EBS MORTGAGE FINANCE

DIRECTORS' REPORT AND ANNUAL FINANCIAL STATEMENTS
For the financial year ended 31 December 2015

CONTENTS

DIRECTORS AND OTHER INFORMATION

DIRECTORS

Denis Holland	Independent Non-Executive Director and Chairman
William Cunningham	Independent Non-Executive Director
Fidelma Clarke	Group Non-Executive Director
Gerry Gaffney	Executive Director
Owen Purcell	Executive Director (Managing Director)

SECRETARY	Catherine Kelly
REGISTERED OFFICE	2 Burlington Road Dublin 4 Ireland
REGISTERED NUMBER	463791
REGISTERED AUDITOR	Deloitte Chartered Accountants & Statutory Audit Firm Hardwicke House Hatch Street Dublin 2 Ireland
BANKERS	EBS Limited 2 Burlington Road Dublin 4 Ireland BNP Paribas Ireland 5 George's Dock International Financial Services Centre Dublin 1 Ireland
COVER-ASSETS MONITOR	Mazars Harcourt Centre Block 3 Harcourt Road Dublin 2 Ireland

DIRECTORS' REPORT

The Directors present their annual report and financial statements for the financial year ended 31 December 2015. The Directors' responsibility statement in relation to the financial statements appears on page 36.

Principal activities

EBS Mortgage Finance ('the Bank' or 'EBSMF'), a public unlimited company, obtained an Irish banking licence under the Irish Central Bank Act, 1971 (as amended) and was registered as a designated mortgage credit institution under the Asset Covered Securities Act, 2001 on 30 October 2008. The Bank is a wholly owned subsidiary of EBS Limited ('EBS' or 'Parent') and a member of EBS Group (the 'Group'). EBS is a wholly owned subsidiary of Allied Irish Banks, p.l.c. ('AIB p.l.c.' or 'AIB Group'). AIB Group and its subsidiaries, including EBSMF, came under the direct supervision of, and are deemed to be authorised by the European Central Bank ('ECB') since the introduction on 4 November 2014 of the Single Supervisory Mechanism ('SSM'). The SSM places the ECB as the central prudential supervisor of financial institutions in the Eurozone, including AIB and its subsidiaries. The Bank continues to be supervised by the Central Bank of Ireland for non-prudential matters, including, consumer protection and the combat of money laundering.

The Bank's principal purpose is to issue mortgage covered securities for the purpose of financing mortgage loans secured on residential property in accordance with the Asset Covered Securities Act, 2001 and the Asset Covered Securities (Amendment) Act 2007 ('the Asset Covered Securities Acts'). The Bank does not sell mortgage loans directly to the public. It has an origination agreement with EBS whereby EBS continues to sell mortgage loans directly to the public and may subsequently transfer loan portfolios to the Bank for an appropriate consideration.

The Bank was incorporated on 30 October 2008 and commenced trading on 1 December 2008. During the period from that date to the end of 2011, EBS sold €8.3bn of residential loans to the Bank and in turn the Bank issued a series of covered bonds. The Bank did not purchase any loans from EBS since 2011, however a loan purchase from EBS is being considered for late 2016.

The business strategy for 2016 is anticipated to continue to entail the provision of liquidity to AIB p.l.c. via the issue of suitably rated ECB repo eligible collateral, and maximise efficient use of mortgage collateral, subject to requirement of the Banks' cover pool management, ACS Act and rating agency requirements. The ongoing amortization of the cover pool, with all other things being equal, will result in declining nominal and regulatory over collateralisation ('OC') levels, however given the extent of the surplus OC available with respect to current bonds outstanding there will be no requirement to re-purchase and cancel outstanding bonds.

The Bank's business activities are restricted, under the Asset Covered Securities Acts, to dealing in, and holding, mortgage credit assets and limited classes of other assets, engaging in activities connected with the financing and refinancing of such assets, entering into certain hedging contracts and engaging in other activities which are incidental to, or ancillary to, the above activities. In accordance with the Asset Covered Securities Acts, the Cover-Assets Monitor, Mazars monitors compliance with the Acts and reports independently to the Central Bank of Ireland.

The Bank's activities are financed through the issuance of mortgage covered securities with the balance of funding being provided by AIB Group. The Bank was also party to the Mortgage-Backed Promissory Notes agreements with the Central Bank of Ireland, however this type of funding has not been utilised since 2011.

All of the Bank's operational & support activities are outsourced to AIB p.l.c. under a Managed Services Agreement. AIB, as Service Provider for the Bank, services the mortgage loans, and provides treasury services in connection with financing as well as a range of other support services.

Corporate governance statement

The Board of Directors

Governance is exercised through a Board of Directors ('the Board') and a Senior Management Team. The Board is responsible for corporate governance encompassing leadership, direction and control of the Bank and is responsible for financial performance to its shareholder and ultimate parent Allied Irish Banks, p.l.c. ('AIB'). The conditions of the Bank's Central Bank licence require that there should be a minimum of two Non-Executive Directors who are independent of the parent company. Throughout 2015, there were two independent Non-Executive Directors on the Board of the Bank. The Board also includes two Executive Directors, both of whom are directly involved in the operation of EBS Mortgage Finance, and one other Director who, while also an employee of AIB, is deemed to be a Group Non-Executive Director by virtue of her role in an area of AIB Group which is not directly related to the operations of EBS Mortgage Finance.

The Board is responsible for ensuring that appropriate systems of internal controls and risk management are maintained, specifically the Board sets the Risk Appetite Statement, approves the Risk Framework and approves the annual financial plans. The Bank benefits as a subsidiary of AIB from the wider AIB Group governance and operating structure, including in relation to oversight of audit and risk related activities. AIB and EBS provide services to EBS Mortgage Finance through a formal managed services agreement, updates in respect of the performance against which are provided to the Board regularly. In the event that material failings or weaknesses in the systems of risk management or internal control are identified, explanation of the issue is presented with proposed remediation plan to the Board. Agreed remediation plans are tracked to conclusion, with status updates provided to the Board. Given the work of the Board and representations made by the Management Team during the year, the Board is satisfied that the necessary actions to address any material failings or weaknesses identified through the operation of the risk management and internal control framework have been taken, or are currently being undertaken. In addition, the Board has considered the identification in 2015 of failings that originated in prior years that require customer redress. Taking this and all other information into consideration as outlined above, the Board is satisfied that there has been an effective system of control in place throughout the year.

The Board receives regular updates on the Bank's risk profile from the AIB Group Risk function. The Board held 4 scheduled meetings during 2015 and no out of course meetings were held. Further detail about Directors' attendance of the meetings can be found in the table below.

The Board also has responsibility for:

- the quality and integrity of the Bank's accounting policies, financial statements and disclosure practices;
- compliance with relevant laws, regulations, codes of conduct and 'conduct of business' rules;
- the independence and performance of the External Auditor ('the Auditor') and Internal Audit; and
- the adequacy and performance of systems of internal control and the management of financial and non-financial risks.

DIRECTORS' REPORT (continued)

Corporate governance statement (continued)

The Board of Directors (continued)
These responsibilities are discharged through its meetings with and receipt of reports from the Auditor and management including Finance, Internal Audit and Risk. At its meetings during 2015 the Board reviewed the annual financial statements, and related accounting policies, key judgements, and practices; the effectiveness of internal controls; and the findings, conclusions and recommendations of the Auditor and Internal Auditor. The Board satisfied itself through regular reports from the Internal Auditor, Risk and the Auditor, and through reports on the performance of services from AIB and EBS under the managed services agreement, that the system of internal controls supporting EBS Mortgage Finance were effective. The Board is satisfied that appropriate measures are taken to consider and address any control issues identified by Internal Audit and the Auditor.

During 2015, the Bank was subject to the provisions of the Central Bank of Ireland's Corporate Governance Code for Credit Institutions and Insurance Undertakings ("the Central Bank Code") (which is available on www.centralbank.ie), which imposes minimum core standards upon all credit institutions and insurance undertakings licensed or authorised by the Central Bank of Ireland ('the Central Bank'). The Directors believe that the Bank materially complied with the provisions of the 2010 Code throughout 2015.

During December 2015, the Central Bank published the Corporate Governance Requirements for Credit Institutions 2015 ("the 2015 Requirements") (which are available on www.centralbank.ie), which became effective for all credit institutions on 11 January 2016. Under the 2015 Requirements, the Bank is designated as a "high impact institution", in accordance with its categorisation under the Central Bank's Probability Risk Impact System. This designation resulted in a number of significant incremental obligations above those outlined in the 2010 Code. The Bank sought and received derogations from the Central Bank from a number of the significant incremental obligations including those relating to Board Committees, Board composition, and meeting frequency.

The Bank's corporate governance practices are designed to ensure compliance with applicable legal and regulatory requirements including, Irish company law and the Listing Rules applicable to debt listings of the Main Securities Market of the Irish Stock Exchange.

The Bank believes it has robust governance arrangements, which include a clear organisational structure with well defined, transparent, and consistent lines of responsibility, effective processes to identify, manage, monitor and report the risks to which it is or might be exposed, and adequate internal controls, including sound administrative and accounting procedures, IT systems and controls.

Business review
The Irish economy improved generally during 2015 including a decreasing unemployment rate standing at 8.8% at the end of December 2015 against a peak of 12.1% in 2014 (Source: Central Statistics Office) and decreasing mortgage arrears. Total market mortgage drawdowns in Ireland were €4.9bn (Source: Banking & Payments Federation of Ireland ('BPFI')) in 2015 compared with €3.9bn in 2014.

The CSO Residential Property Price Index showed an increase in prices nationally of 6.6% in the 12 months to December 2015 (16.3% in 2014). This was particularly evident outside Dublin where the 2015 annual increase was 10.2% (December 2014 10.2%). Property prices in Dublin increased in the 12 month period by 2.6% (increase of 22.3% in 2014). The national fall from peak property prices (February 2007) was 33.5% at December 2015 (37.6% at December 2014).

The Bank's loan portfolio before provisions decreased by 6.9% during 2015 to €5.5bn as at 31 December 2015 principally due to customers repayments and loan restructuring accounts.(2014: decrease 6.4%).

EBS Mortgage Finance's residential mortgage portfolio comprises €5.5bn owner occupier (2014: €5.9bn) and €0.2bn buy-to-let mortgages (2014: €0.2bn). At 31 December 2015, EBS Mortgage Finance mortgage loans accounted for 15.1% (2014: 15.3%) of the AIB Group's residential mortgage portfolio of €36.8bn (2014: €38.8bn).

As a result of positive trends in the Irish economy, including an improving residential property market and decreasing unemployment, leading to an improvement in asset values and borrower repayment capacity, the Bank's impaired loans have decreased to €1.0bn, or 17.3% of total loans (2014: €1.3bn or 21.5%).

Mortgage arrears resolution strategy
AIB Group has developed a Mortgage Arrears Resolution Strategy ('MARS') which builds on and formalises AIB Group's Mortgage Arrears Resolution Process, to implement the Codes of Conduct as set out by the Central Bank of Ireland, for dealing in a professional and timely manner with mortgage customers in difficulty or likely to be in difficulty. The core objectives of MARS are to ensure that arrears solutions are sustainable in the long-term and that they comply with the spirit and the letter of all regulatory requirements. MARS includes long-term forbearance solutions which have been devised to assist existing primary residential mortgage customers in difficulty.

At 31 December 2015, there were forbearance solutions in place on circa 9k accounts with loan balances of €1.1bn (2014: circa 8k accounts with €1.0bn balance). The stock of loans subject to forbearance increased by €0.1bn in 2015, driven by the Bank's strategy to ensure the forbearance solutions agreed with customers are sustainable in the long-term. During 2015 there was a migration from short term to longer term sustainable forbearance solutions, in particular increases in arrears capitalisations of €120m, and additional low fixed interest rate solutions of €46m offset by a reduction loan balances on interest only of €71m and reduced term extensions of €37m.

Results for the year
EBS Mortgage Finance generated a profit before taxation for 2015 of €122m, compared to €109m in 2014. Increased profitability is due to lower funding costs and a write back of provisions for impaired loans credited to the income statement, offset by increased administration expense due to restitution provision of €35m. Profit after tax of €107m was added to Shareholders Equity in 2015 compared to €95m in 2014.

DIRECTORS' REPORT (continued)

Results for the year (continued)

Net Interest Margin/Income

The net interest margin for 2015 was 2.93% an increase of 0.58% compared to 2.35% for 2014 due to reduced interest expense of €69m (2014: €135m), as a result of the early maturity of a higher interest rate bond, offset by lower interest income of €231m (2014: €274m) due to reductions in fixed and variable customer rates and lower average loan balances.

Other operating expense

Other operating expense is €9m due to a loss on an early maturity of a bond offset by savings in interest expense of €8.6m.

Administration Expenses

Administrative expenses increased by €36m to €44m during the year due to year due to the recording of a provision of €35m for customers redress and other related matters relating to a request from the Central Bank of Ireland ("CBI") in December 2015, to the Irish banking industry, including AIB, to conduct a broad examination of tracker mortgage related issues.

Provisions Writeback

Overall provision writeback for 2015 of €10m compared to a charge €22m in 2014, an improvement of €32m. Specific impairment provision charge has increased by €6m to €18m in 2015 (2014: €12m).The Incurred but Not Reported ("IBNR") stock levels have been reduced in 2015, resulting in a writeback of €28m (2014: €10m charge) due to an updated AIB private dwelling model implemented for provisioning.

Specific provision stock amounts to €253m (2014: €280m) and IBNR provisions stand at €28m (2014: €56m) as at 31 December 2015. Total provisions as percentage of total loans covered decreased to 5.1% (2014: 5.6%).

Funding activities

The covered bond market continued to benefit from a favourable market backdrop in 2015, with the ECB's Covered Bond Purchase Programme (CBPP3) continuing to purchase bonds in both the primary and secondary markets, accumulating holdings of circa €150bn by January 29th, 2016. CBPP3 is aimed at enhancing the functioning of the monetary policy transmission mechanism, supporting financing conditions in the euro area, facilitating credit provision to the real economy and generating positive spill overs to other markets.

In January 2015 the ECB announced an expanded asset purchase programme (APP) aimed at fulfilling the ECB's price stability mandate by adding a public sector purchase programme for government bonds to the existing private sector programmes for covered bonds and ABS. In December it was announced that the APP would run for an extended period, until at least March 2017, and that principal payments under the programme would be reinvested as they mature. It was also announced that the eligibility criteria would be expanded to include euro-denominated marketable debt instruments issued by regional and local governments. The ECB also announced a further cut in the deposit rate to minus 30 basis points at the December 2015 meeting.

Towards the latter part of 2015 covered bond spreads saw some widening, driven by a mixture of elevated supply in the asset class from September onwards and declining secondary market liquidity, among other factors. The covered bond primary market has remained active in the early part of 2016 despite a highly volatile market backdrop in the global equity and credit markets.

At 31 December 2015, the total amount of principal outstanding in respect of mortgage covered securities issued was €2.40bn (31 December 2014: €1.85bn) subscribed for in full by EBS Limited. The Bank repurchased €450m of the Series 8 bonds in June 2015 and replaced them with Series 14 &15 covered bonds of €500m each. At the end of 2015, the total nominal value of covered bonds issued was €2.1bn subscribed for in full by EBS.

Moody's upgraded the EBS Mortgage Finance covered bond programme to Aa1 from Aa2 in November 2015 having previously upgraded the programme to Aa2 from A3 in May 2015. Fitch upgraded the covered bond programme rating to A+ from A in December 2015 following a previous upgrade from A- to A in September 2015 and a downgrade from A to A- in May 2015.

The ratings as at 8 February 2016, for the Bank's Covered Bond Programme, AIB Group, and Ireland are shown below:

Rating Agency	EBS Mortgage Finance Covered Bond Programme	Allied Irish Banks p.l.c Issuer default rating	Ireland (Sovereign)
Fitch	A+	BB+	A
Moody's	Aa1	Ba1	Baa1

Share capital

The share capital of the Bank is €552m (2014: €552m), comprised of ordinary shares of €1 each.

DIRECTORS' REPORT (continued)

Capital resources and regulatory capital ratios

The table below shows the components of the EBS Mortgage Finance's Common equity Tier 1 and total capital ratios as at 31 December 2015 and 31 December 2014.

	CRD IV Transitional basis	
	31 December 2015	31 December 2014
	€m	€m
Core tier 1/common equity tier 1 capital	**626**	519
Total Tier 2 capital	**20**	29
Total capital	**646**	548
Risk Weighted Assets	**2,760**	3,049
Core tier 1/common equity tier 1 ratio	**22.7%**	17.0%
Total capital ratio	**23.4%**	18.0%

Under the fully loaded CRDIV capital basis the Total Capital ratio is reduced by 0.7% at 31 December 2015.

Outlook

The capital position of the Bank is stable due an increase of profitability and the ongoing commitment of support from AIB. AIB is sufficiently capitalised to meet its regulatory requirements.

Risk Management

The risk management framework provides a bank-wide definition of risk and lays down principles of how risk is to be identified, assessed, measured, monitored and controlled / mitigated, and the associated allocation of capital against same. Further information in relation to the Risk Management are set out in the Management Report on pages 9 to 36. The principal risks and uncertainties facing the Bank are disclosed in the AIB Group's Annual Financial Report.

Going concern

The Directors of the Bank have prepared the financial statements on a going concern basis.

EBS Mortgage Finance is dependent on its ultimate parent, Allied Irish Banks, p.l.c. for continued funding and is therefore dependent on the going concern status of the ultimate parent.

The financial statements of Allied Irish Banks, p.l.c. have been prepared on a going concern basis. In making its assessment, the Directors of AIB Group have considered a wide range of information relating to present and future conditions. These have included financial plans approved by the Board of AIB Group in December 2015 covering the period 2016 to 2018, the Restructuring Plan approved by the European Commission in May 2014, liquidity and funding forecasts, and capital resources projections, all of which have been prepared under base and stress scenarios. In addition, the Directors of AIB Group have considered the outlook for the Irish, the eurozone and UK economies and the factors and uncertainties impacting their performance.

On the basis of the continued availability of funding from AIB p.l.c. to EBS Mortgage Finance, the Directors of the Bank believe that it is appropriate to prepare the financial statements on a going concern basis.

DIRECTORS' REPORT (continued)

Directors' and Secretary's interests in shares
The beneficial interests of the Directors and the Secretary in office at 31 December 2015 and of their spouses and minor children in the share capital or debentures of the parent company, Allied Irish Banks, p.l.c. ("AIB") were less than 1% of the nominal value of AIB's issued share capital as at 1 January and 31 December 2015 and are not required to be disclosed in accordance with the Companies Act 2014.

Share options
Neither the Directors nor the Secretary held any options in AIB's Share Option Scheme as at 31 December 2015. There were no changes in the Directors' and Secretary's interests between 31 December 2015 and 18 March 2016.

Attendance at scheduled Board Meetings

Name	Board	Board
Directors	**A**	**B**
Bill Cunningham	4	4
Fidelma Clarke	4	4
Gerry Gaffney	4	4
Denis Holland	4	4
Owen Purcell	4	4

Column A indicates the number of scheduled meetings held during 2015 which the Director was eligible to attend; Column B indicates the number of meetings attended by each Director during 2015.

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 2015. 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 2015 and 18 March 2016.

Directors and Secretary
Ms. Sarah McLaughlin resigned as Company Secretary for the Company on 26 March 2015. Ms. Catherine Kelly was appointed as Company Secretary on the same date.

There were no changes to the Board during 2015.

Adequate Accounting Records
The Directors believe that they have complied with the requirements of Section 281 to 285 of the Companies Act 2014 with regard to adequate accounting records by allocating personnel with appropriate expertise and by providing adequate resources to the financial function under the Managed Services Agreement for the provision of various services including accounting and other financial services to EBSMF by AIB p.l.c.. The accounting records of the Company are maintained at the registered office of its ultimate parent at AIB, Bankcentre, Ballsbridge, Dublin 4.

Political donations
The Directors are satisfied that no political donations were made during the financial year (2014: Nil).

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 Bank.

Independent auditor
Deloitte, Chartered Accountants and Statutory Audit Firm, has expressed their willingness to continue in office under Section 383(2) of the Companies Act 2014.

On behalf of the Board

Denis Holland
Chairman

Owen Purcell
Managing Director

Date: 18 March 2016

RISK MANAGEMENT REPORT

1. Introduction
All of the Bank'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 AIB Group's risk management framework. The principal risks and uncertainties facing AIB Group are discussed on pages 50 to 59 of AIB Group's Annual Financial Report 2015.

2. Risk framework
EBS Mortgage Finance relies on this AIB Group framework and its supporting policies, processes and governance. The AIB Group risk governance and management framework is described on pages 60 to 62 of the AIB Group's Annual Financial Report 2015. For more information on the operation of the Board of EBS Mortgage Finance see page 3 to 4 of this report.

3 Individual risk types
This section provides details of the exposure to, and risk management of, the following individual risk types which have been identified through the AIB Group risk assessment process and which are relevant to EBSMF:

3.1 Credit risk
3.2 Liquidity risk
3.3 Conduct Risk
3.4 Operational risk
3.5 Regulatory compliance risk
3.6 Non-trading interest rate risk

The 6 applicable risk types are discussed overleaf.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk

Credit risk is the risk that the Bank will incur losses as a result of either a customer or counterparty being unable or unwilling to meet a commitment that it has entered into and that pledged collateral does not fully cover amounts due to the Bank. The most significant credit risks assumed by the Bank arise from mortgage lending activities to customers in the Republic of Ireland. Credit risk also arises on funds placed with other banks and in respect of derivatives relating to interest rate risk management.

Credit risk management objectives are to:

- Establish and maintain a control framework to ensure credit risk taking is based on sound credit management principles;
- Control and plan credit risk taking in line with external stakeholder expectations;
- Identify, assess and measure credit risk clearly and accurately across the Bank, from the level of individual facilities up to the total portfolio; and
- Monitor credit risk and adherence to agreed controls.

The most significant credit risks arise from lending activities to customers and banks, derivatives relating to interest rate risk management and 'off-balance sheet' commitments.

Maximum exposure to credit risk from on balance sheet and off balance sheet financial instruments is presented before taking account of any collateral held or other credit enhancements (unless such enhancements meet accounting offsetting requirements). For financial assets recognised on the statement of financial position, the maximum exposure to credit risk equals their carrying amount, and for loan commitments that are irrevocable over the life of the respective facilities, it is the full loan amount of the committed facilities.

The table below sets out the maximum exposure to credit risk that arises within the Bank. The table 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*

			2015			2014
	Amortised Cost	**Fair Value**	**Total**	Amortised Cost	Fair Value	Total
	€ m	**€ m**	**€ m**	€ m	€ m	€ m
Derivative financial instruments	**-**	**20**	**20**	-	22	22
Loans and receivables to banks	**60**	**-**	**60**	77	-	77
Loans and receivables to customers	**5,265**	**-**	**5,265**	5,623	-	5,623
Included elsewhere:						
Accrued interest	**-**	**-**	**-**	-	-	-
Other assets	**-**	**-**	**-**	-	-	-
	5,325	**20**	**5,345**	5,700	22	5,722
Off balance sheet loan commitments	**11**	**-**	**11**	12	-	12
Maximum exposure to credit risk	**5,336**	**20**	**5,356**	5,712	22	5,734

Credit risk organisation and structure

AIB Group's credit risk management systems operate through a hierarchy of lending authorities. The Bank relies on the AIB Group credit framework and its supporting policies, processes and governance. All customer mortgage applications are subject to an individual credit assessment process.

The role of the AIB Group Credit Risk function is to provide direction, oversight and challenge of credit risk-taking. AIB Group's Risk Appetite Statement sets out the credit risk appetite and framework. Credit Risk appetite is set at AIB Group Board level and is described, reported and monitored through a suite of metrics, supported by credit risk policies, concentration limits to manage risk and exposure within the AIB Group's approved risk appetite. AIB Group's risk appetite for credit risk is reviewed and approved annually.

*Forms an integral part of the audited financial statements

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Measurement of credit risk
One of the objectives of credit risk management is to accurately quantify the level of credit risk to which AIB 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;
- Loss given default ("LGD") – the loss associated with a defaulted loan or borrower, and;
- Expected loss ("EL") – the loss that can be incurred as a result of lending to a borrower that may default. It is the average expected loss in value over a specified period.

To calculate PD, AIB 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, at which authority level they can be approved, and how any existing limits are managed for current borrowers.

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. 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. In the retail portfolio, which is characterised by a large number of customers with small individual exposures, risk assessment is largely automated through the use of statistically-based scoring models.

Mortgage applications are generally assessed centrally with particular reference to affordability, assisted by scoring models. However, for larger cases with connected exposures, some mortgage applications are assessed by the Relevant Credit Authority. 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 the portfolio.

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 event(s) 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 Bank's criticised portfolio, which noted above includes impaired loans, is subject to a more intense assessment and review because of the increased risk associated with them. Credit management and credit risk management continues to be a 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.

The amount of incurred credit losses provided for in the financial statements differs from the amount determined from the expected loss models. For reporting purposes, impairment allowances are recognised only with respect to losses that have been incurred at the balance sheet date based on objective evidence of impairment.

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

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

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

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

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 loan assets.

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

EBSMF rely on AIB Group to conduct 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, 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").

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Collateral
Collateral is required as a secondary source of repayment in the event of the borrower's default. Credit risk mitigation includes the requirement to obtain collateral as set out in AIB Group's policies and procedures. AIB Group maintains guidelines on the acceptability of specific classes of collateral. The principal collateral types for mortgage loans are mortgages over residential real estate.

For residential mortgages, the Bank takes collateral in support of lending transactions for the purchase of residential property. Collateral valuations are required at the time of origination of each residential mortgage. AIB Group adjusts open market property values to take account of the costs of realisation and any discount associated with the realisation of collateral. The fair value at 31 December 2015 is based on property values at origination or date of latest valuation and applying the Central Statistics Office ("CSO") Residential Property Price index (Republic of Ireland) to these values to take account of price movements in the interim.

Forbearance strategies*
Forbearance occurs when a borrower is granted a temporary or permanent concession or agreed change to a loan ('forbearance measure') for reasons relating to the actual or apparent financial stress or distress of that borrower. A forbearance agreement is entered into where the customer is in financial difficulty to the extent that they are unable currently to repay both the principal and interest in accordance with the original contract terms. Modifications to the original contract can be of a temporary (e.g. interest only) or permanent (e.g. term extension) nature.

AIB Group uses a range of tools and treatment strategies to support customers. AIB 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. Key principles include providing support for viable SMEs, and the objective of supporting customers to remain in a family home whenever possible. AIB Group has implemented the standards for the Codes of Conduct in relation to customers in difficulty as set out by the Central Bank of Ireland ensuring these customers are dealt with in a professional and timely manner.

The effectiveness of the forbearance measures over the lifetime of those arrangements will be measured and reviewed. A forbearance measure is deemed to be effective if the borrower meets the modified or original terms of the contract over a sustained period of time resulting in an improved outcome for the Group and the borrower.

AIB 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 AIB Group's Mortgage Arrears Resolution Process ("MARP").

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:

Low fixed interest rate sustainable solution – This solution is to support customers who have an income (and can afford a mortgage), but the income is not currently sufficient to cover full capital and interest on their mortgage based on their current interest rate(s) and/or personal circumstances. Their current income is, however, sufficient to cover full capital and interest at a lower rate. It involves the customer being provided with a low fixed interest rate for an agreed period after which the customer will convert to the prevailing variable rate for the remainder of the term of the mortgage on the basis that there is currently a reasonable expectation that the customer's income and/or circumstances will improve over the period of the reduced rate. The customer must pay full capital and interest throughout.

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 this may also include an element of debt write-off.

Positive equity sustainable solution – This solution involves a reduced payment to support customers who do not qualify for other forbearance solutions such as Split loans due to positive equity.

Credit policies are in place which outline the principles and processes underpinning AIB Group's approach to forbearance which EBSMF has adopted.

*Forms an integral part of the audited financial statements

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Loan loss provisioning*

AIB Group's provisioning policy requires for impairments to be recognised promptly and consistently across the different loan portfolios. A financial asset is considered to be impaired, and therefore its carrying amount is adjusted to reflect the effect of impairment, when there is objective evidence that events have occurred which give rise to an adverse impact on the estimated future cash flows that can be reliably estimated.

Impairment provisions are calculated on individual loans and on groups of loans assessed collectively. All exposures, individually or collectively, are regularly reviewed for objective evidence of impairment. Impairment losses are recorded as charges to the income statement. The carrying amount of impaired loans on the balance sheet is reduced through the use of impairment provision accounts. Losses expected from future events are not recognised.

It is EBSMF's policy to provide for impairment promptly and consistently across the loan book. All business areas formally review and confirm the appropriateness of their provisioning methodologies and the adequacy of their impairment provisions on a quarterly basis. Forborne loans are tested for impairment on a portfolio basis and all EBSMF loans are automatically impaired when the account reaches 90 days past due. In addition, individual loans that are not 90 days past due, which required forbearance, which would result in a loss to the Bank are impaired.

The following are triggers to prompt/guide case managers regarding the requirement to assess for impairment:

Mortgage portfolio triggers

- Deterioration in the debt service capacity;
- A material decrease in rents received on a buy-to-let property;
- Borrowers that are 90 days past due; and
- On receipt of a forbearance request.

In addition, the following factors are taken into consideration when assessing whether a loss event has occurred:

- Loss of significant tenant/material reduction in rental income;
- Significant financial difficulty;
- Decrease in cash flow;
- Loss of employment;
- Net worth; and
- Planned sale of property asset did not take place.

.For those loans where objective evidence of impairment exists, impairment losses are determined considering the following factors:

- the bank's aggregate exposure to the customer;
- the amount and timing of expected receipts and recoveries;
- the realisable value of security (or other credit mitigants) and likelihood of successful repossession;
- the likely deduction of any costs involved in recovery of amounts outstanding; and
- the ability of the borrower to obtain and make payments in the currency of the loan if not denominated in local currency.

Specific provisions

Specific impairment provisions arise when the recovery of a specific loan or group of loans is in doubt based on impairment triggers as outlined above and an assessment that all the expected future cash flows either from the loan itself or from the associated collateral will not be sufficient to repay the loan. The amount of the specific impairment provision is the difference between the present value of expected future cash flows for the impaired loan(s) discounted at the original effective interest rate and the carrying value of the loan(s).

When raising specific impairment provisions, the Bank divides its impaired portfolio into two categories, namely Individually Significant (IS) and Individually Insignificant (II).

Across the Group portfolios, the Individually Significant threshold is €750,000 by customer connection. The calculation of an impairment charge for loans below the 'Significant' threshold is undertaken on a collective basis.

Individually Significant ('IS') Mortgages

All loans that are considered individually significant are assessed on a case-by-case basis throughout the year if there is any objective evidence that a loan may be impaired. Assessment is based on ability to pay and collateral value. Individually significant provisions are calculated using discounted cash flows for each exposure. The cash flows are determined with reference to the individual characteristics of each credit including an assessment of the cash flows that may arise from foreclosure less costs to sell in respect of obtaining and selling any associated collateral. The time period likely to be required to realise the collateral and receive the cash flows is taken into account in estimating the future cash flows and discounting these back to present value

*Forms an integral part of the audited financial statements

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Loan loss provisioning* (continued)

Specific provisions (continued)

Individually Insignificant ('II') Mortgages
Provisioning is assessed on a collective basis to estimate losses for homogeneous groups of loans that are considered individually insignificant. This applies for customer connections less than €750,000.

The individually insignificant mortgage provisioning methodology applies to both owner-occupier and buy-to-let exposures.

Individually insignificant mortgage specific provisions are calculated using a collective and IBNR mortgage provisioning model. This methodology is based on the calculation of three possible resolution outcomes: cure; forbearance (with and without loss); and repossession (forced and voluntary), with different loss rates associated with each. 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 have been refined during the year based on an additional one year dataset.

Key model parameters at 31 December 2015 for owner-occupier mortgages are as follows: cure (6%); and disposal/forbearance (94%). (2014: cure 4% and disposal forbearance 96%).

The corresponding buy-to-let model parameters at 31 December 2015 are as follows: cure (3.5%) and disposal forbearance (96.5%), (2014: cure 0.5% and disposal forbearance 99.5%).

The cure rate parameter in the individually insignificant model reflects the percentage of loans which were impaired/defaulted but have exited impairment/ default after a 12 month satisfactory performance and no loss to the Bank.

The modelled loss is calculated on a case by case basis 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: percentage of forced disposals; costs and time to dispose (voluntary and forced); house price fall from peak; loss rate on advanced forbearance; and haircut on sale (voluntary and forced).

The model parameters are reviewed at Group credit committee on a quarterly basis. The main parameter changes for the year ended 31 December 2015 were an increase in the haircut on disposal for both Dublin and outside Dublin in addition to the application of updated house price fall from peak parameters again for both Dublin and outside Dublin.

Incurred But Not Reported Provisions (IBNR)
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 the Bank has incurred as a result of events occurring before the balance sheet date, which the Bank 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. The estimation of IBNR also takes into consideration re-default and execution risk for restructured loans.

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 (loss emergence rates based on historic grade migration experience or probability of default) 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);
- loss given default rates based on historical loan loss experience, adjusted for current observable data;
- 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, for example, non-impaired forborne mortgages and restructured loans.

*Forms an integral part of the audited financial statements

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Loan loss provisioning (continued)*

The table below sets out the parameters used in the calculation of IBNR provisions for the residential mortgages portfolio:

2015

	Owner-Occupier			Buy-to-let		
Grade	Exposure €m	Average PD %	Average LGD %	Exposure €m	Average PD %	Average LGD %
Good upper	2,529	0.6	16.4	2	1.7	9.8
Good lower	1,546	2.7	21.2	7	5.7	32.3
Watch	431	15.9	19.6	-	96.0	29.5
Vulnerable	66	57.6	20.9	-	-	-

The parameters for Cured and Forborne – Not impaired, are set out below. As a result, these sub-portfolios within the residential mortgages carry a higher level of IBNR:

Cured	326	15.3	20.5	1	18.2	18.2
Forborne – Not impaired	525	100	23.43	1	100	27.6

2014

	Owner-Occupier			Buy-to-let		
Grade	Exposure €m	Average PD %	Average LGD %	Exposure €m	Average PD %	Average LGD %
Good upper	2,410	0.7	17.7	1	1.8	9.0
Good lower	1,698	2.8	23.5	6	3.7	24.3
Watch	440	16.4	21.2	1	96.6	27.0
Vulnerable	123	63.5	22.5	-	35.4	7.3

The parameters for Cured and Forborne – Not impaired, are set out below. As a result, these sub-portfolios within the residential mortgages carry a higher level of IBNR:

Cured	91	11.5	20.2	-	-	-
Forborne – Not impaired	454	15.0	21.0	1	24.6	17.9

Average PD and LGD are based on the PDs and LGDs, weighted by the EAD for all owner-occupier and buy-to-let loans included in the Individually Insignificant /IBNR mortgage model. The mortgage provision model calculates individually insignificant specific provisions and IBNR run rate provisions. Any additional IBNR provision as determined by management judgement is applied at a portfolio level and is not included in the analysis above.

* Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Loan loss provisioning* (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.

Emergence periods are reflective of the characteristics of the particular portfolio. Emergence periods are estimated based on historic loan loss experience supported by back-testing, and as appropriate individual case sampling.

Emergence periods are reviewed on at least an annual basis. At 31 December 2015, there was no change made to the emergence period for the mortgage portfolio (12 months).

Approval process

The AIB Group operates an approval framework for impairment provisions which are approved, depending on amount, by various delegated authorities and referred to Area Credit Committee level, as required. These committees are chaired by a designated Credit Risk representative as outlined in the terms of reference for Credit Committees (approved by ERC), where the valuation/impairment is reviewed and challenged for appropriateness and adequacy. Impairments in excess of the segment authorities are approved by the AIB Group Credit Committee and Board (where applicable). Segment impairments, mortgage model parameters and provisions are ultimately reviewed by the AIB Group Credit Committee as part of the quarterly process.

The valuation assumptions and approaches used in determining the impairment provisions required are documented and the resulting impairment provisions are reviewed and challenged as part of the approval process by segment and AIB Group senior management.

Write-offs

When the prospects of recovering a loan, either partially or fully, do not improve, a point will come when it will be concluded that as there is no realistic prospect of recovery, the loan (and any related specific provision) will be written off. Where the loan is secured, the write-off will take account of receipt of the net realisable value of security held. Partial write-offs may also occur when it is considered that there is no prospect for the recovery of the provisioned amount, for example when a loan enters a legal process. The provision is written off but the remaining reduced loan balance remains on balance sheet as impaired. In addition, some write-off's may reflect restructuring activity agreed with customers who are subject to the terms of the agreement and satisfactory performance.

Reversals of impairment

If the amount of an impairment loss decreased in a subsequent period, and the decrease can be related objectively to an event occurring after the impairment was recognised, the excess is written back by reducing the loan impairment provision amount accordingly. The write-back is recognised in the income statement.

Impact of changes to key assumptions and estimates on the impairment provisions

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. A significant judgemental area is the calculation of individually insignificant and IBNR impairment provisions which are subject to estimation uncertainty.

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 being not 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 house price fall from peak c. 41% Dublin and 42% non-Dublin 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).

Sensitivity to changes in estimates and assumptions are detailed below:

A 1% favourable change in the cure rate used for the collective mortgage provisions would result in a reduction in impairment provisions of 1% (blended rate of owner-occupier/buy-to-let) or c. €4 million.

The value of collateral is estimated by applying changes in house price indices to the original assessed value of the property. A 1% change in the house price fall from peak assumption used for the collective mortgage provisions for December 2015 is estimated to result in movements in provisions of c. €3 million.

* Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Loan loss provisioning **(continued)***

Impact of changes to key assumptions and estimates on the impairment provisions (continued)
A 1% move in the haircut for a Dublin sale would result in a change of €0.84 million in provisions, (€0.73m II and €0.1m IBNR). A 1% move in the haircut for a sale outside Dublin would result in a change of €1.88 million in provisions, (€1.67m II and €0.2m IBNR).

An increase in the assumed repossession rate of 1% for collective mortgage provisions would result in an increase in provisions of 0.6% (blended rate of owner-occupier/buy-to-let) or c. €2 million.

An IBNR provision is made for impairments that have been incurred but have not been separately identifiable at the balance sheet date. This provision is sensitive to changes in the time between the loss event and the date the impairment is specifically identified. This period is known as the loss emergence period. In the Bank's mortgage portfolio, the emergence period is currently 12 months; a decrease of one month in the loss emergence period in respect of the loan portfolio assessed would result in a decrease of c. €3 million.

Individually impaired loans by geographic location and sector*

	2015 € m	2014 € m
Republic of Ireland		
Home Mortgages	**965**	1,279
	965	1,279

Provision cover table

	Impaired Loan Balance	**Specific Provision**	**Specific Provision Cover %**
Home mortgages – 31 December 2015	**965**	**253**	**26%**
Home mortgages – 31 December 2014	1,279	280	22%

The change in specific provision is driven by more conservative estimates in the provision model plus a decrease in impaired loans during 2015 due to restructuring and write-offs of provisions.

The following pages provide details of:

- Credit profile analysis of the owner occupier and buy-to-let portfolios by arrears and provisions;
- Asset quality of residential mortgages;
- Fair value of residential mortgage collateral;
- Arrears profile of mortgages which were past due but not impaired;
- Arrears profile of mortgages which were impaired;
- Forbearance:
  - Owner occupier
  - Buy-to-let
  - Total;
- Possessions;
- Loan to value profile; and
- Origination profile.

*Forms an integral part of the audited financial statements

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

The following table analyses the owner-occupier and buy-to-let residential mortgage portfolios by arrears and provisions:

Statement of financial position*

	2015			2014		
	Owner-Occupier € m	**Buy-to-Let € m**	**Total € m**	Owner-Occupier € m	Buy-to-Let € m	Total € m
Total gross residential mortgages	**5,528**	**18**	**5,546**	5,940	19	5,959
In arrears (>30 days past due)(1)	**994**	**9**	**1,003**	1,360	11	1,371
In arrears (>90 days past due)(1)	**956**	**9**	**965**	1,268	11	1,279
Of which impaired	**956**	**9**	**965**	1,268	11	1,279
Statement of financial position specific provisions	**249**	**4**	**253**	276	4	280
Statement of financial position IBNR provisions	**28**	**-**	**28**	56	-	56

(1) Includes all loans past due whether impaired or not.

Total impaired loans amounted to €965 million at 31 December 2015 (2014: €1,279 million), of which €85 million (2014: €96 million) was individually assessed for impairment and €880 million (2014: €1,183 million) was collectively assessed for impairment.

Provision cover percentage*

	2015			2014		
	Owner-Occupier %	**Buy-to-Let %**	**Total %**	Owner-Occupier %	Buy-to-Let %	Total %
Specific provisions as a % of impaired loans cover	**26.0**	**44.4**	**26.2**	21.8	36.4	21.9

Owner-occupier and Buy-to Let Specific Provision cover rates increased primarily due to parameter changes in the Mortgage Provisioning model.

Income statement (2)

	2015			2014		
	Owner-Occupier € m	**Buy-to-Let € m**	**Total € m**	Owner-Occupier € m	Buy-to-Let € m	Total € m
Income statement specific provisions	**18**	**-**	**18**	15	-	15
Income statement IBNR provisions	**(28)**	**-**	**(28)**	7	-	7
Total impairment provisions	**(10)**	**-**	**(10)**	22	-	22

(2) In the table above, writebacks of provisions are presented as a negative and charges presented as a positive.

Asset quality of residential mortgages*

The following table shows criticised loans for the total residential mortgages portfolio analysed between owner-occupier and buy-to-let. Criticised loans include watch, vulnerable and impaired loans.

	2015			2014		
	Owner-Occupier € m	**Buy-to-Let € m**	**Total € m**	Owner-Occupier € m	Buy-to-Let € m	Total € m
Satisfactory	**4,075**	**9**	**4,084**	4,109	7	4,116
Watch	**431**	**-**	**431**	440	1	441
Vulnerable	**66**	**-**	**66**	123	-	123
Impaired	**956**	**9**	**965**	1,268	11	1,279
Criticised	**1,453**	**9**	**1,462**	1,831	12	1,843
Gross mortgages	**5,528**	**18**	**5,546**	5,940	19	5,959
	%	**%**	**%**	%	%	%
Criticised loans as % of total mortgages	**26.3**	**50.0**	**26.4**	30.8	63.2	30.9
Impaired loans as % of total mortgages	**17.3**	**50.0**	**17.4**	21.3	57.9	21.5

*Forms an integral part of the audited financial statements

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Collateral and other credit enhancements

For residential mortgages, AIB Group takes collateral in support of lending transactions for the purchase of residential property. Collateral valuations are required at the time of origination of each residential mortgage. AIB Group adjusts open market property values to take account of the costs of realisation and any discount associated with the realisation of collateral. The fair value at 31 December 2015 is based on property values at origination or date of latest valuation and applying the CSO Residential Property Price index (Republic of Ireland) and indices to these values to take account of price movements in the interim.

Loans and receivables to customers – residential mortgages*

The following tables show the fair value (FV) of collateral held for residential mortgages at 31 December 2015 and 31 December 2014:

				2015
Fully collateralised	**Neither past due nor impaired € m**	**Past due but not impaired € m**	**Impaired € m**	**Total € m**
Loan-to-value ratio:				
Less than 50%	**948**	**27**	**76**	**1,051**
50%-70%	**834**	**32**	**107**	**973**
71%-80%	**520**	**20**	**70**	**610**
81%-90%	**478**	**22**	**84**	**584**
91%-100%	**469**	**17**	**71**	**557**
	3,249	**118**	**408**	**3,775**
Partially collateralised				
Collateral value relating to loans over 100% LTV	**999**	**50**	**421**	**1,470**
Total collateral value	**4,248**	**168**	**829**	**5,245**
Gross residential mortgages	**4,406**	**175**	**965**	**5,546**
Statement of financial position specific provisions			**(253)**	**(253)**
Statement of financial position IBNR provisions				**(28)**
Net residential mortgages			**712**	**5,265**

				2014
Fully collateralised	**Neither past due nor impaired € m**	**Past due but not impaired € m**	**Impaired € m**	**Total € m**
Loan-to-value ratio:				
Less than 50%	822	32	99	953
50%-70%	775	37	148	960
71%-80%	439	23	88	550
81%-90%	456	24	106	586
91%-100%	418	27	104	549
	2,910	143	545	3,598
Partially collateralised				
Collateral value relating to loans over 100% LTV	1,267	87	540	1,894
Total collateral value	4,177	230	1,085	5,492
Gross residential mortgages	4,430	250	1,279	5,959
Statement of financial position specific provisions			(280)	(280)
Statement of financial position IBNR provisions				(56)
Net residential mortgages			999	5,623

The fair value of collateral held for residential mortgages which are fully collateralised has been capped at the carrying value of the loans outstanding at each year end.

* Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Arrears profile of mortgages which were past due but not impaired*

Residential mortgages are impaired if they are past due for more than 90 days or if the borrower exhibits an inability to meet its obligations to the Bank based on objective evidence of loss events. Loans are deemed impaired where their carrying value is shown to be in excess of the present value of future cash flows, and an appropriate provision is raised. Where loans are not deemed to be impaired, they are collectively assessed as part of the IBNR provision calculation.

The following tables profile the residential mortgage portfolio that was past due but not impaired at 31 December 2015 and 31 December 2014:

			2015
	Owner – Occupier	**Buy-to-Let**	**Total**
	€ m	**€ m**	**€ m**
1 - 30 days	**137**	**-**	**137**
31 - 60 days	**25**	**-**	**25**
61 - 90 days	**13**	**-**	**13**
91 - 180 days	**-**	**-**	**-**
181 - 365 days	**-**	**-**	**-**
Over 365 days	**-**	**-**	**-**
Total past due but not impaired	**175**	**-**	**175**

			2014
	Owner – Occupier	Buy-to-Let	Total
	€ m	€ m	€ m
1 - 30 days	158	-	158
31 - 60 days	60	-	60
61 - 90 days	32	-	32
91 - 180 days	-	-	-
181 - 365 days	-	-	-
Over 365 days	-	-	-
Total past due but not impaired	250	-	250

Arrears profile of mortgages which were impaired*

The following tables profile the residential mortgage portfolio that was impaired at 31 December 2015 and 31 December 2014:

			2015
	Owner – Occupier	**Buy-to-Let**	**Total**
	€ m	**€ m**	**€ m**
Not past due	**259**	**2**	**261**
1 - 30 days	**49**	**-**	**49**
31 - 60 days	**25**	**-**	**25**
61 - 90 days	**17**	**-**	**17**
91 - 180 days	**53**	**-**	**53**
181 - 365 days	**70**	**-**	**70**
Over 365 days	**483**	**7**	**490**
Total impaired	**956**	**9**	**965**

			2014
	Owner – Occupier	Buy-to-Let	Total
	€ m	€ m	€ m
Not past due	296	1	297
1 - 30 days	83	-	83
31 - 60 days	34	-	34
61 - 90 days	26	-	26
91 - 180 days	92	1	93
181 - 365 days	155	1	156
Over 365 days	582	8	590
Total impaired	1,268	11	1,279

Impaired loans decreased by €314m as restructuring and write offs exceeded newly impaired loans. New to impaired were significantly lower in 2015 compared to 2014 driven by an improved economic environment. Of the residential mortgage portfolio that was impaired at 31 December 2015, €261m or 27.0% was not past due (2014: €297m or 23%) of which €214m (2014: €248m) were subject to forbearance measures.

* Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Forbearance
AIB has developed a Mortgage Arrears Resolution Strategy ('MARS') for dealing with mortgage customers in difficulty or likely to be in difficulty which builds on and formalises AIB Group's Mortgage Arrears Resolution process. The core objectives of MARS are to ensure that arrears solutions are sustainable in the long-term and that they comply with the spirit and the letter of all regulatory requirements. MARS includes long-term forbearance solutions which have been devised to assist existing primary residential mortgage customers in difficulty.

The following table analyses the movement in stock of loans subject to forbearance by (i) owner-occupier, (ii) buy-to-let and (iii) total residential mortgages at 31 December 2015 and 31 December 2014:

Residential owner-occupier mortgages – subject to forbearance*

	2015		2014	
	Number	**Balance €m**	Number	Balance €m
At 1 January	**8,026**	**950**	4,914	578
Additions	**1,954**	**271**	4,204	536
Expired arrangements	**(1,096)**	**(131)**	(880)	(112)
Payments	**-**	**(51)**	-	(48)
Interest	**-**	**30**	-	29
Closed accounts [(1)]	**(255)**	**(10)**	(212)	(10)
Advanced Forbearance Arrangements - Valuation Adjustments	**-**	**(3)**	-	-
Write-Offs [(2)]	**(7)**	**(7)**	-	-
Transfer from owner-occupier to buy-to-let	**(3)**	**(1)**	-	-
Other movements	**-**	**-**	-	(23)
At 31 December	**8,619**	**1,048**	8,026	950

Buy-to-let mortgages – subject to forbearance*

	2015		2014	
	Number	**Balance €m**	Number	Balance €m
At 1 January	**20**	**2**	18	2
Additions	**3**	**-**	6	1
Expired arrangements	**(1)**	**-**	(4)	(1)
Payments	**-**	**(2)**	-	-
Interest	**-**	**2**	-	-
Closed accounts [(1)]	**-**	**-**	-	-
Advanced Forbearance Arrangements - Valuation Adjustments	**-**	**-**	-	-
Write-Offs [(2)]	**-**	**-**	-	-
Transfer from owner-occupier to buy-to-let	**3**	**1**	-	-
Other movements	**-**	**-**	-	-
At 31 December	**25**	**3**	20	2

Total mortgage portfolio – subject to forbearance*

	2015		2014	
	Number	**Balance €m**	Number	Balance €m
At 1 January	**8,046**	**952**	4,932	580
Additions	**1,957**	**271**	4,210	537
Expired arrangements	**(1,097)**	**(131)**	(884)	(113)
Payments	**-**	**(53)**	-	(48)
Interest	**-**	**32**	-	29
Closed accounts [(1)]	**(255)**	**(10)**	(212)	(10)
Advanced Forbearance Arrangements - Valuation Adjustments	**-**	**(3)**	-	-
Write-Offs [(2)]	**(7)**	**(7)**	-	-
Transfer from owner-occupier to buy-to-let	**-**	**-**	-	-
Other movements	**-**	**-**	-	(23)
At 31 December	**8,644**	**1,051**	8,046	952

(1) Accounts closed during the year due primarily to customer repayments and redemptions.

(2) Includes contracted and non-contracted write-offs in 2015.

The stock of loans subject to forbearance measures increased by €99m in 2015 (2014: increased by €372m), mainly due to the increase in arrears capitalisations and low fixed interest rate. This increase is driven by the Group's strategy to deliver sustainable long-term solutions to customers and support customers in remaining in their family home.

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Forbearance (continued)
The following tables further analyse by type of forbearance, (i) owner-occupier, (ii) buy-to-let and (iii) total residential mortgages that were subject to forbearance measures at 31 December 2015 and 31 December 2014:

Residential owner-occupier mortgages*

2015

	Total		Loans >90 days in arrears and/or impaired		Loans neither >90 days in arrears nor impaired	
	Number	Balance € m	Number	Balance € m	Number	Balance € m
Interest only	614	93	311	52	303	41
Reduced payment (greater than interest only)	-	-	-	-	-	-
Payment moratorium	-	-	-	-	-	-
Low fixed interest rate	456	70	29	6	427	64
Arrears capitalisation	5,088	612	2,015	251	3,073	361
Term extension	1,132	90	57	5	1,075	85
Split mortgage	901	146	357	60	544	86
Sale for loss	112	6	72	4	40	2
Positive equity solution	315	30	10	1	305	29
Other	1	1	-	-	1	1
Total	**8,619**	**1,048**	**2,851**	**379**	**5,768**	**669**

2014

	Total		Loans >90 days in arrears and/or impaired		Loans neither >90 days in arrears nor impaired	
	Number	Balance € m	Number	Balance € m	Number	Balance € m
Interest only	1,152	164	583	86	569	78
Reduced payment (greater than interest only)	-	-	-	-	-	-
Payment moratorium	-	-	-	-	-	-
Low fixed interest rate	160	24	116	18	44	6
Arrears capitalisation	4,263	493	2,185	251	2,078	242
Term extension	1,507	127	153	13	1,354	114
Split mortgage	781	128	781	128	-	-
Sale for loss	88	6	61	5	27	1
Positive equity solution	70	7	52	5	18	2
Other	5	1	2	-	3	1
Total	8,026	950	3,933	506	4,093	444

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Forbearance (continued)

Buy-to-let mortgages*

2015

	Total		Loans >90 days in arrears and/or impaired		Loans neither >90 days in arrears nor impaired	
	Number	Balance € m	Number	Balance € m	Number	Balance € m
Interest only	1	-	1	-	-	-
Reduced payment (greater than interest only)	-	-	-	-	-	-
Payment moratorium	-	-	-	-	-	-
Low fixed interest rate	-	-	-	-	-	-
Arrears capitalisation	9	1	3	-	6	1
Term extension	10	1	1	-	9	1
Split mortgage	-	-	-	-	-	-
Sale for loss	5	1	5	1	-	-
Positive equity solution	-	-	-	-	-	-
Other	-	-	-	-	-	-
Total	**25**	**3**	**10**	**1**	**15**	**2**

2014

	Total		Loans >90 days in arrears and/or impaired		Loans neither >90 days in arrears nor impaired	
	Number	Balance € m	Number	Balance € m	Number	Balance € m
Interest only	2	-	2	-	-	-
Reduced payment (greater than interest only)	-	-	-	-	-	-
Payment moratorium	-	-	-	-	-	-
Low fixed interest rate	-	-	-	-	-	-
Arrears capitalisation	6	-	5	-	1	-
Term extension	7	1	-	-	7	1
Split mortgage	-	-	-	-	-	-
Sale for loss	5	1	5	1	-	-
Positive equity solution	-	-	-	-	-	-
Other	-	-	-	-	-	-
Total	20	2	12	1	8	1

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Forbearance (continued)

Total mortgage portfolio*

2015

	Total		**Loans >90 days in arrears and/or impaired**		**Loans neither >90 days in arrears nor impaired**	
	Number	**Balance € m**	**Number**	**Balance € m**	**Number**	**Balance € m**
Interest only	**615**	**93**	**312**	**52**	**303**	**41**
Reduced payment (greater than interest only)	**-**	**-**	**-**	**-**	**-**	**-**
Payment moratorium	**-**	**-**	**-**	**-**	**-**	**-**
Low fixed interest rate	**456**	**70**	**29**	**6**	**427**	**64**
Arrears capitalisation	**5,097**	**613**	**2,018**	**251**	**3,079**	**362**
Term extension	**1,142**	**91**	**58**	**5**	**1,084**	**86**
Split mortgage	**901**	**146**	**357**	**60**	**544**	**86**
Sale for loss	**117**	**7**	**77**	**5**	**40**	**2**
Positive equity solution	**315**	**30**	**10**	**1**	**305**	**29**
Other	**1**	**1**	**-**	**-**	**1**	**1**
Total	**8,644**	**1,051**	**2,861**	**380**	**5,783**	**671**

2014

	Total		Loans >90 days in arrears and/or impaired		Loans neither >90 days in arrears nor impaired	
	Number	Balance € m	Number	Balance € m	Number	Balance € m
Interest only	1,154	164	585	86	569	78
Reduced payment (greater than interest only)	-	-	-	-	-	-
Payment moratorium	-	-	-	-	-	-
Low fixed interest rate	160	24	116	18	44	6
Arrears capitalisation	4,269	493	2,190	251	2,079	242
Term extension	1,514	128	153	13	1,361	115
Split mortgage	781	128	781	128	-	-
Sale for loss	93	7	66	6	27	1
Positive equity solution	70	7	52	5	18	2
Other	5	1	2	-	3	1
Total	8,046	952	3,945	507	4,101	445

A key feature of the forbearance portfolio is the growth in the proportion of advanced forbearance solutions (mainly split mortgages, positive equity solutions and low fixed interest rate) driven by the AIB Group's strategy to deliver sustainable long-term solutions to customers. Advanced forbearance solutions at €253 million accounted for 24% of the total forbearance portfolio as at 31 December 2015, compared to 17% (€166 million) as at 31 December 2014. Following restructure, loans are reported as impaired for a probationary period of at least 12 months (unless part of a larger individually assessed case).

58% of the loans subject to forbearance measures at 31 December 2015 are loans on which arrears have been capitalised. These loans, along with Term Extensions, remain within the stock of forbearance for a period of 5 years. The increase in the stock of loans on arrears capitalisation in 2015 includes some customers whose interest only arrangement had expired during 2015 but who received a capitalisation of arrears at some time over the last 5 years.

Interest income on impaired loans amounted to €29 million in 2015. At 31 December 2015, the net carrying value of impaired loans amounted to €712 million (€965m impaired balance - €253m closing provision) which included forborne impaired mortgages of €315 million (€380m forborne impaired balance - €65m forborne closing provision).

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Forbearance (continued)

Credit profile of residential mortgages in forbearance

Forbearance stock - past due but not impaired*

All loans that are assessed for a forbearance solution are tested for impairment either individually or collectively, irrespective of whether such loans are past due or not. Where the loans are deemed not to be impaired, they are collectively assessed as part of the IBNR provision calculation.

The following table profiles the residential mortgage portfolio that was subject to forbearance measures and which was past due but not impaired at 31 December 2015 and 31 December 2014:

	Owner – Occupier €m	Buy-to-Let €m	2015 Total €m
1 - 30 days	67	-	67
31 - 60 days	15	-	15
61 - 90 days	7	-	7
91 - 180 days	-	-	-
181 - 365 days	-	-	-
Over 365 days	-	-	-
Total past due but not impaired	**89**	**-**	**89**

	Owner – Occupier €m	Buy-to-Let €m	2014 Total €m
1 - 30 days	50	-	50
31 - 60 days	22	-	22
61 - 90 days	13	-	13
91 - 180 days	-	-	-
181 - 365 days	-	-	-
Over 365 days	-	-	-
Total past due but not impaired	85	-	85

8% of the residential mortgage portfolio that was subject to forbearance measures was past due but not impaired at 31 December 2015 (31 December 2014: 9%).

Forbearance stock – impaired*

The following table profiles the residential mortgage portfolio that was subject to forbearance measures and which was impaired at 31 December 2015 and 31 December 2014:

	Owner – Occupier €m	Buy-to-Let €m	2015 Total €m
Not past due	213	1	214
1 - 30 days	38	-	38
31 - 60 days	17	-	17
61 - 90 days	11	-	11
91 - 180 days	30	-	30
181 - 365 days	22	-	22
Over 365 days	48	-	48
Total impaired	**379**	**1**	**380**

* Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Forbearance (continued)

Credit profile of residential mortgages in forbearance (continued)

Forbearance stock – impaired (continued)*

			2014
	Owner – Occupier € m	Buy-to-Let € m	Total € m
Not past due	248	-	248
1 - 30 days	74	-	74
31 - 60 days	26	-	26
61 - 90 days	14	-	14
91 - 180 days	35	-	35
181 - 365 days	42	-	42
Over 365 days	67	1	68
Total impaired	506	1	507

The proportion of forbearance that is impaired decreased from 53% at 31 December 2014 to 36% at 31 December 2015. This is mainly due to accounts restructured in 2014 becoming unimpaired after a probationary period of 12 months. The proportion of forborne impaired loans that were not past due increased from 49% at 31 December 2014 to 56% at 31 December 2015.

Analysis by Loan-to-value ('LTV') of residential mortgages in forbearance*

The following table profiles the residential mortgage portfolio that was subject to forbearance measures by the indexed loan-to value ratios at 31 December 2015 and 31 December 2014:

			2015
Loan-to-value (LTV) ratio:	**Owner – Occupier € m**	**Buy-to-Let € m**	**Total € m**
Less than 50%	**158**	**1**	**159**
50% - 70%	**195**	**-**	**195**
71% - 80%	**117**	**-**	**117**
81% - 90%	**118**	**-**	**118**
91% - 100%	**89**	**-**	**89**
101% -120%	**179**	**1**	**180**
121% - 150%	**174**	**-**	**174**
Greater than 150%	**12**	**-**	**12**
Unsecured (Zero Collateral)	**6**	**1**	**7**
Total forbearance	**1,048**	**3**	**1,051**

			2014
Loan-to-value (LTV) ratio:	Owner – Occupier € m	Buy-to-Let € m	Total € m
Less than 50%	124	-	124
50% - 70%	156	-	156
71% - 80%	93	-	93
81% - 90%	100	-	100
91% - 100%	89	-	89
101% -120%	141	1	142
121% - 150%	206	-	206
Greater than 150%	34	-	34
Unsecured (Zero Collateral)	7	1	8
Total forbearance	950	2	952

The degree of negative equity in the residential mortgage portfolio that was subject to forbearance measures at 31 December 2015 has reduced to 35% compared to 41% at 31 December 2015, due primarily to increases in property prices and loan repayments in 2015.

* Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Properties in possession*

EBSMF seeks to avoid repossession through working with customers, but where agreement cannot be reached, EBSMF proceeds to repossession of the property or the appointment of a receiver, using external agents to realise the maximum value as soon as is practicable. Where EBSMF believes that the proceeds of sale of a 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.

For the purpose of the following table, a residential property is considered to be in EBSMF's possession when it has taken possession of and is in a position to dispose of the property. This includes situations of repossession, voluntary surrender and abandonment of the property.

The number (stock) of repossessions as at 31 December 2015 and 31 December 2014 is set out below:

	2015		2014	
	Stock	**Balance Outstanding €m**	Stock	Balance Outstanding €m
Owner-occupier	**176**	**43**	147	36
Buy-to-let	**4**	**1**	4	1
Total	**180**	**44**	151	37

The increase in the stock of properties in 2015 relates to 155 properties repossessed offset by 126 disposals. There continues to be an increase in stock due to continued focus on arrears management.

The following tables analyse the disposals of repossessed properties during the years 31 December 2015 and 31 December 2014:

2015

	Number of Disposals	**Balance outstanding at repossession date € m**	**Gross sales proceeds € m**	**Costs to sell € m**	**Loss on sale[(1)] € m**	**Average LTV at sale Price %**
Owner-occupier	**124**	**34**	**14**	**1**	**21**	**240%**
Buy-to-let	**2**	**1**	**-**	**-**	**-**	**271%**
Total residential	**126**	**35**	**14**	**1**	**21**	**250%**

2014

	Number of Disposals	Balance outstanding at repossession date € m	Gross sales proceeds € m	Costs to sell € m	Loss on sale[(1)] € m	Average LTV at sale Price %
Owner-occupier	13	3	1	-	2	240%
Buy-to-let	2	-	-	-	-	309%
Total residential	15	3	1	-	2	246%

[(1)]Before specific impairment provisions.

The figures in the tables above do not cross total due to rounding.

Losses on the sale of properties in possession are recognised in the Income Statement as part of the specific provision charge.

The disposal of 126 residential properties resulted in a loss on disposal of €21 million at 31 December 2015 (before specific impairment provisions), (2014: 15 disposals, €2 million loss on disposal).

* Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Loan-to-value (LTV) (index linked) information

The property values used in the completion of the following loan-to-value tables are determined with reference to the original or most recent valuation, indexed to the Central Statistics Office ("CSO") Residential Property Price Index in the Republic of Ireland for November 2015. The CSO Residential Property Price Index for November 2015 reported that national residential property prices were 34% lower than their highest level in early 2007 and reported an annual increase in residential property prices of 6.5% in the financial year to 30 November 2015.

Actual and average LTV across mortgage portfolios*

The following tables profile the residential mortgage portfolio by the indexed loan-to-value ('LTV') ratios and the weighted average indexed LTV ratios at 31 December 2015 and 31 December 2014:

			2015
Loan-to-value (LTV) ratio:	**Owner – Occupier**	**Buy-to-Let**	**Total**
	€ m	**€ m**	**€ m**
Less than 50%	**1,049**	**1**	**1,050**
50% - 70%	**971**	**2**	**973**
71% - 80%	**609**	**2**	**611**
81% - 90%	**583**	**1**	**584**
91% - 100%	**556**	**1**	**557**
101% -120%	**862**	**6**	**868**
121% - 150%	**748**	**3**	**751**
Greater than 150%	**124**	**1**	**125**
Unsecured (Zero Collateral)	**26**	**1**	**27**
Total	**5,528**	**18**	**5,546**
Weighted average indexed LTV (1)			
Stock of residential mortgages at year end	**82%**	**98%**	**82%**
New residential mortgages during year	**-**	**-**	**-**
Impaired mortgages	**106%**	**111%**	**106%**

			2014
Loan-to-value (LTV) ratio:	Owner – Occupier	Buy-to-Let	Total
	€ m	€ m	€ m
Less than 50%	952	1	953
50% - 70%	959	1	960
71% - 80%	549	1	550
81% - 90%	584	2	586
91% - 100%	549	1	550
101% -120%	947	4	951
121% - 150%	1,121	6	1,127
Greater than 150%	263	2	265
Unsecured (Zero Collateral)	16	1	17
Total	5,940	19	5,959
Weighted average indexed LTV (1)			
Stock of residential mortgages at year end	90%	108%	90%
New residential mortgages during year	-	-	-
Impaired mortgages	109%	117%	109%

(1)Weighted average indexed LTV's are the individual indexed LTV calculations weighted by the mortgage balance against each property.

32% of the total owner-occupier and 61% of the total buy-to-let mortgages were in negative equity at 31 December 2015, compared to 40% and 68% respectively at 31 December 2014. The weighted average indexed loan-to-value for the total residential mortgage book was 82% at 31 December 2015 compared to 90% at 31 December 2014, with the reduction driven primarily by the increase in property prices in 2014, coupled with amortisation of the loan book and restructuring activity.

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Actual and average LTV across mortgage portfolios (continued)

Neither past due nor impaired*

The following tables profile the residential mortgage portfolio that was neither past due nor impaired by the indexed loan to value ratios at 31 December 2015 and 31 December 2014

Loan-to-value (LTV) ratio:	**Owner – Occupier €m**	**Buy-to-Let €m**	**2015 Total €m**
Less than 50%	**948**	**1**	**949**
50% - 70%	**833**	**1**	**834**
71% - 80%	**519**	**2**	**521**
81% - 90%	**478**	**1**	**479**
91% - 100%	**468**	**-**	**468**
101% -120%	**678**	**3**	**681**
121% - 150%	**470**	**1**	**471**
Greater than 150%	**2**	**-**	**2**
Unsecured (Zero Collateral)	**1**	**-**	**1**
Total	**4,397**	**9**	**4,406**

Loan-to-value (LTV) ratio:	Owner – Occupier €m	Buy-to-Let €m	2014 Total €m
Less than 50%	821	1	822
50% - 70%	774	1	775
71% - 80%	439	1	440
81% - 90%	455	1	456
91% - 100%	418	-	418
101% -120%	721	2	723
121% - 150%	755	2	757
Greater than 150%	38	-	38
Unsecured (Zero Collateral)	1	-	1
Total	4,422	8	4,430

The proportion of residential mortgages that were neither past due nor impaired and in negative equity at 31 December 2015 decreased in comparison to 31 December 2014, reflecting the increases in residential property prices in the period, coupled with amortisation of the loan book. 26% of residential mortgages that were neither past due nor impaired were in negative equity at 31 December 2015 compared to 34% at 31 December 2014.

Past due but not impaired*

The following tables profile the residential mortgage portfolio that was past due but not impaired at 31 December 2015 and 31 December 2014:

Loan-to-value (LTV) ratio:	**Owner – Occupier €m**	**Buy-to-Let €m**	**2015 Total €m**
Less than 50%	**27**	**-**	**27**
50% - 70%	**32**	**-**	**32**
71% - 80%	**20**	**-**	**20**
81% - 90%	**22**	**-**	**22**
91% - 100%	**17**	**-**	**17**
101% -120%	**32**	**-**	**32**
121% - 150%	**25**	**-**	**25**
Greater than 150%	**-**	**-**	**-**
Unsecured (Zero Collateral)	**-**	**-**	**-**
Total	**175**	**-**	**175**

Loan-to-value (LTV) ratio:	Owner – Occupier €m	Buy-to-Let €m	2014 Total €m
Less than 50%	32	-	32
50% - 70%	37	-	37
71% - 80%	23	-	23
81% - 90%	24	-	24
91% - 100%	27	-	27
101% - 120%	43	-	43
121% - 150%	58	-	58
Greater than 150%	6	-	6
Unsecured (Zero Collateral)	-	-	-
Total	250	-	250

Of the residential mortgages that were past due but not impaired at 31 December 2015, 33% were in negative equity at 31 December 2015 compared to 43% at 31 December 2014.

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Actual and average LTV across mortgage portfolios (continued)

Greater than 90 days past due and/or impaired*

The following tables profile the residential mortgage portfolio that was greater than 90 days past due and/or impaired by the indexed LTV ratios at 31 December 2015 and 31 December 2014:

Loan-to-value (LTV) ratio:	Owner – Occupier €m	Buy-to-Let €m	2015 Total €m
Less than 50%	75	-	75
50% - 70%	106	1	107
71% - 80%	70	1	71
81% - 90%	83	1	84
91% - 100%	71	-	71
101% -120%	152	2	154
121% - 150%	253	2	255
Greater than 150%	121	1	122
Unsecured (Zero Collateral)	25	1	26
Total	**956**	**9**	**965**

Loan-to-value (LTV) ratio:	Owner – Occupier €m	Buy-to-Let €m	2014 Total €m
Less than 50%	99	1	100
50% - 70%	148	-	148
71% - 80%	87	-	87
81% - 90%	105	1	106
91% - 100%	104	-	104
101% -120%	183	2	185
121% - 150%	308	4	312
Greater than 150%	219	2	221
Unsecured (Zero Collateral)	15	1	16
Total	1,268	11	1,279

The proportion of residential mortgages that were greater than 90 days past due and/or impaired and in negative equity at 31 December 2015 (58%) increased in comparison to 31 December 2014 (57%). Total loans greater than 90 days past due and/or impaired has decreased by 25%. The decreases in arrears can be mainly attributable to restructuring activity in the period.

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.1 Credit risk (continued)

Residential Mortgages by year of origination*

The following tables profile the residential mortgage portfolio and impaired residential mortgage portfolio at 31 December 2015 and 2014 by year of origination:

				2015
	Mortgage portfolio		Impaired mortgage portfolio	
	Number	Balance €m	Number	Balance €m
1996 and before	1,997	62	177	8
1997	859	20	59	2
1998	867	26	76	5
1999	986	37	85	6
2000	1,203	65	115	9
2001	1,582	107	131	12
2002	2,195	177	172	18
2003	2,477	197	272	28
2004	2,858	262	277	32
2005	4,242	431	504	74
2006	7,321	1,025	1,106	197
2007	6,980	1,053	1,473	270
2008	6,505	940	1,230	205
2009	4,156	531	454	62
2010	4,155	566	239	36
2011	392	47	8	1
2012	-	-	-	-
2013	-	-	-	-
2014	-	-	-	-
2015	-	-	-	-
Total	**48,775**	**5,546**	**6,378**	**965**

				2014
	Mortgage portfolio		Impaired mortgage portfolio	
	Number	Balance €m	Number	Balance €m
1996 and before	2,690	76	317	15
1997	941	25	93	4
1998	954	31	104	6
1999	1,079	44	143	9
2000	1,366	75	162	13
2001	1,705	121	188	17
2002	2,357	198	259	27
2003	2,666	220	389	39
2004	3,037	288	416	48
2005	4,608	467	692	97
2006	7,617	1,096	1,508	265
2007	7,237	1,119	1,948	350
2008	6,755	994	1,636	268
2009	4,313	562	590	79
2010	4,382	593	295	41
2011	408	50	3	1
2012	-	-	-	-
2013	-	-	-	-
2014	-	-	-	-
Total	52,115	5,959	8,743	1,279

The majority (€3.4bn or 62%) of the €5.5bn residential mortgage portfolio was originated between 2005 and 2008, of which 22% (€0.7bn) was impaired at 31 December 2015.

Further information on credit risk
Further information on credit risk can be found in the notes to the financial statements:

- Provisions for impairment of loans and receivables *(note 8);*
- Derivatives financial instruments *(note 10);*
- Loans and receivables to banks *(note 11);*
- Loans and receivables to customers *(note 12).*

* Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.2 Liquidity risk*

Liquidity risk is the risk that the Bank will not be able to fund its assets and meet its payment obligations as they come due, without incurring unacceptable costs or losses. The objective of liquidity management is to ensure that, at all times, the Bank holds sufficient funds to meet its contracted and contingent commitments and regulatory requirements, at an economic price.

EBSMF's Liquidity risk has been incorporated into the AIB centralised risk management model in line with AIB common approach to Treasury Risk management. Under this centralised approach the management of liquidity and related activities are overseen and controlled by AIB Treasury, and as a consequence, EBSMF is integrated with its ultimate parent, AIB Group for funding, and liquidity management.

AIB Group, including EBSMF, applies the maturity mismatch approach to the management of liquidity following the adoption of this method by the CBI in July 2007 as set out in the 'Requirements for the Management of Liquidity Risk' regulatory document. The overall purpose of a maturity mismatch approach is to ensure that AIB Group, including EBSMF, 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').

In October 2011, the Central Bank revoked the requirement for the Bank to comply with the 'Requirements for the Management of Liquidity Risk' regulatory document under Section 9.2 of that document. From this time, EBSMF Liquidity Ratios have been reflected in the AIB Group Consolidated Liquidity Reports.

The maturity mismatch approach measures liquidity risk in the form of liquidity ratios, which are calculated and reported on a daily basis internally to the Treasury Front Office and monthly to the Financial Regulator as part of the AIB Group Regulatory Liquidity Reports. The Liquidity Ratios are also reported on a monthly basis to EBS Group Management team. Any breaches of limits are escalated immediately in line with the escalation procedure.

In addition to the maturity mismatch approach, AIB monitors and manages the funding support provided by its deposit base to its loan portfolio through a series of measures including the Capital Requirements Directive IV ("CRD") related liquidity ratios i.e. the Liquidity Coverage Ratio ("LCR") and Net Stable Funding Ratio ("NSFR") as required by the 2013 Capital Requirements Regulation ("CRR") and the CRD and ultimately the LCR as required by the published European Commission Delegated Regulation ("the Delegated Act") to supplement the CRR and which came into force on 1 October 2015.

In accordance with Capital Requirements Regulation (Regulation (EU) No. 575/2013), the Bank has appointed AIB as its liquidity manager to fulfil daily cashflow management, oversee any changes required in liquidity management or reporting and manage the Bank's liquidity risk as part of the overall AIB Group liquidity risk management process. This means the procedures by which these liquidity management activities are performed, and the procedures by which AIB Group ensures the Bank complies with AIB Group Liquidity Policy, are managed through a Managed Service Agreement ("MSA").

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

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

AIB Group conducts both regular and ad-hoc funding and liquidity risk stress testing to assess on an ongoing basis the ability of AIB, including EBSMF, 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. Funding contingency plans are continually under review. These activities are conducted in conjunction with AIB Group Asset & Liability Management.

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.2 Liquidity risk* (continued)

Financial liabilities by contractual maturity*

2015	Repayable on demand € m	3 months or less but not repayable on demand € m	1 year or less but over 3 months € m	5 years or less but over 1 year € m	Over 5 years € m	Total € m
Deposits by Banks	-	2,271	-	-	-	2,271
Derivative financial instruments	-	-	-	-	20	20
Debt securities in issue	-	425	666	796	500	2,387
Total	-	2,696	666	796	520	4,678

2014	Repayable on demand € m	3 months or less but not repayable on demand € m	1 year or less but over 3 months € m	5 years or less but over 1 year € m	Over 5 years € m	Total € m
Deposits by Banks	-	3,383	-	-	-	3,383
Derivative financial instruments	-	-	-	-	22	22
Debt securities in issue	-	-	432	1,375	-	1,807
Other liabilities	-	-	-	-	-	-
Total	-	3,383	432	1,375	22	5,212

3.3 Conduct Risk*

Conduct Risk is the risk that inappropriate actions, or inaction, by the Bank can cause poor and unfair outcomes for its customers, and potential market instability. The Conduct Risk management strategy is to adopt sound practices in the identification, evaluation, mitigation, monitoring and reporting of Conduct Risks to ensure that they are managed in accordance with the Conduct Risk Appetite of AIB Group. This includes the embedding of a customer centric culture aligned to AIB's Brand Values and Code of Conduct, the promotion of good conduct throughout the organisation and the operation of a control environment for the measurement and management of Conduct Risk, in accordance with the relevant limits and other requirements set out in the Board Risk Appetite Statement.

The Central Bank announced in October 2015 that it had commenced a broad examination of tracker mortgage-related issues across Irish Banks. In December 2015, the Central Bank confirmed to the affected banks that the objective of the examination is to assess compliance with both contractual and regulatory requirements. In circumstances where customer detriment is identified from this Examination, the Group is required to provide appropriate redress and compensation in line with the CBI "Principles for Redress". Notwithstanding the provisions for customer redress as set out in note 18 "Provisions for liabilities and commitments", it is not possible at this stage to assess the final outcome of the Examination or any related litigation or regulatory action required.

3.4 Operational risk*

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. It includes legal risk, information technology risk, business continuity risk, outsourcing risk, and health and safety risk. It does not include strategic and business risk. As such, operational risk covers a broad range of potential sources of financial loss which the Bank and the AIB Group actively seek to mitigate against.

The key people, systems and processes supporting EBSMF are provided by AIB Group and this relationship is governed by a Managed Services Agreement. The AIB Group operational risk framework applies across all areas of AIB Group including EBS Limited and the Bank. The AIB Group Operational Risk function is responsible for overseeing the management of operational risk across AIB Group. A key focus of operational risk management in EBSMF is the oversight of outsourced service activities, in particular activities related to the requirements of the ACS Act.

EBSMF undertakes an operational risk self-assessment which focuses on activities specific to the Bank e.g. the Bank's funding activities and its compliance with the ACS Act. This process includes periodic assessments of relevant operational risks and the effectiveness of the related controls to address these risks. It complements the risk-based audit approach applied by internal audit in its role as independent assessor of management's control and risk management processes.

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.5 Regulatory compliance risk*

Regulatory compliance risk is defined as the risk of regulatory sanctions, material financial loss or loss to reputation which the Bank may suffer as a result of failure to comply with all applicable laws, regulations, rules, related self-regulatory standards and codes of conduct applicable to its activities.

The level of regulatory risk remained high in 2015 as the regulatory landscape for the banking sector continued to evolve with a strong focus on supporting the stability of the banking system and ensuring appropriate resolution and recovery mechanisms are in place post the global financial crisis. The Bank is committed to proactively identifying regulatory and compliance obligations arising in the Bank's operating markets in Ireland, and ensuring the timely implementation of regulatory change. Throughout 2015, projects were mobilised within AIB Group to prepare for the significant regulatory change horizon as outlined in AIB Group's annual report: Governance and Oversight – Supervision and Regulation.

The level of regulatory change is expected to continue in 2016.

EBS Mortgage Finance's regulatory compliance risk is managed as part of the overall AIB Group Regulatory compliance framework. This includes risk identification and assessment, risk management and mitigation, and risk monitoring and reporting processes.

3.6 Non-trading interest rate risk*

Market risk is the risk that changes in market prices, such as interest rate, and credit spreads (funding risk) will affect the Bank's income. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk. The Bank has aligned the measurement methods and reporting of its market risk exposures to that of AIB Group.

The Bank is not allowed to engage in proprietary trading under the conditions of the Asset Covered Securities Act and its license. AIB Group Treasury manages non trading Interest Rate Risk using gap and sensitivity analysis. Derivatives, such as interest rate swaps are used to hedge these market risks.

Interest rate risk is the risk that changes in interest rates will affect the Bank's income, or the value of its holdings of financial instruments. The objective of interest rate risk management is to manage and control interest rate risk exposures in accordance with the requirements of the Asset Covered Securities Act and internal parameters.

The Bank has outsourced the measurement and reporting management of its interest rate risk to AIB Group. AIB Capital and Liquidity in conjunction with AIB Group Treasury measures and manages these risks using gap and sensitivity analysis. Derivatives such as interest rate swaps are used by the Bank for hedging purposes (i.e. reducing risk) only.

EBS Market risk exposures are managed by AIB Group Treasury together with the Group exposures to such risks under the AIB Centralised Risk Management model.

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.6 Non-trading interest rate risk* (continued)

Interest Rate Sensitivity*

The net interest rate sensitivity of EBS Mortgage Finance at 31 December 2015 is illustrated in the following table;

	0≤1mth	1≤3mths	3≤12mths	1≤2yrs	2≤3yrs	3≤4yrs	4≤5yrs	5yrs+	Rate Insensitive	Total
Assets	€ m	€ m	€ m	€ m	€ m	€ m	€ m	€ m	€ m	€ m
Loans and receivables to customers	5,036	40	154	105	84	21	60	46	(281)	5,265
Loans and receivables to banks	60	-	-	-	-	-	-	-	-	60
Derivatives and other financial instruments	-	-	-	-	-	-	-	-	20	20
Other assets	-	-	-	-	-	-	-	-	2	2
Total Assets	5,096	40	154	105	84	21	60	46	(259)	5,347
Liabilities										
Deposits by banks	2,271	-	-	-	-	-	-	-	-	2,271
Derivatives and other financial instruments	-	-	-	-	-	-	-	-	20	20
Debt issued	2,387	-	-	-	-	-	-	-	-	2,387
Other liabilities	-	-	-	-	-	-	-	-	43	43
Shareholders' equity	-	-	-	-	-	-	-	-	626	626
Total Liabilities	4,658	-	-	-	-	-	-	-	689	5,347
Derivatives financial instruments (interest rate swaps)										
Floating rate interest receivable	(5,707)	-	-	-	-	-	-	-	-	(5,707)
Floating rate interest payable	5,197	40	154	105	84	21	60	46	-	5,707
Total derivatives	(510)	40	154	105	84	21	60	46	-	-
Interest sensitivity gap	948	-	-	-	-	-	-	-	(948)	-
Cumulative interest sensitivity gap	948	948	948	948	948	948	948	948	-	-

The impact on net interest income over a twelve month period of a 100 basis point ("bp") downward/upward movement in interest rates on 31 December 2015 would be circa -€2,034k/ €2,951k respectively.

*Forms an integral part of the audited financial statements.

RISK MANAGEMENT REPORT (CONTINUED)

3.6 Non-trading interest rate risk* (continued)

Interest Rate Sensitivity* ***(continued)***

Interest Rate Sensitivity analysis for the Bank at 31 December 2014 is as follows:

	0≤1mth	1≤3mths	3≤12mths	1≤2yrs	2≤3yrs	3≤4yrs	4≤5yrs	5yrs+	Rate Insensitive	Total
Assets	€ m	€ m	€ m	€ m	€ m	€ m	€ m	€ m	€ m	€ m
Loans and receivables to customers	5,586	17	92	133	61	21	20	29	(336)	5,623
Loans and receivables to banks	77	-	-	-	-	-	-	-	-	77
Derivatives and other financial instruments	-	-	-	-	-	-	-	-	22	22
Other assets	-	-	-	-	-	-	-	-	10	10
Total Assets	5,663	17	92	133	61	21	20	29	(304)	5,732
Liabilities										
Deposits by banks	3,383	-	-	-	-	-	-	-	-	3,383
Derivatives and other financial instruments	-	-	-	-	-	-	-	-	22	22
Debt issued	1,807	-	-	-	-	-	-	-	-	1,807
Other liabilities	-	-	-	-	-	-	-	-	1	1
Shareholders' equity	-	-	-	-	-	-	-	-	519	519
Total Liabilities	5,190	-	-	-	-	-	-	-	542	5,732
Derivatives financial instruments (interest rate swaps)										
Floating rate interest receivable	(6,139)	-	-	-	-	-	-	-	-	(6,139)
Floating rate interest payable	5,766	17	92	133	61	21	20	29	-	6,139
Total derivatives	(373)	17	92	133	61	21	20	29	-	-
Interest sensitivity gap	846	-	-	-	-	-	-	-	(846)	-
Cumulative interest sensitivity gap	846	846	846	846	846	846	846	846	-	-

The impact on net interest income over a twelve month period of a 100 basis point ("bp") downward/upward movement in interest rates on 31 December 2014 would be circa €2,279k/ €1,512k respectively

*Forms an integral part of the audited financial statements

DIRECTORS' RESPONSIBILITY STATEMENT

The Directors' are responsible for preparing the Directors' report and annual financial statements in accordance with applicable Irish law and regulations.

Irish company law requires the Directors to prepare financial statements for each financial year. Under the law, the Directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards ("IFRS"). Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the assets, liabilities and financial position of the Bank as at the financial year end date and of the profit or loss of the Bank for the financial year and otherwise comply with the Companies Act 2014.

In preparing these financial statements, the Directors are required to:

- select suitable accounting policies for the Company financial statements and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether the financial statements have been prepared in accordance with applicable accounting standards, identify those standards, and note the effect and the reasons for any material departure from those standards; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Directors are responsible for ensuring that the Bank keeps or causes to be kept adequate accounting records which correctly explain and record the transactions of the Bank, enable at any time the assets, liabilities, financial position and profit or loss of the Bank to be determined with reasonable accuracy, enable them to ensure that the financial statements and Directors' Report comply with the Companies Act 2014 and enable the financial statements to be audited. They are also responsible for safeguarding the assets of the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

On behalf of the Board

Denis Holland
Chairman

Owen Purcell
Managing Director

Date: 18 March 2016

Deloitte.

Deloitte
Chartered Accountants &
Statutory Audit Firm

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF EBS MORTGAGE FINANCE

We have audited the financial statements of EBS Mortgage Finance (the "Bank") for the financial year ended 31 December 2015 which comprise the Income Statement, the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Cash Flows, the Statement of Changes in Shareholders' Equity and the related notes. The relevant financial reporting framework that has been applied in their preparation is the Companies Act 2014 and International Financial Reporting Standards (IFRS) as adopted by the European Union ("relevant financial reporting framework").

This report is made solely to the Bank's members, as a body, in accordance with Section 391 of the Companies Act 2014. Our audit work has been undertaken so that we might state to the Bank's members those matters we are required to state to them in an 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 Bank and the Bank'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 Directors' Responsibility Statement, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view and otherwise comply with the Companies Act 2014. Our responsibility is to audit and express an opinion on the financial statements in accordance with the Companies Act 2014 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 Bank'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 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 financial statements:

- give a true and fair view of the assets, liabilities and financial position of the Bank as at 31 December 2015 and of the profit for the financial year then ended; and
- have been properly prepared in accordance with the relevant financial reporting framework and, in particular, with the requirements of the Companies Act 2014.

Continued on next page/

Deloitte.

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INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF EBS MORTGAGE FINANCE

Matters on which we are required to report by the Companies Act 2014

- We have obtained all the information and explanations which we consider necessary for the purposes of our audit.
- In our opinion the accounting records of the Bank were sufficient to permit the financial statements to be readily and properly audited.
- The financial statements are in agreement with the accounting records.
- In our opinion the information given in the Directors' report is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the provisions in the Companies Act 2014 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
Chartered Accountants and Statutory Audit Firm
Dublin

Date 18 March 2016

INCOME STATEMENT

For the financial year ended 31 December 2015

	Note	2015 €m	2014 €m
Interest income and similar income	3	231	274
Interest expense and similar charges	4	(69)	(135)
Net Interest Income		162	139
Net trading gain	5	3	2
Other operating expense	6	(9)	-
Total Operating Income		156	141
Administrative expenses	7	(44)	(8)
Impairment of intangible assets	13	-	(2)
Operating profit before impairment losses and taxation		112	131
Writeback/ (Provisions) for impairment of loans and advances to customers	8	10	(22)
Operating profit before taxation		122	109
Income tax charge	9	(15)	(14)
Profit for the financial year		107	95

The operating profit arises from continuing operations.

The notes on pages 44 to 72 are an integral part of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME

For the financial year ended 31 December 2015

	Note	2015 €m	2014 €m
Profit for the financial year		**107**	95
Total comprehensive income for the financial year		**107**	95

The notes on pages 44 to 72 are an integral part of these financial statements.

STATEMENT OF FINANCIAL POSITION

As at 31 December 2015

	Note	2015 €m	2014 €m
Assets			
Derivative financial instruments	10	20	22
Loans and receivables to banks	11	60	77
Loans and receivables to customers	12	5,265	5,623
Deferred taxation	14	-	9
Asset held for sale	15	2	-
Total assets		5,347	5,731
Liabilities			
Deposits by banks	16	2,271	3,383
Derivative financial instruments	10	20	22
Debt securities in issue	17	2,387	1,807
Current taxation	9	7	-
Accruals and deferred income		1	-
Provisions for liabilities and commitments	18	35	-
Total liabilities		4,721	5,212
Shareholders' equity			
Issued share capital presented as equity	19	552	552
Revenue reserves		74	(33)
Shareholders' equity		626	519
Total liabilities and shareholders' equity		5,347	5,731

The notes on pages 44 to 72 are an integral part of these financial statements

Denis Holland
Chairman

Owen Purcell
Managing Director

Gerry Gaffney
Executive Director

Catherine Kelly
Secretary

Date: 18 March 2016

STATEMENT OF CASH FLOWS

For the financial year ended 31 December 2015

	Note	2015 €m	2014 €m
Cash flows from operating activities			
Operating profit before taxation		**122**	109
Amortisation of FV discount on debt securities in issue	**4**	**30**	63
Gain on repurchase of debt securities in issue		**9**	-
Provisions (release)/ charge for impairment on loans and receivables	**8**	**(10)**	22
Impairment of intangibles	**13**	**-**	2
Fair value movement on hedging derivatives		**-**	-
		151	196
Changes in operating assets and liabilities			
Change in loans and receivables to customers		**367**	338
Change in accruals and deferred income		**-**	-
Change in deposits by banks		**(1,112)**	405
Change in debt securities in issue		**-**	-
Change in accrual and deferred income		**1**	-
Change in provision for liability and commitments		**35**	-
Redemption/ (issue) of debt securities		**541**	(950)
Change in other assets		**(2)**	-
Change in other liabilities		**2**	(1)
Net cash flows from operations before taxation		**(17)**	(12)
Taxation refund/ (charge)		**-**	-
Net cash flows from operations		**(17)**	(12)
Net cash flow from investing activities		**-**	-
Cash flows from financing activities			
Proceeds from issue of ordinary share capital		**-**	-
Net cash flows from financing activities		**-**	-
Net decrease in cash and cash equivalents		**(17)**	(12)
Cash and cash equivalents at 1 January		**77**	89
Cash and cash equivalents at 31 December	**21**	**60**	77

The notes on pages 44 to 72 are an integral part of these financial statements.

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

At 31 December 2015

	Ordinary Share Capital €m	Revenue Reserves €m	Total Shareholders' Equity €m
At 1 January 2015	**552**	**(33)**	**519**
Total comprehensive income for the period	**-**	**107**	**107**
At 31 December 2015	**552**	**74**	**626**
At 1 January 2014	552	(128)	424
Total comprehensive income for the period	-	95	95
At 31 December 2014	552	(33)	519

NOTES TO THE FINANCIAL STATEMENTS

NOTES TO THE FINANCIAL STATEMENTS (continued)

1. ACCOUNTING POLICIES INDEX

NOTES TO THE FINANCIAL STATEMENTS (continued)

1. ACCOUNTING POLICIES

The accounting policies applied in the preparation of the financial statements for the financial year ended 31 December 2015 are set out below.

1.1. Reporting entity

EBS Mortgage Finance (the 'Bank') is a public unlimited company and commenced trading on 1 December 2008 operating under the Irish Central Bank Act, 1971 (as amended) and is a designated mortgage credit institution under the Asset Covered Securities Acts 2001 and 2007. The Bank is a wholly owned subsidiary of EBS Limited, is part of the EBS (the 'Group') and AIB Group ("AIB Group") and is regulated by the SSM.

The Bank 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. The Bank is not a participating institution under the new Credit Institutions (Eligible Liabilities Guarantee) Scheme 2009 which came into effect on 9 December 2009.

The Bank is currently a participating institution under the National Asset Management Agency Act 2009. However, there were no mortgage loans transferred under the Act.

1.2. Statement of compliance

The financial statements have been prepared in accordance with International Accounting Standards and International Financial Reporting Standards (collectively "IFRSs") 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 financial year ended 31 December 2015. The accounting policies have been consistently applied by the Bank and are consistent with the previous year, unless otherwise described. The financial statements also comply with the Companies Act 2014 applicable to companies reporting under IFRS and the European Communities (Credit Institutions: Financial Statements) Regulations, 2015 (as amended) and the Asset Covered Securities Acts 2001 and 2007.

1.3. Basis of preparation

Functional and presentation currency

The financial statements are presented in Euro, which is the functional currency of the Bank, rounded to the nearest million.

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, and certain hedged financial assets and financial liabilities.

The financial statements comprise the income statement, the statement of comprehensive income, the statement of financial position, the statement of cash flows, and the 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 section of the 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, 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 periods affected. The estimates that have 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 and determination of the fair value of certain financial assets and liabilities and provisions for liabilities and commitments. 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. A description of these estimates and judgements is set out in note 2 of the financial statements.

Going concern

The financial statements for the financial year ended 31 December 2015 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. The period of assessment used by the Directors is twelve months from the date of approval of these annual financial statements.

EBS Mortgage Finance is dependent on its ultimate parent, Allied Irish Banks, p.l.c. for continued funding and is therefore dependent on the going concern status of the ultimate parent.

The financial statements of Allied Irish Banks, p.l.c for the financial year ended 31 December 2015 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 period of assessment. The period of assessment used by the Directors of AIB Group is twelve months from the date of approval of its annual financial statements.

In making its assessment, the Directors of AIB Group have considered a wide range of information relating to present and future conditions. These have included financial plans approved by the Board of AIB Group in December 2015 covering the period 2016 to 2018, the Restructuring Plan approved by the European Commission in May 2014, liquidity and funding forecasts, and capital resources projections, all of which have been prepared under base and stress scenarios. In formulating these plans, the current Irish economic environment and forecasts for growth and employment were considered as well as the stabilisation of property prices. The Directors of AIB Group have considered the outlook for the Irish, the eurozone and UK economies and the factors and uncertainties impacting their performance.

NOTES TO THE FINANCIAL STATEMENTS (continued)

1. ACCOUNTING POLICIES (continued)

1.3. Basis of preparation (continued)

***Going concern* (continued)**

The Directors of AIB Group have also considered the principal risks and uncertainties which could materially affect the Group's future business performance and profitability.

The Directors of AIB Group 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 of AIB Group are satisfied, based on AIB's position in the market place, that in all reasonable circumstances required liquidity and funding from the Central Bank of Ireland/ECB would be available to the Group during the period of assessment.

On the basis of the above, the Directors of AIB Group 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 Groups ability to continue as a going concern over the period of assessment.

Conclusion

On the basis of the continued availability of funding from Allied Irish Banks, p.l.c to EBS Mortgage Finance, the Directors of the Bank 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 its ability to continue as a going concern over the period of assessment.

Adoption of new accounting standards

During the year to 31 December 2015, the Group adopted amendments to standards and interpretations which had an insignificant impact on these financial statements.

1.4. 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 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 receivable and expense payable on the instrument evenly in proportion to the amount outstanding over the period to maturity or repayment.

In calculating the effective interest rate, the Bank 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 any expected 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.

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;
- 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.

1.5. Net trading income

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

1.6. Financial assets

Loans and receivables

Loans and receivables 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 EBSMF acquires loans or receivables with no intention of trading the loan. Loans and receivables are initially recognised at fair value adjusted for direct and incremental transaction costs and are subsequently carried on an amortised cost basis.

NOTES TO THE FINANCIAL STATEMENTS (continued)

ACCOUNTING POLICIES (continued)

1.7. Financial liabilities
Issued financial instruments and their components are classified as liabilities where the substance of the contractual arrangement results in the Bank having a present obligation to either deliver cash or another financial asset to the holder or 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 the 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 is recognised in the income statement using the effective interest rate method.

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

1.8. Derivatives and hedge accounting
Derivatives, such as interest rate swaps are used for risk management purposes.

Derivatives
Derivatives are measured initially at fair value on the date on which the derivative contract is entered into and subsequently remeasured 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.

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 Bank designates certain derivatives as hedges of the fair value of recognised assets or liabilities or firm commitments ('fair value hedge').

When a financial instrument is designated as a hedge, the Bank 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 Bank 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.

The Bank discontinues hedge accounting when:
- it is determined that a derivative is not, or has ceased to be, highly effective as a hedge;
- the derivative expires, or is sold, terminated, or exercised;
- the hedged item matures or is sold or repaid.

To the extent that the changes in the fair value of the hedging derivative differ from changes in 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 Bank 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 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.

Derivatives used to manage interest rate risk arising on mortgage covered securities have been designated as fair value hedges.

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 these derivative instruments are recognised immediately in the income statement.

Derivatives used to manage interest rate risk arising on mortgage loans to customers do not qualify for hedge accounting. Changes in their fair value are recognised immediately in the income statement.

NOTES TO THE FINANCIAL STATEMENTS (continued)

ACCOUNTING POLICIES (continued)

1.9. 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 EBSMF, 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 7 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.

1.10. Impairment of financial assets

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

Impairment

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or a portfolio of financial assets is impaired. A financial asset or portfolio of financial assets is 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 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, is impaired includes observable data that comes to the attention of the Bank 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 Bank 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 Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant (i.e. individually insignificant). If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and includes these performing assets under the collective incurred but not reported ('IBNR') assessment.

An IBNR 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 IBNR), 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 cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and 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 assumption used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

NOTES TO THE FINANCIAL STATEMENTS (continued)

ACCOUNTING POLICIES (continued)

1.10. Impairment of financial assets (continued)

Impairment loss
For loans and receivables, 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. 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. The Group 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.

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 the 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.

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

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 when that customer 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. 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 3.1. A request for a forbearance solution acts as a trigger for an impairment test.

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 mortgage loans, 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 restructuring of the loan in accordance with new agreed terms, comprising typically, a period of twelve months of consecutive payments of full principal and interest and, the upgrade would initially be to Watch/Vulnerable grades. Where upgraded out of impaired, loans are included in the Group's collective assessment for IBNR provisions.

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 in the Income Statement. Interest accrues on the new loan based on the current market rates in place at the time of renegotiation.

Where a loan has been subject to an impairment provision and the renegotiation leads to a customer granting equity to the Group 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

ACCOUNTING POLICIES (continued)

1.10. Impairment of financial assets (continued)

Non-forbearance renegotiation

Occasionally, the Bank may temporarily amend the contractual repayments terms 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 paragraph 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.

However, 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 or IBNR assessment purposes.

1.11. 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.

1.12. Income tax, including deferred tax

Income tax comprises 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 financial 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 deferred tax asset is reviewed at the end of each reporting period and the carrying amount is reduced to the extent that sufficient taxable profits will be available to allow the asset to be recovered.

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 the revaluation of certain financial assets and financial liabilities including derivative contracts.

1.13. Cash and cash equivalents

For the purposes of the cash flow statements, cash comprises cash on hand and demand deposits and cash equivalents comprise 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.

1.14. Shareholder's 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 Bank. Incremental costs directly attributable to the issue of an equity instrument are deducted from the initial measurement of the equity instrument.

Share capital

Share capital represents funds raised by issuing shares in return for cash or other consideration. Share capital comprises ordinary shares.

Dividends and distributions

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

1. ACCOUNTING POLICIES (continued)

1.14. Shareholder's Equity (continued)

Revenue reserves
Revenue reserves represent retained earnings of the Bank.

1.15 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 are used where those prices are considered to represent actual and regularly occurring market transactions for financial instruments 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, and 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, equity and commodity prices, credit spreads, option volatilities and currency rates. In addition, the Group considers the impact of own credit risk and counterparty risk when valuing its derivative liabilities.

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

1. ACCOUNTING POLICIES (continued)

1.15. Determination of fair value of financial instruments (continued)

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 price 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 the assumptions market participants would use when fair valuing the financial instrument.

The Group tests the outputs of the valuation 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 and 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.

1.16. Foreign currency translation

Items included in the financial statements of EBSMF 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 re-translated at the rate prevailing at the period end. Foreign exchange gains and losses resulting from the settlement of such transactions and from the re-translation at period end exchange rates of the amortised cost of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

1.17. Asset held for sale

An asset is classified as held for sale if it is expected that its carrying amount will be recovered principally through sale rather than through continuing use, it is available for immediate sale and sale is highly probable within one year. For the sale to be highly probable, the appropriate level of management must be committed to a plan to sell the asset.

On initial classification as held for sale, generally, assets are measured at the lower of previous carrying amount and fair value less costs to sell with any adjustments taken to the income statement. The same applies to gains and losses on subsequent re-measurement. Financial assets within the scope of IAS 39 continue to be measured in accordance with that standard.

Impairment losses subsequent to classification of assets as held for sale are recognised in the income statement. Subsequent increases in fair value less costs to sell of assets that have been classified as held for sale are recognised in the income statement to the extent that the increase is not in excess of any cumulative impairment loss previously recognised in respect of the asset. Assets classified as held for sale are not depreciated.

Gains and losses on re-measurement and impairment losses subsequent to classification as assets held for sale are shown within continuing operations in the income statement.

Assets held for sale are presented separately on the statement of financial position. Prior periods are not reclassified.

1.18. Prospective accounting changes

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

(a) Amendments to IAS 1 Presentation of Financial Statements: Disclosure Initiative

<u>Nature of Change</u>

The amendments to IAS 1 are designed to further encourage companies to apply professional judgement in determining what information to disclose in the financial statements. Furthermore, the amendments clarify that companies should use professional judgement in determining where and in what order information is presented in the financial disclosures.

These amendments are not expected to have a significant impact on the Bank.

<u>IASB Effective Date</u>

Annual periods beginning on or after 1 January 2016.

NOTES TO THE FINANCIAL STATEMENTS (continued)

ACCOUNTING POLICIES (continued)

1.18. Prospective accounting changes (continued)

(b) Annual improvements to IFRSs 2012–2014 cycle

Nature of Change
The IASB's annual improvements project provides a process for making amendments to IFRSs that are considered non-urgent but necessary. The amendments clarify guidance and wording, or correct for relatively minor unintended consequences, conflicts or oversights in existing IFRSs. Annual Improvements to IFRSs 2012-2014 Cycle amend IFRSs in relation to four issues addressed during this cycle.

None of the amendments are expected to have a significant impact on reported results or disclosures.

IASB Effective Date
Annual periods beginning on or after 1 January 2016.

(c) IFRS 15 Revenue from Contracts with Customers

Nature of Change
IFRS 15, which was issued in May 2014, replaces IAS 11 *Construction Contracts* and IAS 18 *Revenue* in addition to IFRIC 13, IFRIC 15, IFRIC 18 and SIC-31. IFRS 15 specifies how and when an entity recognises revenue from a contract with a customer through the application of a single, principles based five-step model. The standard specifies new qualitative and quantitative disclosure requirements to enable users of financial statements understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

The impacts of this standard are being considered by the Bank.

This standard is subject to EU endorsement.

IASB Effective Date
Annual periods beginning on or after 1 January 2018.

(d) IFRS 9 Financial Instruments

Nature of Change
IFRS 9 Financial Instruments was issued in July 2014 and will replace IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 includes a revised classification and measurement model, a forward looking 'expected credit loss' impairment methodology and modifies the approach to hedge accounting. Unless early adopted, the standard is effective for accounting periods beginning 1 January 2018. The key changes under the standard are:

Classification and measurement
Financial assets are classified on the basis of the business model within which they are held and their contractual cashflow characteristics. The classification and measurement categories are amortised cost, fair value through other comprehensive income and fair value through profit and loss.

A financial asset is measured at amortised cost if two criteria are met: a) the objective of the business model is to hold the financial asset for the collection of the contractual cash flows, and b) the contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest.

If a financial asset is eligible for amortised cost measurement, an entity can elect to measure it at fair value if it eliminates or significantly reduces an accounting mismatch.

Interest is calculated on the gross carrying amount of a financial assets, except where the asset is credit impaired in which case interest is calculated on the carrying amount after deducting the impairment provision.

There is no separation of an embedded derivative where the instrument is a financial asset.

Equity instruments must be measured at fair value, however, an entity can elect on initial recognition to present fair value changes, including any related foreign exchange component on non-trading equity investments directly in other comprehensive income. There is no subsequent recycling of fair value gains and losses to profit or loss; however dividends from such investments will continue to be recognised in profit or loss.

Impairment
Requires more timely recognition of expected credit losses using a three stage approach. For financial assets where there has been no significant increase in credit risk since origination, a provision for 12 months expected credit losses is required. For financial assets where there has been a significant increase in credit risk or where the asset is credit impaired, a provision for full lifetime expected losses is required.

The assessment of whether credit risk has increased significantly since origination is performed for each reporting period by considering the change in risk of default occurring over the remaining life of the financial instrument, rather than by considering an increase in expected credit loss.

NOTES TO THE FINANCIAL STATEMENTS (continued)

ACCOUNTING POLICIES (continued)

1.18. Prospective accounting changes (continued)

(d) IFRS 9 Financial Instruments (continued)

Impairment (continued)
The assessment of credit risk, and the estimation of expected credit loss, are required to be unbiased and probability-weighted, and should incorporate all available information which is relevant to the assessment, including information about past events, current conditions and reasonable and supportable forecasts of future events and economic conditions at the reporting date. In addition, the estimation of expected credit loss should take into account the time value of money. As a result, the recognition and measurement of impairment is more forward-looking than under IAS 39 and the resulting impairment charge will tend to be more volatile. It will also tend to result in an increase in the total level of impairment allowances, since all financial assets will be assessed for at least 12-month expected credit loss and the population of financial assets to which lifetime expected credit loss applies is likely to be larger than the population for which there is objective evidence of impairment in accordance with IAS 39.

Financial liabilities
The classification of financial liabilities is essentially unchanged, except that, for certain liabilities measured at fair value, gains or losses relating to changes in the entity's own credit risk are to be included in other comprehensive income;

Hedge accounting
The general hedge accounting requirements aim to simplify hedge accounting, creating a stronger link with risk management strategy and permitting hedge accounting to be applied to a greater variety of hedging instruments and risks. The standard does not explicitly address macro hedge accounting strategies, which are being considered in a separate project. To remove the risk of any conflict between existing macro hedge accounting practice and the new general hedge requirements, IFRS 9 includes an accounting policy choice to remain with IAS 39 hedge accounting.

Transition
A Group-wide Programme, led jointly by Risk and Finance, commenced work during 2015 to oversee delivery of the requirements for implementation of IFRS 9.
The governance structure includes a Steering Committee mandated to oversee implementation in accordance with the standard, a Technical Approval Group to approve key accounting policy change decisions and an Operating Model Design Authority to approve operating model specifications.

Detailed planning was completed during 2015 and the Design Phase commenced thereafter, with a number of key decisions required over the course of the first few months in 2016. The Programme is structured with various work streams responsible for designing and implementing the end state target operating model, technical accounting interpretations, building and validating IFRS 9 provision models and assessing data and systems requirements.

Classification and measurement of financial assets is not expected to result in any significant changes for the Group. Given that the Group does not fair value its own debt, there is no impact as a result of changes required under IFRS 9. However, due to the complexity of decisions required in relation to impairment, it is not possible at this stage to quantify the potential impact.

This standard is subject to EU endorsement.

IASB Effective Date
Annual periods beginning on or after 1 January 2018

(e) Amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses

The amendments in *Recognition of Deferred Tax Assets for Unrealised Losses, which were issued in January 2016,* clarify the following aspects:
- Unrealised losses on debt instruments measured at fair value and measured at cost for tax purposes give rise to a deductible temporary difference regardless of whether the debt instrument's holder expects to recover the carrying amount of the debt instrument by sale or by use;
- The carrying amount of an asset does not limit the estimation of probable future taxable profits;
- Estimates for future taxable profits exclude tax deductions resulting from the reversal of deductible temporary differences; and
- An entity assesses a deferred tax asset in combination with other deferred tax assets. Where tax law restricts the utilisation of tax losses, an entity would assess a deferred tax asset in combination with other deferred tax assets of the same type.

These amendments are not expected to have a significant impact on the Bank.

The amendments are subject to EU endorsement.

IASB Effective Date
Annual periods beginning on or after 1 January 2017

NOTES TO THE FINANCIAL STATEMENTS (continued)

1.18. Prospective accounting changes (continued)

(f) IFRS 16 Leases

IFRS 16, which was issued in January 2016, replaces IAS 17 Leases. The new standard brings most leases on-balance sheet for lessees under a single model, eliminating the distinction between operating and finance leases. Under IFRS 16 a lessee recognises a right-of-use asset and a lease liability. The right-of-use asset is treated similarly to other non-financial assets and depreciated accordingly. The lease liability is initially measured at the present value of the lease payments payable over the lease term, discounted at the rate implicit in the lease if that can be readily determined. If that rate cannot be readily determined, the lessee shall use their incremental borrowing rate.

Lessor accounting remains largely unchanged and the distinction between operating and finance leases is retained.

These amendments will impact the Bank although the impact has not been identified. The impact will be evaluated in due course.

This standard is subject to EU endorsement.

IASB Effective Date
Annual periods beginning on or after 1 January 2019

(g) Amendments to IAS 7 – *Statement of Cash Flows*

The amendments to IAS 7 *Statement of Cash Flows,* which were issued in January 2016, require that the following changes in liabilities arising from financing activities be disclosed to the extent necessary:

- Changes from financing cash flows;
- Changes arising from obtaining or losing control of subsidiaries or other businesses;
- The effect of changes in foreign exchange rates;
- Other changes

It also stresses that the new disclosure requirements also relate to changes in financial assets if they meet the definition. These amendments are not expected to have a significant impact on the Bank.

The amendments are subject to EU endorsement.

IASB Effective Date
Annual periods beginning on or after 1 January 2017.

2. CRITICAL ACCOUNTING JUDGEMENTS AND ESTIMATES

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 judgement involves making estimates concerning the likelihood of future events, the actual results could differ from those estimates.
The accounting policies that are deemed critical to EBS Mortgage Finance's results and financial position, in terms of the materiality of the items to which the policy is applied and the estimates that have a significant impact on the financial statements are set out in this section. In addition, estimates with a significant risk of material adjustment in the next year are also discussed.

(a) Going concern
The financial statements for the financial year ended 31 December 2015 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 Mortgage Finance is dependent on its ultimate parent, Allied Irish Banks, p.l.c. for continued funding and is therefore dependent on the going concern status of the ultimate parent Bank is dependent on its parent, Allied Irish Banks, p.l.c. for continued funding and is therefore dependent on the going concern status of the parent.

The financial statements of Allied Irish Banks, p.l.c for the financial year ended 31 December 2015 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 period of assessment.

In making its assessment, the Directors of AIB Group have considered a wide range of information relating to present and future conditions. These have included financial plans approved by the Board of AIB Group in December 2015 covering the period 2016 to 2018, the Restructuring Plan approved by the European Commission in May 2014, liquidity and funding forecasts, and capital resources projections. These have all been prepared under base and stress scenarios having considered the outlook for the Irish, the eurozone and UK economies. In addition, the Directors of AIB Group have considered the commitment of support provided by the Irish Government.

On the basis of the continued availability of funding from Allied Irish Banks, p.l.c to EBS Mortgage Finance, the Directors of the Bank 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 its ability to continue as a going concern over the period of assessment

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. CRITICAL ACCOUNTING JUDGEMENTS AND ESTIMATES (continued)

(b) Loan impairment

The Banks' accounting policy for impairment of financial assets is set out in accounting policy number 1.10. The provisions for impairment on loans and receivables at 31 December 2015 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 economic climate, conditions in various industries to which the borrowers are 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 AIB Group credit and risk management. The Bank assesses and approves its provisions on a quarterly basis. A quarterly assessment of provision adequacy is also considered by AIB Group Credit Committee, prior to AIB Group Audit Committee and Board approval being sought.

After a period of time when it is concluded that there is no real prospect of recovery of loans/part of loans which have been subjected to a specific provision, the Bank writes off that amount of the loan deemed irrecoverable against the specific provision held against the loan.

Specific provision

A specific provision is made against an impaired loan when, in the judgement of management, the estimated realisable value, including available security, is expected to fall short of the principal and interest amount outstanding on the loan. A specific provision is set aside based on the estimate of the difference between the present value of future cash flows, and the assets' carrying value.

As the amount of specific provision required is primarily model driven, and based on estimates of the timing and amount of future cash flows, the amount of the Bank's provision is somewhat uncertain, and may not fully reflect the impact of the prevailing market conditions. Underlying assumptions are reviewed and updated on a regular basis. For further details please refer to: 'Impact of changes to key assumptions and estimates on the impairment provisions' on pages 15 and 16 of the Risk management section of this report.

Incurred but not reported provisions

Incurred but not reported ("IBNR") provisions are maintained to cover impaired loans which are known to be present within the portfolio, but have not been specifically identified as impaired at the reporting date. IBNR provisions are maintained at levels that are deemed appropriate following management assessment of a wide range of credit, portfolio, sectorial, and other economic factors.

The total amount of impairment loss in the Bank's non-impaired portfolio, and therefore the adequacy of the IBNR provision is inherently uncertain. Key assumptions underpinning the Bank's estimates of collective and IBNR provisions are regularly reviewed in line with experience. For further details please refer to: 'Impact of changes to key assumptions and estimates on the impairment provisions' on pages 15 and 16 of the Risk management section of this report.

Forbearance

The Bank has developed a number of forbearance strategies to assist customers experiencing financial difficulties, which involve modifications to contractual repayment terms, in order to improve the recoverability of outstanding debt. Advanced forbearance strategies currently being implemented are subject to high levels of judgement and estimation, which may impact on loan impairment provisions. Further information on forbearance strategies is set out in the 'Risk management' section of this report.

(c) Fair value of financial instruments

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 and contingent capital instruments, the income statement.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. CRITICAL ACCOUNTING JUDGEMENTS AND ESTIMATES* (continued)

(d) Provisions for liabilities and commitments

EBSMF's accounting policy for provisions for liabilities and commitments is set out in accounting policy number 1.11 'Non-credit risk provisions' in Note 1.

EBSMF recognises liabilities where it has present legal or constructive obligations as a result of past events and it is more likely than not that these obligations will result in an outflow of resources to settle the obligations and the amount can be reliably estimated. Details of the Bank's liabilities and commitments are shown in Note 18 to the financial statements.

The recognition and measurement of liabilities, in certain instances, may involve a high degree of uncertainty, and thereby, considerable time is expended on research in establishing the facts, scenario testing, assessing the probability of the outflow of resources and estimating the amount of any loss. This process will, of its nature, require significant management judgement and will require revisions to earlier judgements and estimates as matters progress towards resolution. However, at the earlier stages of provisioning, the amount provided for can be very sensitive to the assumptions used and there may be a wide range of possible outcomes in particular cases. Accordingly, in such cases, it is often not practicable to quantify a range of possible outcomes. In addition, it is also not practicable to measure ranges of outcomes in aggregate in a meaningful way because of the diverse nature of these provisions and the differing fact patterns.

In this regard, the Central Bank of Ireland ('CBI') in December 2015, requested the Irish Banking industry, including EBSMF, to conduct a broad examination of tracker mortgage related issues, comprising of a review of mortgage loan books (including both Owner Occupied and Buy-to-Let properties and loans that have been redeemed and/or sold), to assess compliance with both contractual and regulatory requirements. These regulatory requirements require the Bank to demonstrate that the customers' interest are protected, that customers are being treated fairly, and in the context of customers' understanding with regard to their entitlement to a tracker rate, to consider information provided and the disclosures made to such customers over time. In situations where customer detriment is identified from this examination, EBSMF is required to provide appropriate redress and compensation in line with the CBI 'Principles for Redress'. The CBI has also indicated that any tax liability that impacted customers may incur, in respect of redress, compensation or other payment by the lender, is to be discharged by the lender. This examination is required to cover the period of time from when EBSMF, commenced offering tracker interest rates to 31 December 2015.

AIB Group has instigated a project which is on-going to identify all mortgage loans where customer detriment may have occurred and to determine appropriate redress and compensation in such cases. The recognition of provisions for customer redress and related matters which are included in 'provisions for liabilities and commitments' requires significant levels of judgement and estimation in such cases. The project involves determining the population potentially subject to redress, reviewing the relevant contractual documentation, determining changes that have occurred in the interest rates and computing the financial impact and related accounting of such redress.

At 31 December 2015, EBSMF has provided €21 million where either the interest rates are not in accordance with the relevant contractual documentation or where the Bank will offer revised terms on mortgage accounts. This mainly relates to the refund of interest (difference in interest charged to customers compared to the interest that would have been charged when the tracker rate is applied). The provision also includes amounts for compensating customers, such as reimbursement for the time value of money and other compensation amounts.

Furthermore, EBSMF has recognised a provision of €14 million for (a) the accounting impact of a constructive obligation under IAS 37 for fair value remeasurement losses that will be recognised in areas where the Bank will offer revised terms on mortgage accounts; (b) tax liabilities arising from redress or other compensation which the Bank may be required to discharge on behalf of impacted customers; and (c) other costs associated with the examination.

Validation of the final number of impacted accounts is subject to independent third party assurance and also subject to assessment and challenge by the CBI.

Given the uncertainty attaching to certain of the assumptions and judgements underpinning the above provisions, it is possible that the eventual outcome may differ from the current estimates with a resultant charge/credit to the income statement in future periods.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. INTEREST INCOME AND SIMILAR INCOME

	2015 € m	2014 € m
Interest on loans and receivables to customers	**187**	230
Amortisation of fair value discount on loans and receivables to customers	**44**	44
	231	274

Included within various captions under interest income for the financial year ended 31 December 2015 is a total of €29m (2014: €40m) accrued on impaired financial assets.

4. INTEREST EXPENSE AND SIMILAR CHARGES

	2015 € m	2014 € m
Interest payable to credit institutions	**21**	26
Interest on debt securities in issue	**18**	46
Amortisation of fair value discount on debt securities in issue	**30**	63
	69	135

5. NET TRADING GAIN

	2015 € m	2014 € m
Debt Securities and interest rate contracts	**3**	2
	3	2

6. OTHER OPERATING EXPENSE

	2015 € m	2014 € m
Loss on repurchase of debt securities in issue	**9**	
	9	-

7. ADMINISTRATIVE EXPENSES

	2015 € m	2014 € m
Personnel expenses	**-**	-
Other administrative expenses	**39**	2
Amounts payable to EBS	**5**	6
	44	8

Other administrative expenses includes provision for liabilities and commitments of €35m (2014: Nil) that relates to provisions for customer redress (*see note 2 critical accounting judgements and estimates: (d) provisions for liabilities and commitments)*, professional fees €0.5m (2014: €0.6m) and statutory payments (regulatory payments/ levies) €2.1m (2014: €1.2m)

There are no full time equivalents employed by EBS Mortgage Finance in the financial year 2015 (2014: Nil). All EBS Staff moved to AIB contracts at the 1st of January 2014.

Auditors' remuneration (excluding VAT)

	2015 € '000	2014 € '000
Statutory Audit of entity financial statements	**12**	12
Other assurance services	**-**	10
Tax advisory services	**-**	-
Other non-audit services	**-**	-
Total auditors' remuneration	**12**	22

NOTES TO THE FINANCIAL STATEMENTS (continued)

7. ADMINISTRATIVE EXPENSES (continued)

The disclosure of Auditors' fees are in accordance with section 322 of the Companies Act 2014 which mandates fees in particular categories and that fees paid to the EBS Mortgage Finance's Auditor (Deloitte) for services to the Bank only be disclosed in this format. Other assurance services include fees for additional assurance issued by the firm outside of the audit of the statutory financial statements. These fees include assignments where the auditor provides assurance to third parties.

The remuneration of the Independent Non-Executive Directors in office during 2015 is as follows:

	2015	2014
	€ '000	€ '000
Fees	**30**	30
	30	30

Non-Executive Directors' fees includes travel and subsistence expenses incurred in the performance of the duties of their office, which are paid by the Company. The non-executive Director fees are non-pensionable.

8. PROVISIONS FOR IMPAIRMENT OF LOANS AND RECEIVABLES

	2015			2014		
	Specific	**IBNR**	**Total**	Specific	IBNR	Total
	€ m	**€ m**	**€ m**	€ m	€ m	€ m
Balance at start of year	**280**	**56**	**336**	335	46	381
(Release)/charge against income statement	**18**	**(28)**	**(10)**	12	10	22
Amounts written off	**(45)**	**-**	**(45)**	(67)	-	(67)
Balance at end of year	**253**	**28**	**281**	280	56	336

By geographical location and industry sector	**2015**	2014
	€ m	€ m
Republic of Ireland		
Home Mortgages	**281**	336

9. TAXATION

	2015	2014
	€ m	€ m
Current tax charge on income for year	**(7)**	-
Origination of temporary differences	**(8)**	(14)
Total tax charge for the period	**(15)**	(14)

The tax charge (2014: charge) for the financial year is at an effective rate of 12.5%, which is the same as the standard Irish corporation tax rate.

	2015		2014	
	€ m	%	€ m	%
Operating profit before taxation	**122**		109	
Corporation tax charge (12.5%)	**(15)**	**12.5**	(14)	12.5
Effects of:				
Income taxed at higher rates	**-**	**-**	-	-
Tax charge	**(15)**	**12.5**	(14)	12.5

NOTES TO THE FINANCIAL STATEMENTS (continued)

10. DERIVATIVE FINANCIAL INSTRUMENTS

Set out below are details on fair values and derivative information for EBS Mortgage Finance. The Bank interest rate swaps to hedge the interest rate risk. The first type is used to hedge interest rate risk on mortgage loan accounts both within the Cover Assets Pool and outside the Cover Assets Pool, effectively converting interest receivable from a fixed rate basis to a floating rate basis. Although these swaps are considered to be an effective hedge in economic terms, due to their nature, it has not been possible to establish a "Fair Value" hedging relationship under IAS 39 with the mortgage loan accounts and consequently, they are classified as "Held for Trading".

All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative. Allied Irish Banks, p.l.c. is the counterparty to all derivative contracts noted below.

	2015			2014		
	Contract/ Notional Amount € m	**Fair Value Asset € m**	**Fair Value Liability €m**	Contract/ Notional Amount € m	Fair value Asset € m	Fair Value Liability € m
Derivatives classified as trading						
Interest rate swaps	**5,707**	**20**	**20**	6,189	22	22
Total derivatives	**5,707**	**20**	**20**	6,189	22	22

The following table represents the underlying principal and gross replacement costs of the Bank's derivatives as at 31 December 2015 and 31 December 2014.

	Residual Maturity 2015				Residual Maturity 2014			
	Within 1 yr € m	**1 to 5 yrs € m**	**Over 5 yrs € m**	**Total € m**	Within 1 yr € m	1 to 5 yrs € m	Over 5 yrs € m	Total € m
Underlying principal amount								
Interest rate contracts	**-**	**-**	**5,707**	**5,707**	-	-	6,189	6,189
Positive fair value								
Interest rate contracts	**-**	**-**	**20**	**20**	-	-	22	22

11. LOANS AND RECEIVABLES TO BANKS

	2015 € m	2014 € m
Funds placed with EBS Limited		
Analysed by remaining maturity:		
3 months or less	**31**	33
Funds placed with other banks outside AIB Group		
Analysed by remaining maturity:		
3 months or less	**29**	44
	60	77

For the purpose of cash flows the cash and cash equivalents comprise the above. Loans and receivable to banks include balances with original maturities of less than 3 months. The balances held with other banks outside AIB Group represent Cash Substitution Pool Assets. Cash substitution pool assets are an Asset Covered Securities Act concept whereby certain assets can be held as part of the Cover Assets Pool.

NOTES TO THE FINANCIAL STATEMENTS (continued)

12. LOANS AND RECEIVABLES TO CUSTOMERS

	2015 €m	2014 €m
Analysed by remaining maturity:		
Repayable on demand	**960**	1,288
3 months or less	**1**	1
1 year or less but over 3 months	**3**	3
5 years or less but over 1 year	**92**	93
Greater than 5 years	**4,490**	4,574
	5,546	5,959
Provisions for impairment of loans and receivables (Note 8)	**(281)**	(336)
	5,265	5,623

Amounts repayable on demand includes instances where customers have failed to meet specified repayment terms, and are therefore classified as repayable on demand, in accordance with lending conditions.

Loans and receivables to customers comprise EBS Limited originated residential mortgages in the Republic of Ireland.

Interest recognised on impaired loans amounted to €29m (2014: €40m) and is included in the carrying value of loans and receivables to customers. This has been credited to interest income.

By geographic location and sector	2015 €m	2014 €m
Republic of Ireland		
Home mortgages (net of provision)	**5,265**	5,623
	5,265	5,623

13. INTANGIBLE ASSETS

	2015 €m	2014 €m
Computer Software		
Cost		
Balance at 1 January	**3**	3
Additions / Disposals	**-**	-
Balance at 31 December	**3**	3
Amortisation / Impairment		
Balance at 1 January	**(3)**	(1)
Amortisation for period	**-**	-
Impairment for period	**-**	(2)
Balance at 31 December	**(3)**	(3)
Net book value at 31 December	**-**	-

NOTES TO THE FINANCIAL STATEMENTS (continued)

14. DEFERRED TAXATION

	2015	201
	€ m	€ m
At 1 January	9	23
Income statement	(8)	(14)
Adjustment in respect of prior year	(1)	-
At 31 December	-	9

At 31 December 2015 deferred tax assets on tax losses and other temporary differences, net of deferred tax liabilities, totalled Nil (2014: €9m). The tax losses arose in the Irish tax jurisdiction and their utilisation was dependent on the generation of future taxable profits. The deferred tax asset is fully utilised in 2015.

15. ASSETS HELD FOR SALE

	2015	2014
	€ m	€ m
Repossessed assets	**2**	-
	2	-

16. DEPOSITS BY BANKS

	2015	2014
	€ m	€ m
Funds received from EBS Limited	**2,271**	3,383
	2,271	3,383

The facility limit with EBS is €6.0bn and the balance at 31 December 2015 amounted to €2.3bn (2014: €3.4bn). The interest rate is equal to the aggregate of Euribor and an applicable margin as agreed from time to time between the Bank and EBS. The facility can be terminated by either the Bank or EBS in accordance with the terms of the loan agreement. The Bank makes repayments under the facility from time to time without any premium, penalty or break costs.

17. DEBT SECURITIES IN ISSUE

	2015	2014
	€ m	€ m
Mortgage covered securities in issue by remaining maturity:		
3 months or less	**425**	-
1 year or less but over 3 months	**666**	432
5 years or less but over 1 year	**796**	1,375
Greater than 5 years	**500**	-
Carrying value of Debt Securities	**2,387**	1,807
Mortgage covered securities in issue to external investors and internal issuances at nominal value:		
External investors	**-**	-
EBS Limited	**2,400**	1,850
	2,400	1,850

NOTES TO THE FINANCIAL STATEMENTS (continued)

17. DEBT SECURITIES IN ISSUE (continued)

EBS Mortgage Finance is an issuer of mortgage covered securities under the Asset Covered Securities Act 2001, as amended by the Asset Covered Securities Amendment Act, 2007 (the "Act"). The Act requires that mortgage covered securities are secured by assets that are included in a Cover Assets Pool maintained by the issuer and that a register of mortgage covered securities business is kept.

At 31 December 2015, the Cover Assets Pool amounted to €4.27bn (2014: €4.73bn), comprising of €4.24bn (2014: €4.69bn) of mortgage credit assets (mortgage loan accounts) and €0.029bn (2014: €0.044bn) of substitution assets (cash on deposit with suitably rated credit institutions). Section 40 (2) of the Act requires that the following information be disclosed in respect of mortgage credit assets that are recorded in the register of mortgage covered securities business.

(a) Mortgaged properties and principal loan balances outstanding in the Cover Assets Pool

Total Loan Balances

From	To	Total Loan Balances 2015 (1 & 2) € m	Number of Mortgaged Properties 2015	Total Loan Balances 2014 (1 & 2) € m	Number of Mortgaged Properties 2014
€0	€100,000	**540**	**11,650**	566	12,399
€100,000	€200,000	**1,702**	**11,369**	1,801	12,021
€200,000	€500,000	**1,879**	**7,240**	2,167	8,273
Over €500,000		**122**	**173**	153	216
		4,243	**30,432**	4,687	32,909

(1) The total loan balances are categorised by the total loan balance outstanding per mortgaged property, including principal and interest charged to the loan accounts, but excluding interest accrued but not charged to the loan accounts.

(2) There could be one or more loan accounts per mortgaged property. The Cover Assets Pool contains 39,310 loan accounts (2014: 42,972) secured on 30,432 properties (2014: 32,909).

(b) Geographical location of mortgaged properties in the Cover Assets Pool

Geographical Area	Number of Mortgaged Properties 2015		Number of Mortgaged Properties 2014	
Co. Dublin	**10,801**	**35%**	11,798	36%
Outside Dublin	**19,631**	**65%**	21,111	64%
	30,432	**100%**	32,909	100%

(c) Mortgage loan accounts in default in the Cover Assets Pool
As at 31 December 2015, there were 104 mortgage loan accounts (2014: 219) in default in the Cover Assets Pool (in default being defined as impaired mortgage loan accounts).

(d) Mortgage loan accounts in default in the Cover Assets Pool with arrears greater than €1,000
During the year ended 31 December 2015, 2,081 mortgage loan accounts (2014: 3,875) in the Cover Assets Pool had been in default with arrears greater than €1,000. As at 31 December 2015, there were 432 accounts in default in the Cover Assets Pool (2014: 980).

(e) Replacement of non-performing mortgage loan accounts from the Cover Assets Pool
During the year ended 31 December 2015, 340 non-performing mortgage loan accounts (2014: 1,052) were removed in total from the Cover Assets Pool. (For this purpose, non-performing is defined as in arrears by six monthly repayments or more). These loan accounts were not replaced with other assets in 2015 as the Cover Assets Pool continued to meet all regulatory requirements.

(f) Amount of interest in arrears on mortgage loan accounts in the Cover Assets Pool not written off
The total amount of interest in arrears in respect of 1,224 accounts (2014: 2,091) as at 31 December 2015 was €0.7m (2014: €2m).

(g) Total principal and interest payments on mortgage loan accounts
The total amount of repayments (principal and interest) made by customers on mortgage loan accounts in the Cover Assets Pool during the year ended 31 December 2015 was €485m (2014: €520m), of which €336m (2014: €336m) represented repayment of principal and €148m (2014: €185m) represented payment of interest. The repayments of principal include the repayment of mortgage loan accounts by customers closing their existing accounts when opening a new account.

(h) Number and amount of mortgage loans in the Cover Assets Pool secured on commercial property
As at 31 December 2015 there were no loan accounts (2014: Nil) in the Cover Assets Pool that were secured on commercial properties.

NOTES TO THE FINANCIAL STATEMENTS (continued)

18. PROVISIONS FOR LIABILITIES AND COMMITMENTS

	2015 €m	2014 €m
Provision for customer redress	**35**	-
	35[1]	-

Provisions for customer redress
In December 2015, the Central Bank of Ireland ('CBI'), requested the Irish banking industry, including EBSMF, to conduct a broad examination of tracker mortgage related issues, comprising of a review of mortgage loan books (including both Owner Occupied and Buy-to- Let properties and loans that have been redeemed and/or sold), to assess compliance with both contractual and regulatory requirements. In situations where customer detriment is identified from this examination, AIB is required to provide appropriate redress and compensation in line with the CBI 'Principles for Redress'. AIB Group has instigated a project which is on-going to identify all mortgage loans where customer detriment may have occurred and to determine appropriate redress and compensation in such cases.

At 31 December 2015, the Bank has provided €21 million where either the interest rates are not in accordance with the relevant contractual documentation or where the Group will offer revised terms on mortgage accounts. This mainly relates to the refund of interest (difference in interest charged to customers compared to the interest that would have been charged when the tracker rate is applied). The provision also includes amounts for compensating customers, such as reimbursement for the time value of money and other compensation amounts.

Furthermore, the Bank has recognised a provision of €14 million for (a) the accounting impact of a constructive obligation under IAS 37 for fair value remeasurement losses that will be recognised in areas where the Bank will offer revised terms on mortgage accounts; (b) tax liabilities arising from redress or other compensation which the Bank may be required to discharge on behalf of impacted customers; and (c) other costs associated with the examination.

Given that the grounds on which the provisions have been estimated could prejudice the position of the Bank, further information as required by IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* is not disclosed.

[1] The total provisions for liabilities and commitments expected to be settled within one year amount to €35 million (2014: Nil)

19. ISSUED SHARE CAPITAL PRESENTED AS EQUITY

	2015 €m	2014 €m
Authorised:		
1,000,000,000 ordinary shares of €1.00 each	**1,000**	1,000
(2014: 1,000,000,000 ordinary shares of €1.00 each)	**1,000**	1,000
Issued and fully paid up:		
551,540,000 ordinary shares of €1.00 each	**552**	552
(2014: 551,540,000 ordinary shares of €1.00 each)	**552**	552

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 the Bank. All shares rank equally with regard to the Bank's residual assets.

20. CAPITAL MANAGEMENT

Capital regulation
CRD IV consists of the Capital Requirements Regulation ("CRR") and the Capital Requirements Directive ("CRD"), and is designed to strengthen the regulation of the banking sector and to implement the Basel III agreement in the EU legal framework. CRD IV measures include:
– a single set of harmonised prudential rules which enhanced requirements for quality and quantity of capital; and
– CRD IV also harmonises the deductions from own funds in order to determine the amount of regulatory capital that is prudent to recognise for regulatory purposes. Some of the provisions of CRD IV were introduced on a phased basis from 2014, these typically followed 20% in 2014, 40% in 2015 etc. until 2018.

AIB Group commenced reporting to its regulator under the transitional CRD IV rules during 2014. The transitional capital ratios presented on page 6 take account of these phasing arrangements. The fully loaded capital ratios represent the full implementation of CRD IV.

The Single Supervisory Mechanism ("SSM"), comprising the European Central Bank ("ECB") and the national competent authorities of EU countries was established in 2014. The SSM places the ECB as the central prudential supervisor of financial institutions in the Eurozone, including AIB. The aims of the SSM are to ensure the safety and soundness of the EU banking system and to increase financial integration and stability in the EU.

The CET1 transitional ratio is significantly in excess of the SSM's minimum CET1 regulatory requirement (see page 6).

NOTES TO THE FINANCIAL STATEMENTS (continued)

21. STATEMENT OF CASH FLOWS

	2015 €m	2014 €m
Loans and receivables to banks (note 11)	60	77
	60	77

Loans and Receivables to Banks include funds placed on short-term deposit which are treated as cash/ cash equivalents within the cash flow statement.

22. SEGMENTAL INFORMATION

The Bank's income and assets are entirely attributable to mortgage lending activity in the Republic of Ireland.

23. 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 Banks' accounting policy for the determination of fair value of financial instruments is set out in accounting policy number 1.6, 1.7 and 1.15.

Readers of these financial statements are advised to use caution when using the data in the following table to evaluate the Bank's 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, shareholders' equity and assets held for sale. 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 2015.

The valuation of financial instruments, including loans and receivables, involves the application of judgement and estimation. Market and credit risks are key assumptions in the estimation of the fair value of loans and receivables. The Bank 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 AIB Group and valuation methodologies are validated by the Risk function within AIB Group.

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 validated 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 Bank's 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 is estimated.

Counterparty credit and own credit is an input into the valuation of uncollateralised customer derivatives.

Loans and receivables to banks
The fair value of loans and receivables to banks is estimated using discounted cash flows applying either market rates, where practicable, or rates currently offered by other financial institutions for placements with similar characteristics.

NOTES TO THE FINANCIAL STATEMENTS (continued)

23. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

Loans and receivables to customers
The Bank provides lending facilities of varying rates and maturities to 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 receivables 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 2015 took account of the Banks' expectations on credit losses over the life of the loans.

Deposits by banks
The fair value of current accounts and 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.

Debt securities in issue
The estimated fair value of subordinated liabilities and other capital instruments and 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.

Other financial assets and other financial liabilities
This caption includes accrued interest receivable and payable and the carrying amount is considered representative of fair value.

NOTES TO THE FINANCIAL STATEMENTS (continued)

23. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

The following table sets out the carrying value of financial instruments across the three levels of the fair value hierarchy at the 31 December 2015:

2015	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 derivative	Cash flow hedge derivatives	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
Derivative financial instruments	-	-	-		-	-	-	-	-	-
Interest Rate Derivatives	20	-	-		-	20	-	20	-	20
Financial assets not measured at fair value										
Loans and receivables to banks	-	-	-	60	-	60	-	-	60	60
Loans and receivables to customers	-	-	-	5,265	-	5,265	-	-	4,999	4,999
Other financial assets	-	-	-					-		
	20	-	-	5,325	-	5,345	-	20	5,059	5,079
Financial liabilities measured at fair value										
Derivative financial instruments	-	-	-	-	-	-	-	-	-	-
Interest Rate Derivatives	20	-	-	-	-	20	-	20	-	20
Financial liabilities not measured at fair value										
Deposits by banks	-	-	-	-	2,271	2,271	-	-	2,271	2,271
Debt securities in issue	-	-	-	-	2,387	2,387	-	2,123	-	2,123
Other financial liabilities	-	-	-	-	1	1	-	-	1	1
	20	-	-	-	4,659	4,679	-	2,143	2,272	4,415

No transfers in or out of Level 3 have occurred during 2015.

NOTES TO THE FINANCIAL STATEMENTS (continued)

23. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

The following table sets out the carrying value of financial instruments across the three levels of the fair value hierarchy at the 31 December 2014:

	2014									
	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 derivative	Cash flow hedge derivatives	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
Derivative financial instruments										
Interest Rate Derivatives	22	-	-	-	-	22	-	22	-	22
Financial assets not measured at fair value										
Loans and receivables to banks	-	-	-	77	-	77	-	-	77	77
Loans and receivables to customers	-	-	-	5,623	-	5,623	-	-	5,326	5,326
Other financial assets	-	-	-	-	-	-	-	-	-	-
	22	-	-	5,700	-	5,722	-	22	5,403	5,425
Financial liabilities measured at fair value										
Derivative financial instruments										
Interest Rate Derivatives	22	-	-	-	-	22	-	22	-	22
Financial liabilities not measured at fair value										
Deposits by banks	-	-	-	-	3,383	3,383	-	-	3,383	3,383
Debt securities in issue	-	-	-	-	1,807	1,807	-	1,606	-	1,606
Other financial liabilities	-	-	-	-	1	1	-	-	1	1
	22	-	-	-	5,191	5,213	-	1,628	3,384	5,012

No transfers in or out of Level 3 have occurred during 2014.

NOTES TO THE FINANCIAL STATEMENTS (continued)

24. RELATED PARTY TRANSACTIONS

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 the 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.

Summary of the AIB Group relationship with the Irish Government
The Irish Government, as a result of both its investment in AIB's 2009 Preference shares and AIB's participation in Government guarantee schemes, became a related party of AIB in 2009. Following the various ordinary/CNV share issues to NPRFC(1) during 2010 and 2011, AIB is under the control of the Irish Government.

AIB enters into normal banking transactions with the Irish Government and many of its controlled bodies on an arm's length basis. In addition, other transactions include the payment of taxes, pay related social insurance, local authority rates, and the payment of regulatory fees, as appropriate. Following the crisis in the Irish banking sector and the stabilisation measures adopted since 2008, the involvement of the Irish Government in AIB and in other Irish banks has been and continues to be considerable. This involvement is outlined below.

Rights and powers of the Irish Government and the Central Bank of Ireland.
The Irish Minister for Finance ('the Minister') and the Central Bank of Ireland ("the Central Bank") have significant rights and powers over the operations of AIB (and other financial institutions) arising from the various stabilisation measures. These rights and powers relate to, 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, 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 and payment of dividends;
- Restrictions on various types of remuneration;
- Buy-backs or redemptions by the Group of its shares;
- The manner in which the Group extends credit to certain customer groups; and
- Conditions regulating the commercial conduct of Allied Irish Banks, p.l.c, having regard to capital ratios, market share and the Group's balance sheet growth. In addition, various other initiatives such as strategies/codes of conduct for dealing with mortgage and other consumer/business loan arrears are set out in the Risk section of this report.

The relationship of the Irish Government with AIB is outlined under the following headings:
- Guarantee schemes;
- NAMA;
- Funding support;
- PCAR/PLAR;
- Credit Institutions (Stabilisation) Act 2010:
    - (i) Direction Order;
    - (ii) Transfer Order;
    - (iii) Subordinated Liabilities Order;
- Central Bank and Credit Institutions (Resolution) Act 2011.
- Relationship framework which was signed in March 2012.

In addition, the European Commission, in approving AIB's restructuring plan on 7 May 2014, found that restructuring aid granted by Ireland to AIB is in line with EU state aid rules

Guarantee schemes
The Bank is a covered institution 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 European Central Bank arising from Eurosystem monetary operations. Under the terms of the CIFS Scheme the Central Bank in consultation with the Minister regulated the commercial conduct of covered institutions strictly in order to achieve the objectives of this scheme.

NAMA
The Irish Government set up an asset relief scheme in 2009 under the auspices of the National Asset Management Agency in Ireland. The Bank is a participating institution in NAMA. However, no loans were transferred from the Bank to NAMA.

Funding support
At 31 December 2015 the amount of ECB funding received through the ECB Monetary Policy Operation Sale and Repurchase Agreements was Nil (2014: Nil). 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.

(1)Transferred to the Ireland Strategic Investment Fund ("ISIF") on 22 December 2014. Ownership of ISIF vests with the Minister for Finance and is controlled and managed by the NTMA.

NOTES TO THE FINANCIAL STATEMENTS (continued)

24. RELATED PARTY TRANSACTIONS (continued)

Summary of the AIB Group relationship with the Irish Government (continued)

PCAR/PLAR
On 31 March 2011, the Central Bank of Ireland published the 'Financial Measures Programme Report' which detailed the outcome of its review of the capital (PCAR) and funding (PLAR) requirements of the domestic Irish banks. The PCAR/PLAR assessments followed the announcement of the EU-IMF Programme for Ireland in November 2010, in which the provision of an overall amount of €85 billion in financial support for the sovereign was agreed in principle. Up to €35 billion of this support was earmarked for the banking system, €10 billion of which was for immediate recapitalisation of the banks with the remaining €25 billion to be provided on a contingency basis. Arising from the 2011 PCAR and PLAR assessments, AIB, including EBSMF, was required to raise €14.8 billion in total capital (including €1.6 billion in contingent capital), all of which was subsequently raised.

Credit Institutions (Stabilisation) Act 2010
The Credit Institutions (Stabilisation) Act 2010, which was enacted in December 2010, ceased to have effect on 31 December 2014. During the period when the Act was effective, the Minister invoked certain of his powers under the Act in relation to AIB as follows:
- A Direction Order in December 2010;
- A Transfer Order in February 2011;
- A Subordinated Liabilities Order in April 2011; and
- Acquisition of EBS Limited ("EBS").

On 31 March 2011, the Minister proposed the combination of AIB and EBS (formerly EBS Building Society) to form one of the two Pillar banks. On 26 May 2011, AIB entered into an agreement with EBS, the Minister and the NTMA to acquire EBS for a consideration of €1 (one euro). The acquisition was effective from 1 July 2011.

Central Bank and Credit Institutions (Resolution) Act 2011
The Central Bank and Credit Institutions (Resolution) Act 2011 became effective on 28 October 2011. This legislation provides the Central Bank 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 gives the Central Bank 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. On 30 September 2014, the Minister for Finance made Regulations – the Credit Institutions Resolution Fund Levy Regulations, 2014 ("2014 Regulations") – which amend and update the 2012 Regulations and provide for contributions by authorised credit institutions to the Credit Institutions' Resolution Fund ("Resolution Fund") pursuant to Section 15 of the Central Bank and Credit Institutions (Resolution) Act 2011. The 2012 Regulations (as updated by the 2014 Regulations) require every person who, on 1 October 2014, is an authorised credit institution described in the Schedule to the 2012 Regulations to pay a levy in respect of the levy period to the Central Bank of Ireland ("Central Bank") for the account of the Resolution Fund. This includes all banks, building societies and credit unions licensed in Ireland with the exception of institutions covered by the Credit Institutions (Stabilisation) Act, 2010. This Resolution Fund has been designed to provide a source of funding for the resolution of financial instability in, or of, an imminent serious threat to the financial stability of an authorised credit institution.

The Act provides for the establishment of "Bridge-Banks" for the purpose 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 is 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 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.

Relationship framework
In order to comply with the contractual commitments imposed on AIB 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 and AIB in March 2012. This provides the framework under which the relationship between the Minister and AIB is governed. Under the relationship framework, the authority and responsibility for strategy and commercial policies(including business plans and budgets) and conducting AIB's day-to-day operations rest with the Board of AIB and its management team. However, the Board is required to obtain the prior written consent of the Minister, or to consult with the Minister, in respect of certain material matters, such as material disposals.

Restructuring Plan commitments
AIB has committed to a range of measures relating to customers in difficulty: cost caps and reductions; acquisitions and exposures; coupon payments; promoting competition; and the repayment of aid to the State. All of the commitments are aligned to AIB's operational plans and are supportive of AIB's return to viability.

Transactions with EBS Ltd
The following amounts represent the transactions and outstanding balances with EBS Ltd:

- Loans from EBS at 31 December 2015 are €2,271m (2014: €3,383m).
- Deposits placed with EBS at 31 December 2015 are €31m (2014: €33m).
- The nominal value of debt securities in issue to EBS at 31 December 2015 are €2,400m (2014: €1,850m).

NOTES TO THE FINANCIAL STATEMENTS (continued)

24. RELATED PARTY TRANSACTIONS (continued)

Transactions with EBS Ltd (continued)

Derivative financial instruments with EBS Ltd

Interest rate swaps	**2015**	2014
	€m	€m
Assets (Fair value)	**20**	22
Liabilities (Fair value)	**20**	22

At 31 December 2015, there were no derivative transactions between the Bank and the ultimate parent, Allied Irish Banks, p.l.c..

	2015	2014
	€m	€m
Income and expense included in the Income Statement from related parties:		
Service fee	**(5)**	(6)
Interest expense on loans	**(21)**	(26)
Interest expense on debt securities	**(48)**	(109)
Net trading income	**3**	2
Loss on repurchase of debt securities in issue (see note 6)	**(9)**	-

The above transactions arose in the ordinary course of business. The interest charged and interest earned involving related parties is at normal commercial rates appropriate to the transaction.

There have been no contracts or arrangements with the Bank in which a Director of the Bank was materially interested and which were significant in relation to the Bank's business.

Transactions with key management personnel
Loans to Key management personnel are made in the ordinary course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons of similar standing not connected with EBS Mortgage Finance, and do not involve more than the normal risk of collectability or present other unfavourable features. Loans to Executive Directors and Senior Executive Officers are also made in the ordinary course of business, on terms available to other employees in EBS Mortgage Finance generally, in accordance with established policy, within limits set on a case by case basis.

Details of transactions with Key management personnel, and connected parties where indicated, for the year ended 31 December 2015 are as follows:

(i) Current Directors
Directors in office during 2015, being Denis Holland, William Cunningham, Fidelma Clarke, Gerry Gaffney and Owen Purcell had no facilities with EBS Mortgage Finance during 2015.

(ii) Former Directors who were in office during the year
There were no changes to the Board during the year.

(iii) Senior Executive Officers in office during the year
Senior Executive Officers in office during the year had no facilities with EBS Mortgage Finance during 2015.

(iv) Connected persons
There were no loans to connected persons of Directors in office as at 31 December 2015, as defined in Section 220 of the Companies Act 2014 requiring disclosure in accordance with conditions attached to the EBS Mortgage Finance banking licence.

No impairment charges or provisions have been recognised in respect of any of the above loans or facilities detailed in (i) to (iv) and all interest that has fallen due on all of these loans or facilities has been paid.

As at 31 December 2015, no Directors or Senior Executive Officers held guarantees with EBS Mortgage Finance.

25. COMMITMENTS
At 31 December 2015 the Bank had €11m (2014: €12m) of approved mortgage loan applications that had not been drawn down as at the year end.

26. SUBSEQUENT EVENTS
No events have occurred post year end which would require adjustment to or disclosure in these financial statements.

27. APPROVAL OF FINANCIAL STATEMENTS
The financial statements were approved by the Directors on the 18th March 2016.