 101 | 85 | 40 | 4,545 | 10,205 | 1,070 | 16,046 | 4,309 | 468 | 2 | 4,779 |
| **Financial liabilities measured at fair value** | | | | | | | | | | | |
| Derivative financial instruments | 57 | 60 | 63 | - | - | - | 180 | - | 180 | - | 180 |
| **Financial liabilities not measured at fair value** | | | | | | | | | | | |
| Deposits by credit institutions | - | - | - | - | - | 2,756 | 2,756 | | | | |
| Debt securities in issue | - | - | - | - | - | 1,286 | 1,286 | | | | |
| Customer accounts | - | - | - | - | - | 10,983 | 10,983 | | | | |
| Other financial liabilities | - | - | - | - | - | 529 | 529 | | | | |
| | 57 | 60 | 63 | - | - | 15,554 | 15,734 | - | 180 | - | 180 |

## 34. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

**Reconciliation of balances in Level 3 of the fair value hierarchy**

The following table shows a reconciliation from the beginning balances to the ending balances for fair value measurements in Level 3 of the fair value hierarchy for 2013 and 2012:

**31 December 2013**

| Group/Company | Financial assets Derivatives | Equity securities | Total | Financial liabilities Derivatives | Total |
|---|---|---|---|---|---|
| | € | € | € | € | € |
| At 1 January 2013 | - | 2 | 2 | - | - |
| Transfers into Level 3 | 37 | - | 37 | 39 | 39 |
| Other comprehensive income | - | 1 | 1 | - | - |
| **At 31 December 2013** | **37** | **3** | **40** | **39** | **39** |

**31 December 2012**

| Group/Company | Financial assets Derivatives | Equity securities | Total | Financial liabilities Derivatives | Total |
|---|---|---|---|---|---|
| | € | € | € | € | € |
| At 1 January 2012 | - | 6 | 6 | - | - |
| Income Statement | - | (3) | (3) | - | - |
| Other comprehensive income | - | (1) | (1) | - | - |
| **At 31 December 2012** | **-** | **2** | **2** | | |

On transfer of loans to NAMA, 5% of the consideration received by the Company was in the form of NAMA subordinated bonds, which are classified as equity securities. These are unlisted securities and they are valued using valuation techniques which use unobservable market data. The implementation of valuation techniques involves a considerable degree of judgement. While the Group believe that its estimate of fair value is appropriate, the use of different measurements or assumptions could lead to different fair values. The differences between the fair value at initial recognition and the amount that was determined at 31 December 2013 using a valuation technique incorporating significant unobservable data was charged to equity.

External derivatives held, were transferred into level 3 at 31 December 2013, due to the significant unobservable inputs into the valuation techniques. As these were transferred across at the year end, there was no income statement impact for the year.

## 35. CAPITAL MANAGEMENT

**Regulatory capital**

From 1 January 2008 the minimum regulatory capital requirement of the Group's banking operations has been calculated in accordance with the provisions of Basel II as implemented by the European Capital Requirements Directive and the Irish Central Bank of Ireland. The objective of Basel II is to more closely align bank regulatory capital with the economic capital required to support the risks being undertaken. The capital required to cover credit, operational and market risks is required to be explicitly measured under the Basel II methodology. In implementing Basel II, the Group has adopted the standardised approach to credit risk.

EBS Group sets and monitors capital policy in line with regulatory and legislative requirements. Capital adequacy is monitored by the Asset and Liability Committee.

On 18 July 2011 the Central Bank of Ireland confirmed that EBS was required to meet an 8% total capital ratio.

In December 2011, AIB p.l.c. provided €300m of capital to EBS, in July 2012 it provided €400m and in December 2013 provided a further €330m on the issuance of Ordinary Share Capital. Further details are in note 26.

## 35. CAPITAL MANAGEMENT (continued)

**The Group's regulatory capital comprises:**
Tier 1 capital, which includes ordinary share capital and promissory note investments by the Irish government, general reserve capital, deductions for goodwill and intangible assets, and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes.

Tier 2 capital, comprises collective impairment allowances.

Within these tiers, limits are set for different components of capital. There also are restrictions on the amount of collective impairment allowances that may be included as part of Tier 2 capital.

Banking operations are categorised as either banking book or reserve investments, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets exposures.

The Group's policy is to ensure that sufficient capital is in place to meet regulatory requirements.

There have been no material changes in the Group's capital policy during the period.

The Group's regulatory capital at 31 December was as follows:

| | 2013<br>€m | 2012<br>€m |
|---|---|---|
| **Core Tier 1 capital** | | |
| Ordinary share capital | 1,654 | 1,324 |
| Special investment share | - | - |
| General reserve | (868) | (648) |
| Intangible assets | (14) | (17) |
| Other regulatory adjustments | 17 | 47 |
| **Total Tier 1 Capital** | 789 | 706 |
| **Tier 2 Capital** | | |
| Collective allowances for impairment | 99 | 111 |
| Tier 2 Capital | 99 | 111 |
| **Total Regulatory Capital** | **888** | **817** |

The allocation of capital between different business lines is, to a large extent, driven by optimisation of the return achieved on the capital allocated. The allocation of capital to specific business lines and activities is approved by the Group's Management team and is monitored by the Asset and Liability Committee.

Although risk-adjusted capital is the principal basis used in determining how capital is allocated within the Group to particular operations or activities, it is not the sole basis used for decision making. Account also is taken of synergies with other operations and activities, the availability of management and other resources, and the fit of the activity with the Group's longer term strategic objectives. The Group's policies in respect of capital management and allocation are reviewed regularly by the Board of Directors.

### 36. IMPACT OF ADOPTING NEW ACCOUNTING STANDARDS

From 1 January 2013, EBS adopted 'IAS 19 Employee Benefits (Revised)'. This standard is required to be applied retrospectively, and accordingly, EBS has restated previously published comparative periods as set out below:

| | | | | | | Group |
|---|---|---|---|---|---|---|
| | | | 2012 | | | 2011 |
| | Published €m | IAS 19R €m | Restated €m | Published €m | IAS 19R €m | Restated €m |
| **Consolidated income statement (selected lines)** | | | | | | |
| Administrative expenses | (89) | 14 | (75) | (85) | (2) | (87) |
| Loss before taxation from continuing operations | (842) | 14 | (828) | (254) | (2) | (256) |
| Income tax credit from continuing operations | 106 | (2) | 104 | 103 | - | 103 |
| Loss after taxation from continuing operations | (736) | 12 | (724) | (151) | (1) | (152) |
| Loss for the year | (736) | 12 | (724) | (151) | (1) | (152) |
| **Consolidated statement of comprehensive income (selected lines)** | | | | | | |
| Loss for the year | (736) | 12 | (724) | (151) | (1) | (152) |
| Net actuarial losses in retirement benefit schemes | (33) | - | (33) | (18) | 1 | (17) |
| Total items that will not be reclassified to profit or loss | (33) | - | (33) | (18) | 1 | (17) |
| Other comprehensive income for the year, net of tax from continuing operations | 208 | - | 208 | 16 | 1 | 17 |
| Total other comprehensive income for the year, net of tax | 208 | - | 208 | 16 | 1 | 17 |
| Total comprehensive income for the year | (561) | 12 | (549) | (153) | - | (153) |
| **Consolidated statement of financial position (selected lines)** | | | | | | |
| **Assets** | | | | | | |
| Deferred taxation | 254 | (2) | 252 | 172 | - | 172 |
| Total assets | 16,319 | (2) | 16,317 | 18,537 | - | 18,537 |
| **Liabilities** | | | | | | |
| Provisions for liabilities and commitments | 27 | (14) | 13 | 13 | - | 13 |
| Total liabilities | 15,642 | (14) | 15,628 | 17,699 | - | 17,699 |
| **Shareholders' equity** | | | | | | |
| Reserves | (897) | 12 | (885) | (335) | - | (335) |
| Total shareholders' equity | 677 | 12 | 689 | 838 | - | 838 |
| Total liabilities and shareholders' equity | 16,319 | (2) | 16,317 | 18,537 | - | 18,537 |
| **Consolidated statement of cash flows (selected lines)** | | | | | | |
| Loss for the year from continuing operations before taxation | (842) | 14 | (828) | (254) | (2) | (256) |
| Retirement benefits - defined benefit expense | (3) | - | (3) | (1) | 2 | - |
| Change in other provisions / Termination Benefits | 14 | (14) | - | - | - | - |
| **Consolidated statement of changes in equity (selected lines)** | | | | | | |
| Balance at the beginning of the year | 838 | - | 838 | 702 | - | 702 |
| Loss for the year | (736) | 12 | (724) | (151) | (1) | (152) |
| Other comprehensive income | 208 | - | 208 | 16 | 1 | 17 |
| Total comprehensive income | (561) | 12 | (549) | (153) | - | (153) |
| Balance at the end of the year | 677 | 12 | 689 | 838 | - | 838 |

The adoption of IAS 19 (Revised) decreased the provision for liabilities and commitments for 2012 by €14 million as a result of a voluntary severance scheme, which was recognised in 2012, being restated. Also the Retirement benefit charge increased in the consolidated income statement for 2011 by €2 million as a result of the adoption of IAS 19 (Revised).

### 36. IMPACT OF ADOPTING NEW ACCOUNTING STANDARDS

| | | | | | | Company |
|---|---|---|---|---|---|---|
| | | | 2012 | | | 2011 |
| | Published €m | IAS 19R €m | Restated €m | Published €m | IAS 19R €m | Restated €m |
| **Consolidated statement of financial position (selected lines)** | | | | | | |
| **Assets** | | | | | | |
| Deferred taxation | 313 | (2) | 311 | 196 | - | 196 |
| Total assets | 16,048 | (2) | 16,048 | 17,111 | - | 17,111 |
| **Liabilities** | | | | | | |
| Provisions for liabilities and commitments | 27 | (14) | 13 | 12 | - | 12 |
| Total liabilities | 15,748 | (14) | 15,734 | 16,734 | - | 16,734 |
| **Shareholders' equity** | | | | | | |
| Reserves | (897) | 12 | (885) | (796) | - | (796) |
| Total shareholders' equity | 300 | 12 | 312 | 377 | - | 377 |
| Total liabilities and shareholders' equity | 16,048 | (2) | 16,046 | 17,111 | - | 17,111 |
| **Consolidated statement of cash flows (selected lines)** | | | | | | |
| Loss for the year from continuing operations before taxation | (624) | 14 | (610) | (14) | (2) | (16) |
| Retirement benefits - defined benefit expense | (3) | - | (3) | (1) | 1 | - |
| Change in other provisions / Termination Benefits | 15 | (14) | 1 | - | - | - |
| **Consolidated statement of changes in equity (selected lines)** | | | | | | |
| Balance at the beginning of the year | 377 | - | 377 | 105 | - | 105 |
| Loss for the year | (624) | 12 | (612) | 14 | (1) | (15) |
| Other comprehensive income | 208 | - | 208 | 16 | 1 | 17 |
| Total comprehensive income | (477) | 12 | (465) | (28) | - | (28) |
| Balance at the end of the year | 300 | 12 | 312 | 377 | - | 377 |

### 37. REGULATORY COMPLIANCE

During December 2011, EBS Mortgage Finance breached the large exposures limit. This arose due to the acquisition of loans from EBS in November 2011. The issue was resolved and the exposures were brought back within limits in January 2012. There were no other issues in 2012.

EBS Limited exceeded the Related Party Lending limit in June 2013 in respect of pre-existing loans to Hinsona Ltd., a wholly owned subsidiary of EBS. The Central Bank of Ireland was advised of the breach. With effect from 1 July 2013 such inter-company loans were exempt from the Related Party Limit requirement.

At all times during 2013 EBS had capital in excess of its required capital ratio.

### 38. OTHER INFORMATION

At 31 December 2013 the Group reserve ratio is 5.5% (2012: 4.1%) and the liquidity ratio is 13.1% (2012: 17.4%). These are required to be disclosed under certain covenants entered into by EBS.

In accordance with section 40(1) of the Asset Covered Securities Act 2001 (as amended), EBS, as parent entity to the designated mortgage credit institution EBS Mortgage Finance, is reporting the following information as at 31 December 2013:

(i) The total amount of principal outstanding in respect of the mortgage covered securities issued by EBS Mortgage Finance as at 31 December 2013 is €2,800m (2012: €3,150m) of which €50m (2012: €50m) was held by third parties and €2,750m (2012: €3,100m) by the Company.

*(ii)* The total amounts of principal outstanding in respect of the mortgage credit assets and substitution assets comprised in the cover assets pool relating to the mortgaged covered securities as at 31 December 2013 in issue is €5,283m (2012: €5,779m).

### 39. EVENTS SINCE THE REPORTING DATE

There were no significant non-adjusting events that have taken place since 31 December 2013.

### 40. APPROVAL OF FINANCIAL STATEMENTS

The financial statements were authorised for issue by the Board of Directors on 13 March 2014.