PILLAR 3 DISCLOSURES 2012

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1 Overview

1.1 Background

The European Union Capital Requirements Directive came into effect on 1 January 2007. Implementation of the Directive in the UK was by way of rules introduced by the Financial Services Authority (“the FSA”).

The Basel II framework consists of three “pillars”. Pillar 1 of the standards sets out the minimum capital requirements firms are required to meet for credit, market and operational risk. Under Pillar 2, firms and supervisors have to take a view on whether a firm should hold additional capital against risks not covered in Pillar 1 and demonstrate their ability to manage their capital position through a period of stress. The aim of Pillar 3 is to improve market discipline by requiring firms to publish certain details of their risks, capital and risk management.

Yorkshire Building Society (“YBS”) adopted the Pillar 1 standardised approach to credit risk and operational risk from 1 January 2008. It also became subject to Pillars 2 and 3 from that date.

1.2 Basis and Frequency of Disclosures

This disclosure document has been prepared by YBS in accordance with the requirements of Pillar 3. Unless otherwise stated, all figures are as at 31 December 2012, the Group’s financial year-end.

1.3 Scope

YBS is an EEA parent institution that is regulated in the UK by the FSA. The Basel II Framework therefore applies to YBS and its subsidiary undertakings (together “the Group”).

Consolidation of the Group position for regulatory capital purposes (the “Capital Group”) is similar to the statutory consolidated Group position produced for the Annual Report and Accounts but differs in the following respects:

- There is one Group company (Yorkshire Key Services Ltd) that, due to the nature of its activities, is outside the scope of the Basel II framework to be included for capital purposes, but is fully consolidated in the Annual Report and Accounts. This company is immaterial in its impact on Group capital positions.
- Some definitions of assets and capital differ between the regulated capital adequacy rules and the statutory accounting balance sheet standards.

There are no restrictions or impediments to the movement of capital between legal entities within the consolidated Capital Group, and there is no material capital surplus or deficiency for legal entities that comprise the statutory accounting group but not the Capital Group.

Under FSA rules, YBS as a legal entity must also maintain a solo capital requirement. In this area, YBS has made use of the provisions laid down in BIPRU 2.1 (Solo consolidation) to provide capital resources and requirements to the FSA under a solo consolidated basis. This enables both the major intra group exposures and investments of YBS in its subsidiaries within the solo-consolidated group to be eliminated when calculating capital resource requirements and the reserves of such solo subsidiaries to be aggregated to the parent when calculating capital resources.

The principal subsidiaries included under solo consolidation in 2012 were:

- Yorkshire Building Society
- Accord Mortgages Limited
- Yorkshire Investment Services Limited
- Chelsea Mortgage Services Limited
- Norwich & Peterborough (LBS) Ltd

Full details of the principal subsidiary undertakings are included in note 10 to the Annual Report and Accounts.

1.4 Location and Verification

These disclosures have been reviewed by the Group's Risk Committee on behalf of the Group's Board and are published on the Group's corporate website (www.ybs.co.uk). The disclosures are subject to periodic internal independent review by Group Internal Audit but are not subject to external audit except where they are equivalent to those prepared under accounting requirements for inclusion in the Group's Annual Report and Accounts.

1.5 Remuneration Disclosures

The Group has set a remuneration policy that does not encourage undue risk taking and the overall policy is that:

- The remuneration of executive directors, General Managers and other Code Staff should deliver an appropriate balance between encouraging strong financial performance and ensuring sound risk management.
- The remuneration of executive directors (together with that of General Managers and other Code Staff) should be competitive with those of comparable organisations in the financial sector as well as reflecting the responsibilities and the intrinsic skills and capabilities required in the role, so as to attract and retain high-calibre individuals with the relevant experience.
- A significant part of the remuneration of executive directors, General Managers and other Code Staff should be variable, based primarily on the Group's financial, risk and service performance (in particular, the net promoter score) and should also be based on individual performance, using pre-determined targets to motivate and reward successful business and personal performance in the interests of current and future members. However, the proportion of variable pay is limited to ensure that it is feasible for none to be paid in years where business performance does not merit payment.
- Personal reviews of the executive directors, General Managers and other Code Staff are carried out at least annually to assess their performance in meeting individual and strategic objectives. These reviews are reflected in pay reviews which take effect from 1 May each year as well as in awards of variable pay.
- The remuneration of senior staff in the Risk and Compliance function is independently considered by the Group Risk Committee, in addition to being approved by the Remuneration Committee.
- No executive director, General Manager or member of Code Staff is involved in deciding his or her own remuneration.
- The policy should comply with the Financial Services Authority's (FSA) Remuneration Code.

The Group's full remuneration disclosures for 2012 can be found on pages 61 to 68 of the Annual Report and Accounts, which can be found on the Society's Internet site.

1.6 Regulatory Developments

The proposed Basel III regulations are being written in to European law in the form of a Regulation and Directive commonly known as CRD IV. Implementation of these new rules depends on political agreement, but an implementation date of 1st January 2014 is expected . These rules make substantial changes to the definition of capital resources and include additional capital requirements (for example, for counterparty credit risk). The Group's PIBS (Permanent Interest Bearing Shares) and subordinated debt will cease to be eligible capital for regulatory purposes and will be phased out over a 10 year period, in line with the proposed regulations. A leverage ratio measure is also introduced under the proposals.

The Basel III regulations are subject to change as they are implemented in EU and UK law, but the expected impact based on current proposals would be to reduce the Group's Core Tier 1 ratio by c0.6% if the fully phased in rules were applied to the Group's end-2012 position. It is forecast that the Group will remain comfortably in excess of the proposed 3% leverage ratio throughout the planning horizon.

1.7 Recent Developments – Capital Buy Back

In 2012, the Group bought back £235m of remunerated capital[1], realising a pre-tax profit of £62m for the Group. This transaction removed capital that would be phased out over a ten year period under Basel III (as highlighted above) and replaced it with a lower volume of additional Core Tier 1 generated from post-tax profits leading to a net long-term improvement.

In the shorter term this has had the impact of reducing the overall capital and the Tier 1 ratio while increasing the Core Tier 1 ratio. As the latter shows the Group's financial strength as measured by the highest quality capital, it is considered to be the key ratio and the buy back exercise further strengthens the Group's ratio to leave it as one of the strongest in the UK.

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[1] This is the nominal amount – the Tier 1 & Tier 2 capital reduction was greater due to fair value elements being included in the regulatory value.

2 Risk Management Objectives and Policies

2.1 Risk Appetite

The Board has defined its risk appetite as part of its overall risk management strategy. At a more pragmatic level, the Group's risk appetite is used for several practical purposes:

- To provide an objective measure against which the Group's various risk committees can measure the Group's current and proposed risk positions, ensuring compliance with the strategic direction set by the Board.
- To provide a set of measures against which management can look to optimise the risk versus reward equation.
- To provide a base for setting objective measures for different parts of the business, giving them clarity over the parameters within which they must operate.

The Group's overall statement of business risk appetite is:

- **"The organisation will not take, or retain, risk positions that threaten its ability to remain a sustainable and independent mutual organisation, therefore ensuring the sustainability of YBS and thereby ensuring that no stakeholder suffers a loss."**

Underneath this overall statement of appetite are a number of specific risk appetites:

- Retail Credit Risk Appetite
- Wholesale Credit Risk Appetite
- Liquidity and Funding Risk Appetite
- Market Risk Appetite
- Operational Risk Appetite
- Conduct Risk Appetite
- Business Risk Appetite

2.2 Risk Management Framework

The Group's risk management framework and governance structure provides a mechanism for proactively identifying and addressing the key risks to the achievement of the Group's objectives. It delivers comprehensive monitoring, control and ongoing management of the major risks to which the Group is exposed, so as to ensure the security of stakeholder funds. The Group's ability to properly identify, measure, monitor and report risk is critical to its soundness and its ability to provide value and fair outcomes to its membership and customers.

The Board is ultimately responsible for every aspect of the Group's activities. In particular, its role is to focus on the Group's strategy and ensure that the necessary resources are in place to meet its objectives and to ensure that robust financial controls and systems of risk management are in place.

2.3 Risk Identification, Measurement and Control

The Group has a framework of consistently articulated risk appetites and a regularly updated Group Risk Map by which the Group aims to identify the major sources of risk to its strategic objectives, its assets and operations. The Group then deploys appropriate measures to control and monitor those risks. The key risks are plotted on the Group Risk Map with their position determined by the assessment of net impact and likelihood of occurrence, together with an assessment of whether each risk is outside or within the Group's risk appetite. Supporting each risk assessment is a risk dashboard that integrates all the relevant information about the risk, including key risk indicators (KRIs), control assessments, audit and compliance points, emerging issues, and actions being taken. The risk dashboards are updated monthly and reviewed by General Management in detail on a quarterly basis. The Group Risk Committee reviews the dashboards relating to the most significant risks on a quarterly basis. On an annual basis, the Group Risk Map is completely refreshed via a "blank sheet" exercise, going back to first principles.

At an operational level, these principal risks and uncertainties can be considered in a number of categories, around which the Group has constructed its systems of monitoring and control, these categories being:

- Credit risk
- Market, liquidity and funding
- Operational and regulatory/conduct
- Business risk

The individual risks, and the Group's response to them, are considered in more detail within the context of the risk committees established to oversee them under delegated authority of the board, see below. The risk categories into which the key risks to the Group can be categorised are in turn considered as part of the Group's Internal Capital Adequacy Assessment Process (ICAAP).

2.4 Risk Oversight

The Group Risk Committee has been established by the Board to oversee the Group's risk governance framework and to provide an entity-wide perspective on all risk matters. It comprises non-executive directors and senior executives and is chaired by a non-executive director. Its primary responsibilities include:

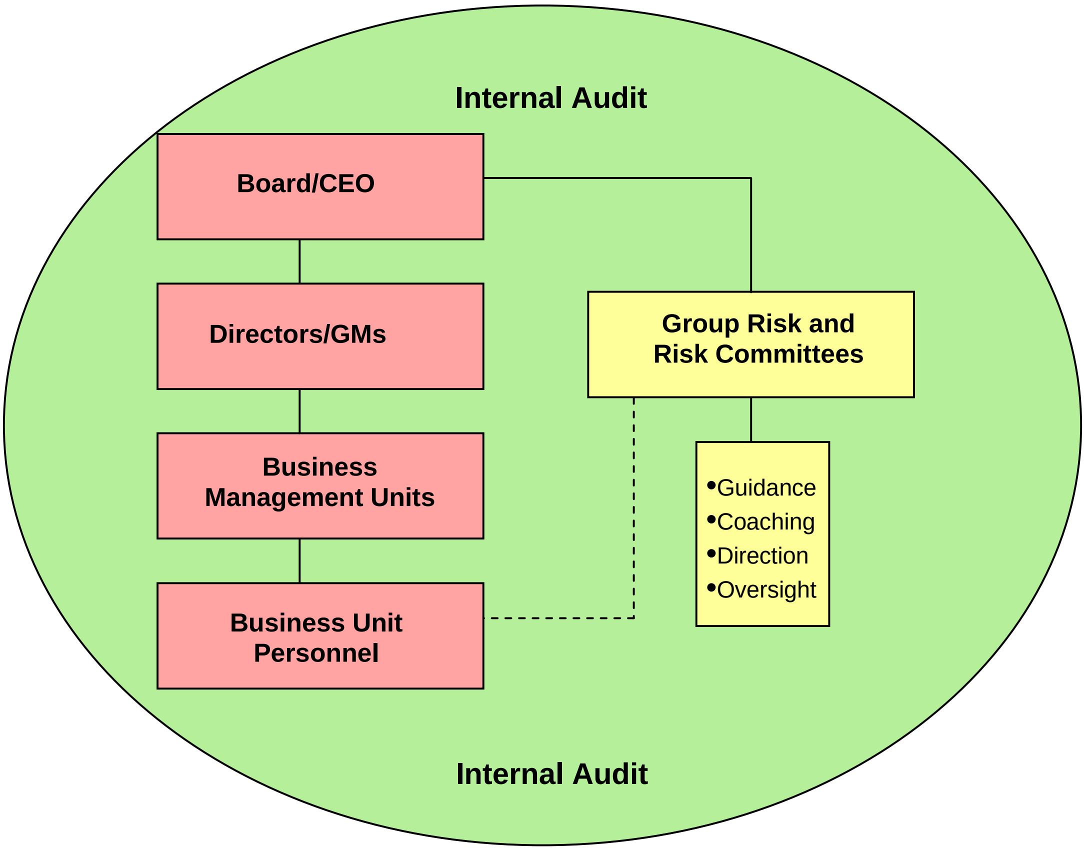
- Oversight of the Group Risk Profile and actions taken to manage key risks.
- Approval of the Group's risk appetite and monitoring of adherence to the appetite throughout the year.
- Recommending the Group Risk Management policies, standards and limits for Board approval.
- Monitoring on-going risk positions and issues, in particular, for compliance with Group Risk Management policies, standards and limits.
- Monitoring the Group's conduct risk management framework and its effectiveness in the delivery of fair/good customer outcomes.
- Annual review and approval of the Group's ICAAP, on recommendation from the Group Capital Committee.
- Approval of the Pillar 3 disclosure policy and annual review of those disclosures.
- Consideration of whether existing activities constitute appropriate utilisation of the Group's available capital.
- Oversight of risk stress testing, including reverse stress tests.
- Annual review and approval of the Group's Individual Liquidity Adequacy Assessment (ILAA) on recommendation from the Group Asset & Liability Committee.
- Review and approval of the Group's compliance with the liquidity regime.
- Review of the Money Laundering Reporting Officer's annual report.
- Review of the Group's current and proposed activities against its risk appetite and capital budgets.
- Oversight of the scope and review of the due diligence process for major acquisitions.
- Review and approval of the Group's recovery and resolution plans.

- Establishment and monitoring of the relevant sub-committees and associated governance structures.

The Group Risk Committee has put in place a risk management policy which documents the Group's approach to risk management across its major risk categories, the governance structure it has put in place, responsibilities of individual risk committees and functions within the risk framework, and a comprehensive set of limits and triggers used by the Board and its sub committees to monitor the risk profile of the Group against its risk appetite.

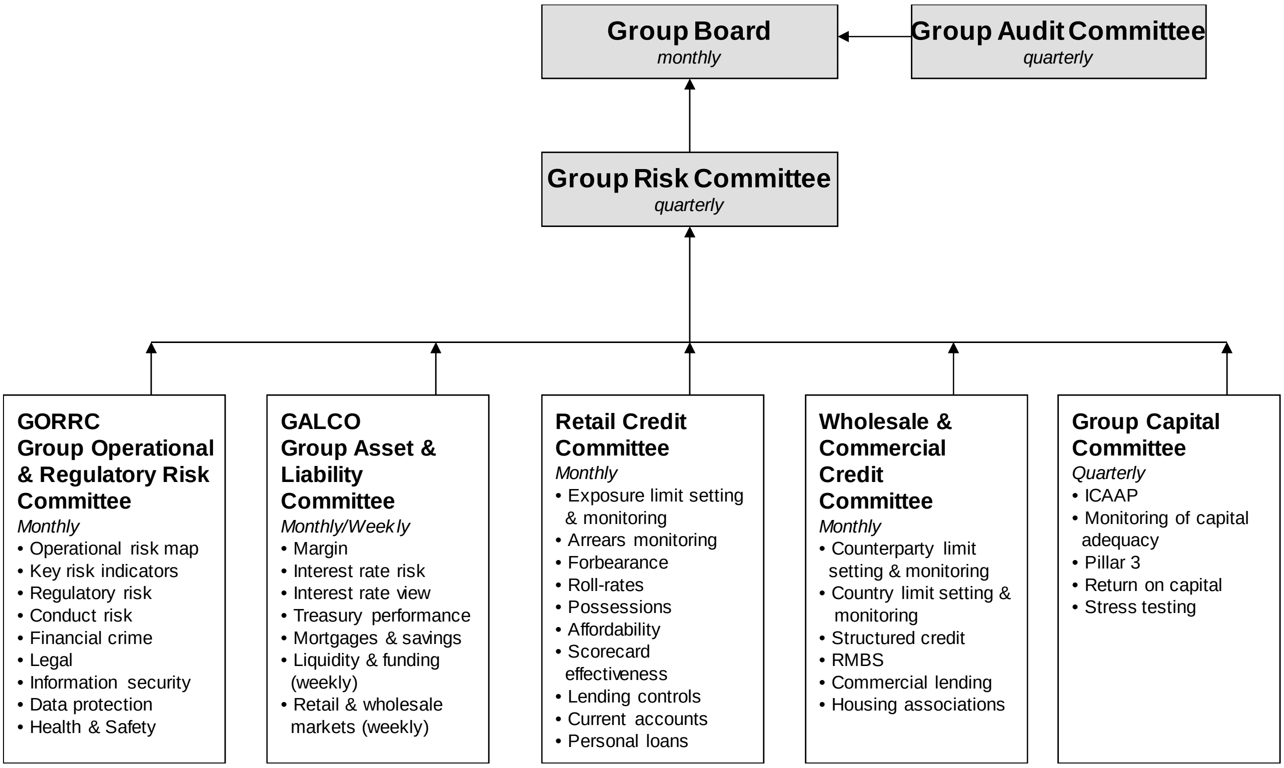
YBS's approach to risk management is founded on robust corporate governance practices and a clear risk culture demonstrating that all are accountable for risk management. The Board takes the lead by establishing the tone from the top including an effective Board Risk Committee.

The industry best practice, and YBS practice, of a three lines of defence risk management model is appropriate and allows for clear accountability where demarcation between the lines of defence exists. The model is best illustrated as (Red = 1st Line, Yellow = 2nd Line, Green = 3rd Line):



The Board ensures that management implements risk policies and risk appetites (qualitative and quantitative) that either limit, or where appropriate, prohibit relationships and activities that could diminish the standing of YBS.

The risk governance structure of the Group is illustrated in the following diagram:



2.5 Risk Monitoring and Reporting

The Group maintains an independent risk management function (Group Risk) that is responsible for ensuring that appropriate risk management techniques and measures are deployed. These seek to reflect leading practice, whilst remaining commensurate with the Group's strategic aims, its appetite for risk and the actual risks it faces at any time. The Group Risk function provides periodic independent reports on risk positions and risk management activities for consideration by the Group Risk Committee, its sub-committees and the Board. The General Manager – Risk provides a formal update to each Board meeting covering all areas of risk management, including both routine reporting and ad hoc issues.

3 Capital Resources

3.1 Total Available Capital

At 31 December 2012 and throughout the year, the Group complied with the capital requirements that were in force as set out by the FSA. The following table shows the breakdown of the total available capital for the capital group and solo-consolidated group as at 31 December 2012:

Table 1 - Capital Resources	**Group**	**Group**	**Solo**	**Solo**
£m	**Dec-2012**	**Dec-2011**	**Dec-2012**	**Dec-2011**
Core Tier 1 Capital				
General reserve	1,685.8	1,581.9	1,704.3	1,485.5
Pension scheme adjustment	(16.6)	(29.4)	(16.6)	(29.4)
Deductions from Core Tier 1 Capital				
Intangible fixed assets	(34.3)	(30.4)	(34.2)	(30.2)
Material holdings	(1.7)	(1.7)	(1.7)	(1.7)
Investments in non solo-consolidated subsidiaries[a]	0.0	0.0	0.0	(3.9)
Securitisation holdings deducted from capital resources	(11.6)	(18.2)	(11.6)	(18.2)
Total Core Tier 1 Capital	**1,621.6**	**1,502.2**	**1,640.2**	**1,402.1**
Additional Tier 1 Capital				
Permanent Interest Bearing Shares (PIBS)	7.3	177.0	7.3	177.0
Total Tier 1 Capital	**1,628.9**	**1,679.2**	**1,647.5**	**1,579.1**
Tier 2 Capital				
Subordinated liabilities	117.2	227.4	117.2	227.4
Collective provisions for impairment	6.3	8.0	6.3	8.0
Deductions for Tier 2 Capital				
Material holdings	(1.7)	(1.7)	(1.7)	(1.7)
Investments in non solo-consolidated subsidiaries[a]	0.0	0.0	0.0	(3.9)
Securitisation holdings deducted from capital resources	(11.6)	(18.2)	(11.6)	(18.2)
Total Tier 2 Capital	**110.2**	**215.5**	**110.2**	**211.6**
Other items excluded	(4.1)	(2.6)	(6.0)	(4.3)
Total Capital Available	**1,735.0**	**1,892.1**	**1,751.7**	**1,786.4**

[a] – Under solo consolidation, investments are not included in capital and are consequently deducted 50% from Tier 1 and 50% from Tier 2.

3.2 Tier 1 Capital

Tier 1 capital comprises the general reserve, PIBS and adjustments for items reflected in the general reserve which are treated separately for capital adequacy purposes.

- PIBS are unsecured deferred shares and rank behind the claims of all subordinated noteholders, depositors, creditors and investing members of YBS. Further details about PIBS are provided in note 30 to the Annual Report and Accounts. Following the buy back of non-core capital detailed in section 1.7, the PIBS reduced considerably in 2012.
- An adjustment is made to Tier 1 capital in respect of the Group's defined benefit pension obligations. The regulatory capital rules allow a pension fund surplus/deficit to be deducted from/added back to regulatory capital and, in the case of a deficit, a deduction taken instead for an estimate of the additional contributions to be made in the next five years, less associated

deferred tax. At 31 December 2012, the net impact of the adjustment was a reduction in Tier 1 capital of £16.6m.

- An adjustment is also made in respect of intangible assets. For accounting purposes, items including software development costs, other intangibles resulting from business combinations and goodwill are capitalised as intangible fixed assets where they meet certain criteria. Intangibles are deducted from capital under the regulatory rules and at 31 December 2012, £34.3m has been deducted from capital in respect of intangible assets.
- Securitisation positions (including resecuritisations as defined in CRD3) that are unrated or have low external ratings can be risk weighted at 1250% or deducted from capital resources, with deductions applied equally between Tier 1 and Tier 2. In 2012, the Group deducted £11.6m from Tier 1 and £11.6m from Tier 2 capital relating to low rated and unrated securitisations.

3.3 Tier 2 Capital

Tier 2 capital comprises the Group's qualifying subordinated liabilities, the collective impairment provision, and adjustments for items treated separately for capital adequacy purposes.

- Subordinated notes are unsecured and rank behind the claims of all depositors, creditors and investing members (other than holders of PIBS) of YBS. More details of the subordinated liabilities are included in note 29 to the Annual Report and Accounts. Following the buy back of non-core capital detailed in section 1.7, the subordinated notes reduced considerably in 2012.
- To the extent that collective provisions for impairment have been recognised in the income and expenditure account these may be added back to Tier 2 capital.

4 Capital Adequacy

4.1 Capital Management

The Group's management of its capital is based on a number of key principles:

- The maintenance of sufficient quality and quantity of regulatory capital to meet solvency requirements and to ensure the Group's risk appetite is not breached. This relates to both current and projected capital (i.e. the levels of capital in light of the Group's strategy and corporate plans, current capital and risk weighted assets combined with future balance sheet movements and profitability, and with the potential for raising external capital).
- The maintenance of sufficient capital strength within the balance sheet to provide comfort to interested third parties, and to safeguard access to wholesale markets and maintain investor confidence.
- The efficient and effective allocation of capital across the Group's operations. Again, this needs to be commensurate with its status as a deposit taker and a mutual organisation.

The Group considers its overall capital requirement as part of its ICAAP, which is detailed in section 4.2.

Summarised regulatory capital positions and forecasts (including forecasts under stress scenarios) are reported monthly to the Board and quarterly to the Group Risk Committee. The Group Capital Committee, a sub-committee of the Group Risk Committee, receives detailed reports of the capital positions and the results of stress testing on a quarterly basis. Based on these, the Group Capital Committee considers whether capital plans should be reviewed. Business stream-specific reports of regulatory capital are also included in the monthly packs of the appropriate risk committees e.g. Group Credit Committee.

Regulatory capital covers the following risks across the capital Group:

- Pillar 1 risks (i.e. credit risk and operational risk). The minimum capital requirement is calculated using regulatory-prescribed risk weightings laid out in the FSA's rulebooks. The Group has adopted the standardised approach to both credit and operational risk since 1 January 2008 in order to calculate the Pillar 1 minimum capital requirement.
- Pillar 2 risks (i.e. all other material risks for which the Group does not require the provision of regulatory capital under Pillar 1). Each material risk that the Group has identified outside the scope of Pillar 1 (e.g. pension obligation risk, interest rate risk, concentration risk) has undergone considered and vigorous stress testing to calculate an economic value for each of the material risks across the Group.
- Capital Planning. The Group calculates an additional capital requirement (in addition to the Pillar 1 and Pillar 2 amounts above) representing the amount by which the Group's capital surplus would reduce through a "severe but plausible" stress scenario over the Group's planning horizon. This additional requirement is called the Capital Planning Buffer and does not technically form part of the overall regulatory minimum capital requirement.

4.2 Internal Capital Adequacy Assessment Process

The Group undertakes at least annually an ICAAP which is an internal assessment of its capital requirement. In performing the ICAAP, the Group considers the key risks to which it is exposed, and the levels of capital and other financial resources that should be held to safeguard the interests of its members and depositors, particularly during times of stress.

This process includes:

- Identification by senior managers of the relevant risk categories for the Group.
- Establishment, under the sponsorship of individual General Managers, of separate work streams to consider each risk category in detail.
- Analysis of the risks within each work stream, involving relevant personnel from across the business, and documented in individual risk assessment documents.
- Consideration of whether capital is an appropriate mitigant to the risk. Where this is deemed to be the case, capital requirements are calculated based on the results of severe stress testing for each risk category. Where capital is not deemed appropriate to mitigate a particular risk, alternative management actions are identified and described within the risk assessment. For certain risks where capital is not an appropriate mitigant, the holding of liquidity can be used to mitigate the risk. In these cases, the risk is considered in more depth as part of the ILAA process.
- Calculation of an appropriate “Capital Planning Buffer” to absorb a “severe but plausible” stress event over the Group’s planning horizon should such a scenario materialise, thereby ensuring minimum capital requirements are maintained.
- Approval of individual risk assessment documents by the relevant sponsor and Group Capital Committee.
- Documentation of the overall process and assessment, which is presented to Group Capital Committee before being presented to Group Risk Committee and the Board (with whom ultimate responsibility lies) for challenge and approval.

Further information on the material risks identified as part of the ICAAP can be found in section 7 of this document.

The Group received a new Individual Capital Guidance (ICG) following the FSA’s review of the 2012 ICAAP.

4.3 Minimum Capital Requirement (Pillar 1)

4.3.1 Credit Risk

The following table shows YBS's overall minimum capital requirement for credit risk under the standardised approach (expressed as 8% of the risk weighted exposure amounts for each of the applicable standardised credit risk exposure classes) at 31 December 2012. Details of the standardised approach to calculation of regulatory requirements are contained in the FSA handbook.

Table 2 - Credit Risk Pillar 1 Requirements	Group	Group	Solo	Solo
£m	**Dec-2012**	**Dec-2011**	**Dec-2012**	**Dec-2011**
Exposures secured on real estate property classes				
Loans to individuals	834.5	829.8	834.5	829.8
Commercial lending	35.6	33.7	35.6	33.7
Exposures secured on real estate property pillar 1 requirement	**870.1**	**863.5**	**870.1**	**863.5**
Wholesale exposure classes				
Asset securitisation	6.5	12.1	6.5	12.1
Central government or central banks	0.0	0.0	0.0	0.0
Covered bonds	0.0	0.0	0.0	0.0
Financial institutions	8.4	26.2	8.4	26.3
Multilateral development banks	0.0	0.0	0.0	0.0
Short term claims on financial institutions and corporates	3.6	4.3	3.5	2.7
Wholesale credit risk pillar 1 requirement	**18.5**	**42.6**	**18.4**	**41.1**
Banking & Personal loans				
Current accounts	0.1	0.0	0.1	0.0
Personal loans	0.3	0.7	0.3	0.7
Banking credit risk pillar 1 requirement	**0.4**	**0.7**	**0.4**	**0.7**
Other credit risk assets	20.4	17.5	21.3	16.9
Credit risk minimum capital requirement	**909.4**	**924.3**	**910.2**	**922.2**

4.3.2 Operational Risk

YBS's overall minimum capital requirement under Pillar 1 is calculated by adding the credit risk charge described in section 4.3.1 to that required for operational risk using the standardised approach. The operational risk charge is calculated by applying the Group's average gross income across the FSA defined income streams (over a 3 year period) to FSA defined ratios (that represent the relative risk in the various income streams).

4.3.3 Overall Minimum Capital Requirement

The table below shows both the Group's overall minimum capital requirement and capital adequacy position under Pillar 1 at 31 December 2012.

Table 3 - Total Capital Resources Less Total Pillar 1 Requirement £m	Group Dec-2012	Group Dec-2011	Solo Dec-2012	Solo Dec-2011
Credit risk (standardised)	909.4	924.3	910.2	922.2
Operational risk (standardised)	43.1	31.0	49.9	32.9
Total pillar 1 capital requirement	**952.5**	**955.3**	**960.1**	**955.1**
Total available capital	1,735.0	1,892.1	1,751.7	1,786.4
Excess of own funds over minimum capital requirement under Pillar 1	**782.5**	**936.8**	**791.6**	**831.3**

Sections 5 and 6 provide further detail on the significant risks captured under Pillar 1, i.e. credit risk and operational risk, including the nature of the exposures and the key risk management techniques. A summary of other significant risks captured under Pillar 2 is contained in section 7.

4.3.4 Risk Weighted Assets

The table below details the risk weighted asset values for each key category of Pillar 1 exposure. These values form the basis of the capital requirements shown in sections 4.3.1 and 4.3.2.

Table 4 – Risk Weighted Assets £m	Group Dec-2012	Group Dec-2011	Solo Dec-2012	Solo Dec-2011
Exposures secured on real estate property classes				
Loans to individuals	10,431.2	10,371.9	10,431.2	10,371.9
Commercial lending	445.6	421.8	445.6	421.8
Exposures secured on real estate property risk weighted assets	**10,876.8**	**10,793.7**	**10,876.8**	**10,793.7**
Wholesale exposure classes				
Asset securitisation	80.7	151.4	80.7	151.4
Central government or central banks	0.0	0.0	0.0	0.0
Covered bonds	0.5	0.5	0.5	0.5
Financial institutions	105.1	327.6	105.1	327.6
Multilateral development banks	0.0	0.0	0.0	0.0
Short term claims on financial institutions and corporates	44.3	53.1	44.0	34.1
Wholesale risk weighted assets	**230.6**	**532.6**	**230.3**	**513.6**
Banking & Personal loans				
Current accounts	1.1	0.3	1.1	0.3
Personal loans	3.2	8.5	3.2	8.5
Banking risk weighted assets	**4.3**	**8.8**	**4.3**	**8.8**
Operational risk weighted assets	538.7	389.8	623.8	411.5
Other credit risk weighted assets	255.3	218.1	266.0	211.5
Total risk weighted assets	**11,905.7**	**11,943.0**	**12,001.2**	**11,939.1**

Given the total minimum capital requirements are not materially different on a Group or solo consolidated basis, the disclosures in the remainder of this document are on a Group basis.

4.3.5 Capital Ratios

The table below shows the key capital ratios, which compare the capital resources as detailed in section 3.1 with the total Pillar 1 risk weighted assets shown in section 4.3.4. The ratios illustrate the Group's continued capital strength after taking account of the Capital Buy Back (which reduced the Solvency and Tier 1 ratios but increased the Core Tier 1 Ratio) – see section 1.7 for further details.

Table 5 - Capital Ratios		
	Dec-2012	**Dec-2011**
RWAs (£m)	11,906	11,943
Core Tier 1 Ratio (%)	13.62%	12.58%
Tier 1 Ratio (%)	13.68%	14.06%
Solvency Ratio (%)	14.57%	15.84%

5 Significant Risk Categories - Credit Risk

5.1 Credit Risk Overview

5.1.1 Introduction

Credit risk is defined as the risk that circumstances emerge such that counterparties fail to meet loan payment obligations resulting in financial loss.

For the purposes of Pillar 3 disclosures, credit risk is sub-divided into loans secured on real estate property, wholesale (treasury) and banking & personal loans. Over 98% of the Group's exposures secured on real estate property are loans to individuals.

The Group has in place a range of risk management tools and methods to ensure that risk exposures remain within overall risk appetite. These tools and methods cover both probability of possession and loss given possession, i.e. likelihood of a borrower to be unable to meet their obligations, and any potential loss mitigation, such as any collateral provided for a loan.

Risk exposures are closely monitored by the Retail Credit Committee and at a higher level by Group Risk Committee and the Board.

5.1.2 Exposures

The gross credit risk exposure (based on the definitions for regulatory capital purposes, before impairment provision and credit risk mitigation) and the average for the year is summarised as follows:

Table 6 - Credit Risk Exposure **£m**	**Average during 2012**	**Dec-2012**	**Average during 2011**	**Dec-2011**
Loans secured on real estate property				
Loans to individuals	27,518.3	27,602.9	24,147.0	27,113.3
Commercial lending	497.0	513.3	172.4	460.7
Total loans secured on real estate property	**28,015.3**	**28,116.2**	**24,319.4**	**27,574.0**
Wholesale				
Asset securitisation	357.7	196.3	1,107.2	637.8
Central governments or central banks	3,494.2	4,265.0	3,023.9	2,626.7
Covered bonds	5.1	5.0	1.3	5.0
Financial institutions	1,165.4	733.5	2,221.9	1,242.2
Multilateral development banks	213.4	153.3	509.3	321.7
Short term claims on institutions and corporates	214.9	221.3	305.4	265.6
Total wholesale exposure	**5,450.7**	**5,574.4**	**7,169.0**	**5,099.0**
Banking & Personal loans				
Current accounts	10.7	3.6	2.9	4.4
Personal loans	12.9	10.3	2.7	16.2
Total banking exposure	**23.6**	**13.9**	**5.6**	**20.6**
Other assets	256.3	255.3	259.4	218.1
Total credit risk exposure	**33,745.9**	**33,959.8**	**31,753.4**	**32,911.7**

The geographical distribution of these exposures at 31 December 2012 is as follows:

Table 7 - Loans Secured on Real Estate Property Geographic Distribution £m	Commercial lending Dec-2012	Loans to individuals Dec-2012	Commercial lending Dec-2011	Loans to individuals Dec-2011
Scotland	13.1	1,978.7	13.2	1,987.8
North East	7.1	1,103.0	7.6	1,132.4
Yorkshire & Humberside	18.0	2,938.0	18.9	3,027.6
North West	42.6	2,831.7	43.8	2,878.0
Midlands	47.5	3,451.8	48.6	3,431.5
East Anglia	26.6	1,380.5	27.7	1,428.6
South West	28.4	1,720.7	22.1	1,695.0
Greater London	132.5	5,250.1	107.5	4,709.1
South East	146.6	5,373.5	128.3	5,114.2
Wales & Northern Ireland	26.0	1,174.8	10.9	1,207.4
Spain	0.0	23.3	0.0	25.3
Gibraltar	0.0	59.4	0.0	67.4
Multiple/Unassigned	16.3	5.3	26.3	16.3
Undrawn	8.6	312.1	5.8	392.7
Total loans secured on real estate property	**513.3**	**27,602.9**	**460.7**	**27,113.3**

Table 8 - Wholesale Exposure - Geographic Distribution 2012 £m	UK Dec-2012	Other European Countries Dec-2012	North America Dec-2012	Rest of the World Dec-2012	Total
Asset securitisation	134.5	38.5	10.6	12.7	**196.3**
Central governments or central banks	4,265.0	0.0	0.0	0.0	**4,265.0**
Covered bonds	5.0	0.0	0.0	0.0	**5.0**
Institutions	353.4	115.9	256.7	7.5	**733.5**
Multilateral development banks	0.0	0.0	0.0	153.3	**153.3**
Short-term claims on institutions and corporates	211.7	9.4	0.2	0.0	**221.3**
Total wholesale credit exposure	**4,969.6**	**163.8**	**267.5**	**173.5**	**5,574.4**

Table 8 - Wholesale Exposure - Geographic Distribution 2011 £m	UK Dec-2011	Other European Countries Dec-2011	North America Dec-2011	Rest of the World Dec-2011	Total
Asset securitisation	568.1	50.9	9.6	9.2	**637.8**
Central governments or central banks	2,626.7	0.0	0.0	0.0	**2,626.7**
Covered bonds	5.0	0.0	0.0	0.0	**5.0**
Financial institutions	347.1	361.9	108.8	424.4	**1,242.2**
Multilateral development banks	321.7	0.0	0.0	0.0	**321.7**
Short-term claims on institutions and corporates	214.8	50.6	0.2	0.0	**265.6**
Total wholesale credit exposure	**4,083.4**	**463.4**	**118.6**	**433.6**	**5,099.0**

The following table shows the residual maturity of the exposures at 31 December 2012:

Table 9 - Credit Risk Exposure - Residual Maturity 2012	Up to 12 months	1 to 5 years	5 to 10 years	> than 10 years	
£m	Dec-2012	Dec-2012	Dec-2012	Dec-2012	Total
Loans secured on real estate property					
Loans to individuals	385.3	1,216.7	2,713.9	23,287.0	27,602.9
Commercial lending	89.4	46.2	66.9	310.8	513.3
Total loans secured on real estate property	**474.7**	**1,262.9**	**2,780.8**	**23,597.8**	**28,116.2**
Wholesale					
Asset securitisation	0.0	40.5	4.0	151.8	196.3
Central governments or central banks	4,153.6	0.0	0.0	111.4	4,265.0
Covered bonds	0.0	0.0	5.0	0.0	5.0
Financial institutions	210.4	50.5	143.1	329.5	733.5
Multilateral development banks	0.0	153.3	0.0	0.0	153.3
Short-term claims on institutions and corporates	221.3	0.0	0.0	0.0	221.3
Total wholesale exposure	**4,585.3**	**244.3**	**152.1**	**592.7**	**5,574.4**
Total credit risk exposure (excl. banking and other assets)	**5,060.0**	**1,507.2**	**2,932.9**	**24,190.5**	**33,690.6**

Table 9 - Credit Risk Exposure - Residual Maturity 2011	Up to 12 months	1 to 5 years	5 to 10 years	> than 10 years	
£m	Dec-2011	Dec-2011	Dec-2011	Dec-2011	Total
Loans secured on real estate property					
Loans to individuals	262.5	814.1	2,081.7	23,955.0	27,113.3
Commercial lending	55.9	38.7	28.8	337.3	460.7
Total loans secured on real estate property	**318.4**	**852.8**	**2,110.5**	**24,292.3**	**27,574.0**
Wholesale					
Asset securitisation	6.2	27.5	13.1	591.0	637.8
Central governments or central banks	1,968.3	323.6	222.6	112.2	2,626.7
Covered bonds	0.0	0.0	5.0	0.0	5.0
Financial institutions	713.5	397.0	35.3	96.4	1,242.2
Multilateral development banks	0.0	321.7	0.0	0.0	321.7
Short-term claims on institutions and corporates	265.6	0.0	0.0	0.0	265.6
Total wholesale exposure	**2,953.6**	**1,069.8**	**276.0**	**799.6**	**5,099.0**
Total credit risk exposure (excl. banking and other assets)	**3,272.0**	**1,922.6**	**2,386.5**	**25,091.9**	**32,673.0**

The maturity of exposures is shown on a contractual basis. In addition, it does not take into account any instalments receivable over the life of the exposure.

5.2 Retail Credit Risk

5.2.1 Coverage

The Group has retail credit portfolios covering the following products and brands:

	Yorkshire Building Society (YBS)	Accord	Chelsea Building Society (CBS)	Barnsley Building Society (BBS)	Norwich & Peterborough (N&P)	EGG
Residential mortgages	Y	Y	Y	Y	Y	Y*
Buy-to-Let mortgages	N	Y	Y*	N	Y*	N
Personal current accounts	N	N	N	N	Y	N
Unsecured personal loans	Y*	N	N	N	Y*	N

** closed to new business*

5.2.2 Governance

The Retail Credit Risk team operates as the "second line of defence" for the credit risk aspects of the Group's business; providing detailed analysis and insight of the Group's retail credit exposures, making, where appropriate, recommendations for change to ensure risk exposure remains within agreed appetites, limits and KRIs. This includes model development, model oversight, portfolio and acquisition analytics, quality assurance and policy oversight / development. Retail Credit Risk also has "dotted line" management responsibility for the Collections and Recoveries Analysis & MI team.

Retail credit risk is overseen by the Retail Credit Committee ("RCC"), a subcommittee of the Group Risk Committee, which meets monthly. Its terms of reference, membership and responsibilities are documented in the Group's Statement of Policy on Retail Credit Risk Management which is formally updated annually and approved by Group Risk Committee. In essence RCC is responsible for ensuring the Group remains within its agreed risk appetite for retail credit risk, via monitoring of both the risk appetite limits and KRIs, including the more detailed drivers of all aspects of credit risk via MI reporting, and approval of changes to credit policy, for new business, further lending and arrears management / collections and recoveries.

In addition, the Lending Criteria Committee, which is a subcommittee of the Retail Credit Committee, reviews in detail lending criteria proposals to assess them for their impact on the risk of the portfolio.

The Group Model Validation Committee exists to approve new predictive models and changes to existing models, monitor the ongoing performance and effectiveness of those models and approve the continued use of models via formal annual review.

The Board receives a report monthly covering the status of the key credit risk measures plus any other points of note.

5.2.3 New Lending Policy

The primary considerations when determining whether a credit product should be offered are ensuring that the applicant is able and willing to service that credit, and (for secured credit) that the property provides adequate security for the loan.

In assessing willingness and ability to service the loan, the Group uses credit scoring systems that factor in the profile of the borrower, the nature of the loan, evidence that the prospective borrower can service other debt obligations satisfactorily and environmental conditions. These scoring systems, and the way they are used within the initial lending process, are varied to suit the different risks and profiles of the Group's underlying credit portfolios. The score decision is combined with a number of other factors such as lending criteria, value of the collateral to be taken as security (for secured lending) and affordability for the customer to service the debt.

For secured lending the maximum percentage of the value of a property (loan-to-value, LTV) that an applicant may borrow is calculated in relation to the credit score, the applicant's income and expenditure profile, and lending criteria. LTVs are based on the market value of the property. No lending is undertaken based solely upon security provided by the value of the underlying assets. Once a mortgage application is made, the sales force has no bearing on the final decision. All mortgages are secured by way of a first legal charge against the property.

5.3 Wholesale Credit Risk

The Group's wholesale credit risk arises principally from assets held for liquidity purposes. The risk is that counterparties with whom the Group invests liquid assets fail to repay those investments and interest when they fall due.

The Group's Wholesale and Commercial Credit Committee ("WACCC") takes primary responsibility for the task of assessing and monitoring wholesale counterparty creditworthiness and conducting credit research and analysis. It does this by reviewing the Group's exposures and through setting limits to individual counterparties based on its internal ratings methodology. The internal ratings are derived by using the average external rating, from Moody's, Fitch and Standard & Poor's as a benchmark and then applying additional internal analysis based on a reflection of the Group's risk appetite. This analysis is then applied to an internal limit matrix derived from the Group's Year End Capital Resources in order to set a specific internal credit limit and rating.

Whilst recognising that exposures will be maintained across a spectrum of counterparties, the Board has maintained a low risk appetite for wholesale credit risk resulting in our inter-bank exposures being limited to operational requirements subject to our internal ratings process. Primary liquidity holdings are buffer eligible restricted to the Bank of England, UK Government and Multilateral Development Banks and secondary liquidity holdings support the overall liquidity requirements and must be considered internally to be liquid. Individual exposure limits are set according to the internal credit rating applied to a given institution. Limits are in place governing the types of instrument in which the Group will invest, as well as geographic and sector limits designed to prevent over exposure to a given country or business type.

Once in place, all individual counterparty limits are reviewed at least annually, with revocation or suspension taking place where considered appropriate. The ratings are compared with those produced by external rating agencies at least annually.

Risk positions are managed in accordance with limits set out in the Group Statement of Policy on Financial Risk Management. The policy also sets out powers which require higher levels of authorisation according to the size of the transaction or the nature of the associated risk.

Positions against limits and ongoing asset quality monitoring is undertaken by the Asset and Liability Management (ALM) function in Group Risk, which is independent at senior executive level from the dealing (Group Treasury) and back office (Treasury Operations) functions. Reports are sent to the Group's Wholesale and Commercial Credit Committee on a monthly basis, incorporating:

- Overall wholesale credit exposures, split between primary and secondary liquidity and structured credit, analysed by both internal and external credit rating bands and showing exposures, expected losses and capital requirements
- Overall distribution of internal and external credit ratings through wholesale portfolio
- High risk exposures (i.e. low rated investments) and large exposures (amounts classed as large exposures ranked by percentage of capital resources)

Treasury uses a number of risk mitigation techniques including netting and collateralisation agreements, which are considered further in section 5.7.

For the purposes of generating risk weightings for its wholesale exposures, YBS uses Standard and Poor's, Fitch and Moody's as External Credit Assessment Institutions (ECAIs), using a composite rating where a counterparty is rated by more than one agency.

The Board recognises that it is not possible to limit the Group's exposure to just institutions with the very highest credit ratings. Nevertheless it considers that the Group's approach (outlined above) is prudent and is designed to minimise the risk of losses.

The following tables show the exposure values associated with each credit quality step for wholesale exposures under the standardised approach:

Table 10 - Wholesale Exposure Credit Quality Steps
Central Government, Central Banks and Multilateral Development Banks

Credit Quality Step	Risk Weight (<3 months / >3 months)	S&P rating	Fitch rating	Moody's rating	Exposure values £m	Exposure values after mitigation[1] £m
Dec-2012						
1	0%/0%	AAA to AA-	AAA to AA-	Aaa to Aa3	4,418.3	4,413.4
2	20%/20%	A+ to A-	A+ to A-	A1 to A3	0.0	0.0
Total					**4,418.3**	**4,413.4**
Dec-2011						
1	0%/0%	AAA to AA-	AAA to AA-	Aaa to Aa3	2,948.4	2,948.4
2	20%/20%	A+ to A-	A+ to A-	A1 to A3	0.0	0.0
Total					**2,948.4**	**2,948.4**

Table 11 - Wholesale Exposure Credit Quality Steps
Financial Institutions, Covered Bonds and Short-termClaims

Credit Quality Step	Risk Weight (<3 months / >3 months)	S&P rating	Fitch rating	Moody's rating	Exposure values £m	Exposure values after mitigation[1] £m
Dec-2012						
1	20%/20%	AAA to AA-	AAA to AA-	Aaa to Aa3	251.2	244.4
2	20%/50%	A+ to A-	A+ to A-	A1 to A3	703.2	281.6
3	20%/50%	BBB+ to BBB-	BBB+ to BBB-	Baa1 to Baa3	5.4	5.4
4	50%/100%	BB+ to BB-	BB+ to BB-	Ba1 to Ba3	0.0	0.0
5	50%/100%	B+ to B-	B+ to B-	B1 to B3	0.0	0.0
6	150%/150%	CCC+ and below	CCC+ and below	Caa1 and below	0.0	0.0
Unrated	20%/50%	Unrated	Unrated	Unrated	0.0	0.0
Total					**959.8**	**531.4**
Dec-2011						
1	20%/20%	AAA to AA-	AAA to AA-	Aaa to Aa3	777.7	721.0
2	20%/50%	A+ to A-	A+ to A-	A1 to A3	571.4	298.3
3	20%/50%	BBB+ to BBB-	BBB+ to BBB-	Baa1 to Baa3	0.1	0.1
4	50%/100%	BB+ to BB-	BB+ to BB-	Ba1 to Ba3	100.9	100.9
5	50%/100%	B+ to B-	B+ to B-	B1 to B3	0.0	0.0
6	150%/150%	CCC+ and below	CCC+ and below	Caa1 and below	62.7	62.7
Unrated	20%/50%	Unrated	Unrated	Unrated	0.0	0.0
Total					**1,512.8**	**1,183.0**

[1]- Mitigation recognises the benefit of collateral held against these investments – see Section 5.8.2Credit Risk Mitigation: Wholesale

5.4 Commercial Credit Risk

The Group's commercial credit risk relates to loans to businesses secured against both commercial and residential properties. The risk is that circumstances emerge such that counterparties fail to meet loan payment obligations when they fall due, resulting in financial loss.

The Group's exposure to commercial credit risk can be broken down distinctly into two parts; one portfolio consists of a small number of large value loans and the other a more granular portfolio of lower value. As the two portfolios are viewed as fundamentally different, they are managed and assessed for risk as such.

Credit risk mitigation for commercial exposures is managed by the Group's Wholesale and Commercial Credit Committee. It does this by the agreement and setting of a commercial lending policy which is agreed by both Wholesale and Commercial Credit Committee and Group Risk Committee and reviewed on an annual basis. This lending policy provides a mandate to manage both the existing exposures on the book and creates a structure for new business approval; dependent on the loan size requested, loans will be reviewed by individual commercial credit risk managers, the Commercial Sanctioning Committee or Wholesale and Commercial Credit Committee accordingly.

A management information pack is produced on a monthly basis and presented to the Wholesale and Commercial Credit Committee. This pack includes:

- A performance summary of the portfolio
- A sample review of any notable loans
- Analysis of risk characteristics of the portfolio
- Report of exposures by sector

5.5 Securitisation

In 2011 and 2012, the Group successfully issued securitisations under the ‘Brass’ programme. This is an issuance rather than an investment, and the strategy for launching Brass was to benefit from attractive funding rates and the structure was not intended to achieve significant transfer of credit risk away from the Group. The risk relating to the underlying mortgage pool therefore remains with the Group and is included in the ‘secured on real estate’ sections detailed in this document. There are no specific capital requirements for Brass No. 1 plc. or Brass No. 2 plc. Note 35 in the Annual Report and Accounts gives more information on the Brass programme.

The Group’s exposure is to purchased securitisation positions, including resecuritisations (which is defined as a securitisation instrument where at least one of the underlying exposures is itself a securitisation). The majority of this exposure is to UK residential mortgage-backed securities (RMBS) which accounts for £135m of the £196m portfolio. The UK RMBS were all rated AAA at issuance and rank in the senior positions in the capital structure. The following table illustrates the breakdown of investment by type:

Table 12 - Securitised Assets by Investment Type	Exposure Values	
£m	Dec-2012	Dec-2011
CDO	4.9	10.0
CLO	28.0	28.9
Credit Fund	0.0	6.2
Principal Protected Note	10.6	9.5
UK Prime RMBS	134.5	568.1
Synthetic CDO	18.3	15.1
Total	**196.3**	**637.8**

Exposures to securitisations are managed through the Wholesale and Commercial Credit Committee, which receives updates from a separate monthly meeting that specifically considers securitisations. This meeting considers all risks associated with securitisation and resecuritisation holdings, including the quality and seniority of underlying exposures (both primary instruments in portfolios and constituent securitisations that form part of a resecuritisation), along with monitoring the changes in the risks associated with these holdings.

For the purposes of generating risk weightings for its investments in securitisations, YBS uses Standard and Poor's (S&P), Fitch and Moody's as External Credit Assessment Institutions (ECAIs), using a composite rating where a counterparty is rated by more than one agency. Risk weights are calculated under the standardised approach. The following table shows the Group's aggregate exposure to purchased securitisations, split by their associated credit quality steps:

Table 13 - Securitised Asset Exposure Credit Quality Steps
Dec-2012

Credit Quality Step	Risk Weight	S & P rating	Fitch rating	Moody's rating	Exposure values £m
1	20%	AAA to AA-	AAA to AA-	Aaa to Aa3	129.7
2	50%	A+ to A-	A+ to A-	A1 to A3	31.8
3	100%	BBB+ to BBB-	BBB+ to BBB-	Baa1 to Baa3	0.0
4	350%	BB+ to BB-	BB+ to BB-	Ba1 to Ba3	8.2
5	Deducted	B+ and below	B+ and below	B1 and below	18.2
Total					**187.9**

Table 13 - Resecuritised Asset Exposure Credit Quality Steps
Dec-2012

Credit Quality Step	Risk Weight	S & P rating	Fitch rating	Moody's rating	Exposure values £m
1	40%	AAA to AA-	AAA to AA-	Aaa to Aa3	0.0
2	100%	A+ to A-	A+ to A-	A1 to A3	2.2
3	225%	BBB+ to BBB-	BBB+ to BBB-	Baa1 to Baa3	0.0
4	650%	BB+ to BB-	BB+ to BB-	Ba1 to Ba3	1.3
5	Deducted	B+ and below	B+ and below	B1 and below	4.9
Total					**8.4**

Table 13 - Securitised Asset Exposure Credit Quality Steps
Dec-2011

Credit Quality Step	Risk Weight	S&P rating	Fitch rating	Moody's rating	Exposure values £m
1	20%	AAA to AA-	AAA to AA-	Aaa to Aa3	563.0
2	50%	A+ to A-	A+ to A-	A1 to A3	28.7
3	100%	BBB+ to BBB-	BBB+ to BBB-	Baa1 to Baa3	0.0
4	350%	BB+ to BB-	BB+ to BB-	Ba1 to Ba3	0.0
5	1250%	B+ and below	B+ and below	B1 and below	26.4
Total					**618.1**

Table 13 - Resecuritised Asset Exposure Credit Quality Steps
Dec-2011

Credit Quality Step	Risk Weight	S & P rating	Fitch rating	Moody's rating	Exposure values £m
1	40%	AAA to AA-	AAA to AA-	Aaa to Aa3	0.0
2	100%	A+ to A-	A+ to A-	A1 to A3	2.3
3	225%	BBB+ to BBB-	BBB+ to BBB-	Baa1 to Baa3	6.1
4	650%	BB+ to BB-	BB+ to BB-	Ba1 to Ba3	1.3
5	Deducted	B+ and below	B+ and below	B1 and below	10.0
Total					**19.7**

5.6 Impairment Provisions

5.6.1 Loans and Advances to Customers

At each statement of financial position date the Group assesses whether or not there is objective evidence that individual financial assets (or groups of financial assets with similar credit characteristics) are impaired. In determining whether an impairment loss should be recognised, the Group makes judgements as to whether there is any evidence indicating a measurable decrease in the present value of cash flows expected from a financial asset or group of financial assets, resulting from an event (or events) that have occurred after initial recognition of the asset, but before the statement of financial position date.

Individual assessments are made of all loans and advances on properties which are in possession or in arrears by two months or more or where specific circumstances dictate that individual provisions are appropriate. All other loans and advances are grouped according to their credit characteristics and a collective review is undertaken of any evidence of impairment. Future cash flows are estimated on grouped credit characteristics in all cases.

Where there is objective evidence of impairment or that trigger events exist at the statement of financial position date, then the impairment loss is calculated as the difference between the assets' carrying value and the present value of the estimated cash flows from those assets. In assessing these cash flows a number of factors are taken into account, including the Group's historic default experience, historic and current loss emergence periods, the effect of changes in house prices and adjustments to allow for ultimate forced sales discounts.

Any increases or decreases in projected impairment losses are recognised through the Income Statement. If a loan is ultimately uncollectable, then any loss incurred by the Group on extinguishing the debt is written off against the provision for loan impairment. Any subsequent recoveries of amounts previously written off are recognised through the Income Statement as an adjustment to the loan impairment provision. If, in a subsequent period, the extent of impairment loss decreases, and that decrease can objectively be related to an event occurring after the initial impairment was recognised, then the impairment provision is adjusted accordingly and the reversal recognised through the Income Statement.

The following table shows the past due loans and provisions for impaired exposures (equivalent to value adjustments) and charges to the income statement for the year ended 31 December 2012:

Table 14 - Loans Secured on Real Estate Property (£m) **Exposures not subject to Fair Value**	**Total** **Dec-2012**	**Total** **Dec-2011**
Neither past due nor impaired	**17,602.6**	**16,186.2**
Past Due		
Up to 3 months	810.2	622.5
3 to 6 months	162.2	193.1
6 to 12 months	81.4	107.2
Over 12 months	32.1	38.8
Possessions	40.0	48.7
Total past due	**1,125.9**	**1,010.3**
Total exposures	**18,728.5**	**17,196.5**
Provisions	**48.0**	**60.7**
Charge(/ credit) for the year	**25.3**	**30.1**
Fair Value Held	**0.0**	**0.0**

Table 14 - Loans Secured on Real Estate Property (£m) **Exposures subject to Fair Value**	**Total** **Dec-2012**	**Total** **Dec-2011**
Neither past due nor impaired	**8,739.8**	**9,665.9**
Past Due		
Up to 3 months	498.9	495.0
3 to 6 months	73.5	105.8
6 to 12 months	31.9	53.5
Over 12 months	13.7	22.7
Possessions	29.9	34.5
Total past due	**647.9**	**711.5**
Total exposures	**9,387.7**	**10,377.4**
Provisions	**14.1**	**0.0**
Charge(/ credit) for the year	**14.0**	**0.0**
Fair Value Held	**216.7**	**235.0**

Table 14 - Loans Secured on Real Estate Property (£m) All Exposures	Total Dec-2012	Total Dec-2011
Neither past due nor impaired	**26,342.4**	**25,852.1**
Past Due		
Up to 3 months	1,309.1	1,117.5
3 to 6 months	235.7	298.9
6 to 12 months	113.3	160.8
Over 12 months	45.8	61.5
Possessions	69.9	83.2
Total past due	**1,773.8**	**1,721.9**
Total exposures	**28,116.2**	**27,574.0**
Provisions	**62.1**	**60.7**
Charge(/ credit) for the year	**39.3**	**30.1**
Fair Value Held	**216.7**	**235.0**

The amounts shown as past due represent the full amount of the loan outstanding, not just the amount that is past due. The assets acquired with the Chelsea and N&P were subject to a number of significant adjustments to reflect their "fair value" rather than the value at which they were recorded in Chelsea or N&P's own records; i.e. as if they had been acquired, individually, by YBS in standalone transactions. This included an adjustment to reflect the amount that the Group expects to lose, at any point in the future, through borrower defaults. This approach is different to that for the existing mortgage assets where only currently impaired loans can be taken into account. The effect is, provided the estimate of future losses is accurate, that any future losses on these assets will not be reflected in the income statement – it is equivalent to bringing forward future loan loss provisions charges to the effective merger date. These are illustrated in the table showing 'Exposures subject to Fair Value'.

The following table summarises the movement during the year in impairment provisions. Further information on the charge to the income statement for provisions and more detailed analysis is included in note 9 to the Annual Report and Accounts:

Table 15 - Individual/Collective Provisions Past due loans and provisions for impaired exposures £m	Individual provisions	Collective provisions	Total
Balance at 31 Dec 2010	**54.0**	**4.5**	**58.5**
Charge for the year	32.5	3.5	36.0
Write offs	(33.8)	0.0	(33.8)
Balance at 31 Dec 2011	**52.7**	**8.0**	**60.7**
Charge for the year	42.1	(1.7)	40.4
Write offs	(39.0)	0.0	(39.0)
Balance at 31 Dec 2012	**55.8**	**6.3**	**62.1**

The interest arising from the unwind of the discount of expected future recoveries is not material.

5.6.2 Debt Instruments

At each statement of financial position date the Group assesses whether or not there is objective evidence that individual debt instruments are impaired. In determining whether there is any objective evidence of impairment the Group takes into account a number of factors including:

- Significant financial difficulties of the issuer or obligor.
- Any breach of contract or covenants.
- The granting of any concession or rearrangement of terms.
- The disappearance of an active market.
- Any significant downgrade of ratings.
- Any significant reduction in market value.

In some cases a significant adverse change in one of the above factors will cause the Group to determine that there is objective evidence of impairment. In other cases it may not be possible to identify a single event that identifies impairment. The Group may additionally determine that there is impairment where there are a number of factors contributing to that view.

Where the Group determines that there is objective evidence of impairment or that trigger events exist at the statement of financial position date, then, in the case of available for sale instruments, the cumulative loss that had been recognised directly in reserves is removed from reserves and recognised in the Income Statement. In the case of held to maturity instruments an appropriate charge is made to the Income Statement.

If in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be related to an event occurring after the impairment loss was recognised through the Income Statement, the impairment loss shall be reversed, with the amount of the reversal recognised through the Income Statement.

As at 31 December 2012, none of the wholesale exposures were either past due or impaired and there are no assets that would otherwise be past due or impaired whose terms have been renegotiated.

The Group evaluates among other factors, the normal volatility in valuation, evidence of deterioration in the financial health of the investee, industry and sector performance and operational and financing cash flows.

At the statement of financial position, the Group had an impairment provision of £12.9m on wholesale investments relating to cash collateralised debt obligations, as shown in note 9 to the Group's Annual Report and Accounts.

5.7 Credit Risk Concentrations

As a UK residential mortgage lender, the Group is inevitably concentrated in this market. Within this overall concentration however, the Group has put in place controls to mitigate undue concentration risk.

For residential mortgages, the Group Retail Credit Committee monitors the overall characteristics of loan portfolios, including:

- Indexed LTV concentrations
- Concentrations within specific segments of the portfolio such as non-standard lending
- Geographic locations

The Board does not believe any undue concentrations of risk exist in the retail portfolio. Further detailed analysis of geographic, LTV and buyer type concentrations is included within note 39 to the Annual Report and Accounts.

Policy limits have also been set to enable the management of wholesale credit risk concentrations. These limits are actively monitored and relate to aggregate counterparty, country and asset class exposures.

5.8 Credit Risk Mitigation

The Group uses a range of techniques to reduce credit risk of its retail and wholesale lending. The most basic of these is performing an assessment of the ability of a borrower to service the proposed level of borrowing without distress, and further details of the tools used to perform this assessment are contained in section 5.2. However, the risk is further mitigated by obtaining collateral for the funds advanced.

5.8.1 Retail (Loans to Individuals Secured on Real Estate Property)

Residential property is the Group's main source of collateral and means of mitigating credit risk inherent in its residential mortgage portfolios. All current mortgage lending activities are supported by an appropriate form of valuation using either an independent firm of valuers (except historical low LTV re-mortgage cases valued without independent valuation) or indexed valuation for further advances.

All residential property must be insured to cover property risks, which may be through a third party. Additional protection is also afforded to borrowers through optional payment protection insurance.

5.8.2 Wholesale

Collateral held as security for wholesale assets is determined by the nature of the instrument. Loans, debt securities, treasury and other eligible bills are generally unsecured with the exception of securitisation positions and similar instruments, which are secured by pools of financial assets.

The Group's legal documentation with its counterparties for derivative transactions grants legal rights of setoff for those transactions. Accordingly, for credit exposure purposes, negative market values on derivatives will offset positive market values on derivatives with the same counterparty in the calculation of credit risk, subject to a minimum absolute exposure of zero by counterparty.

International Swaps and Derivatives Association (ISDA) documentation confers the ability to use designated cash collateral to set against derivative credit exposures in the event of counterparty default. Frequent rebalancing of the collateral requirements reduces the potential increase in future credit exposure. For such collateralised exposures, the posting of collateral reduces the impact of the current market value to the difference between the market value of the derivatives and the value of the collateral. This difference is limited by the operational use of "thresholds" and "minimum transfer amounts", which set criteria to avoid the movement of small amounts of collateral.

5.9 Counterparty Credit Risk for Derivative Contracts

The Group uses derivative instruments to hedge interest rate risk, foreign currency risk or other factors of a prescribed description arising from fixed rate mortgage lending and savings products, funding and investment activities. Derivatives are only used by the Group in accordance with the Building Societies Act 1986. This means that such instruments are not used in trading activity or for speculative purposes.

Counterparty credit risk in the context of this disclosure is the risk that a counterparty to a derivative instrument could default before the final settlement of the transaction's cash flows.

As described in section 5.7, risk is mitigated by offsetting the amounts due to the same counterparties ("Netting benefits") and by cash deposited by certain of the counterparties ("Collateral held"). The following table shows the exposures to counterparty credit risk for derivative contracts at 31 December 2012:

Table 16 - Counterparty Credit Risk for Derivative Contracts		
£m	**Dec-2012**	**Dec-2011**
Interest rate contracts	1,051.4	1,194.3
Foreign exchange contracts	643.9	951.2
Other contracts	356.9	366.9
Gross positive fair value of contracts	**2,052.2**	**2,512.4**
Netting benefits	(1,622.5)	(2,087.1)
Netted current credit exposure	**429.7**	**425.3**
Collateral held	(271.9)	(324.5)
Net derivatives credit exposure	**157.8**	**100.8**

The 'other contracts' element mainly reflects funds provided to counterparties as collateral and the collateral heldincorporates the positions that mitigate this exposure.

The net derivatives credit exposure represents the credit exposure to derivative transactions after taking account of legally enforceable netting agreements and collateral arrangements. The net exposure value of derivatives at 31 December 2012 was £251.2m, which includes uplifts for potential future credit exposure under the mark to market method for assessing counterparty credit risk.

6 Significant Risk Categories - Operational Risk

6.1 Operational Risk Overview

YBS has adopted the standardised approach to operational risk, compliant with the requirements set out in BIPRU 6, and has defined operational risk as: "the risk of loss arising from inadequate or failed internal processes, people and systems, or from external events; it includes the risk of non-compliance with laws and regulations, and the risk of internal or external fraud".

This means that for calculation of minimum capital requirements, the Group calculates its average annual income from prescribed business lines over the past three years. Capital is then held to support operational risk for each business line at prescribed rates from 12% to 18% of its average annual relevant income.

For the amount of capital required to be held against operational risks, please refer to section 4.3.3.

There are certain qualitative requirements for the standardised approach to operational risk which the Group has adopted. The key areas are described in more detail in the sections below.

6.2 Operational Risk Framework

Underpinning the Group's approach to operational risk measurement and management is the enterprise-wide risk map. This covers all key risks to which the Group is exposed, including key operational risks, and therefore incorporates the operational risk framework. Each key risk identified is assigned to a risk owner, all of whom are General Managers. As described previously, YBS operates within a three lines of defence model. Each business stream has delegated officials who are responsible for embedding the operational risk framework within their stream. The Group-wide network of business stream officials are supported by a centralised Operational Risk team providing the second line of defence to ensure consistency across the Group.

6.3 Operational Risk Oversight and Governance

Oversight and governance arrangements for the setting and management of a robust operational risk management policy and framework are the responsibility of the Board, Group Risk Committee and the Group Operational and Regulatory Risk Committee. Each committee has defined Terms of Reference allocating their accountability and responsibilities.

6.4 Operational Risk Monitoring and Reporting

In support of the enterprise-wide risk map, the Group has in place a risk dashboard supporting each key risk. These risk dashboards integrate all the available information about a risk, and summarise the status of the risk, identifying:

- Whether a key risk may be changing
- Whether the operational environment is under stress, stable or improving
- Whether key controls relied on to mitigate the risks are operating effectively

Operational risk assessments and operational risk management information are reported to the Board via the monthly board risk report. In addition, there is an operational risk update to the Group Risk Committee every quarter, including review of the enterprise-wide risk map.

A detailed information pack covering each of the following areas is reported to the Group Operational and Regulatory Risk Committee on a monthly basis:

- Operational and Regulatory Risk Map
- Risk Appetite Statements for Operational Risk and Conduct Risk
- Key Risk Indicators
- Operational Risk Losses
- Risk Acceptances and Updates
- Supplier Risk Assessments
- Control Self Assessment Updates
- FSA Activity Update
- Regulatory Risk Update
- Conduct Risk Management Information
- Financial Crime Update
- Fraud and Money Laundering Update
- Business Continuity Update
- Risk Transfer Update
- Information Security and Data Protection Update
- Audit Action Status Update
- Branch Risk Scorecard

7 Other Significant Risks - Pillar 2

7.1 Pillar 2 Overview

As noted in section 4.2, the Group undergoes its Internal Capital Adequacy Assessment Process (ICAAP) at least annually in line with Basel II Pillar 2 requirements. The outcome of the ICAAP is presented within an Internal Capital Assessment document (ICA) and in 2012 was subject to the FSA's Supervisory Review and Evaluation Process (SREP). Following the SREP the FSA set an Individual Capital Guidance (ICG) for the Group.

The process is led by the Financial Planning department, but involves a wide range of personnel from across the Group, including General Management and executive directors. The ICA, including underlying individual risk assessments for material risk categories, is reviewed by General Management, the Group Capital Committee, the Group Risk Committee and the Board.

The purpose of the process is to identify the key risks to which the Group is exposed, and the levels of capital and other financial resources that should be held to meet the Group's risk appetite during a period of severe stress and the extent to which minimum Pillar 1 requirements do not satisfy the findings of the ICA.

The ICA is prepared at a Group level, and at 31 December 2012 identified the following key risk categories:

- Retail Credit Risk (to individuals secured on real estate property)*
- Wholesale Credit Risk*
- Interest Rate Risk
- Pension Risk
- Operational and Fraud Risk*
- Concentration Risk
- Commercial Credit Risk*
- Banking Risk*
- Equity Release Risk*
- Structured Credit Risk*
- Business Risk

** - These risks are Pillar 1 risks that are considered in detail within Sections 5 and 6 of this document.*

In the case of risk categories that have Pillar 1 capital requirements, stress testing is performed on the exposures to determine whether capital is required over and above the Pillar 1 amounts held. For other risks, stress testing determines the level of Pillar 2 capital required to protect against the risk in a severe stress scenario. See below for further details.

Additional capital is required to be held in the form of the "Capital Planning Buffer" which is the result of a stress test that assesses the capital impact of a "severe but plausible" economic downturn on the Group's strategic plan. Further consideration is provided below within the "Capital Planning Stress Test" section.

7.2 Interest Rate Risk

Interest rate risk relates to the impact of repricing of assets/liabilities through interest rate movements. Given the nature of our operations, the resulting inevitability of some degree of exposure and the fact that crystallisation of such positions is a possibility, the Group's risk appetite in this area can be characterised as medium i.e. even in unstressed scenarios some losses are expected.

The Group has a formal structure for managing all its market risks, including interest rate risk, using established risk limits, reporting lines, mandates and other control procedures. This structure is reviewed regularly by Group Asset and Liability Committee ("GALCO"), which is responsible for managing and controlling the balance sheet exposures of the Group. GALCO meets at least monthly and the Board receives monthly summaries of risk positions and GALCO activity.

The Group has four main measures for managing interest rate risk:

7.2.1 Value at Risk (VaR)

VaR is a risk management tool which evaluates the potential losses that may be incurred as a result of movements in market conditions over a specified holding period and to a given level of confidence. The model used is based on a 10 day holding period and a 99% confidence level.

The VaR model calculates potential movements in market prices by reference to market data from the last 90 days and incorporates underlying risk factors based on historic interest rate volatilities and correlations.

VaR for the Treasury portfolios is calculated and reported on a daily basis and for the Group Statement of Financial Position on a monthly basis. A quarterly back test of the VaR model is performed to test the validity of the assumptions and parameters within the model.

A number of limitations should be considered in relation to the VaR model:

- Historic data is not necessarily a good guide to future events.
- The model, by definition, does not capture potential losses outside the 99% confidence level, particularly those events that are extreme in nature.
- VaR is calculated on the basis of exposures outstanding at the close of business and, therefore, does not necessarily reflect intra-day exposures.

VaR measures are based upon full balance sheet positions excluding the investment of the Group's free reserves.

7.2.2 Structural Risk Analysis (Basis Risk)

An analysis of interest bearing items by rate type is performed to illustrate key areas of structural mismatch. It identifies mismatches between administered rates, fixed rates and other rates including those linked to Bank Base Rate and LIBOR.

The effect of LIBOR mismatches within the Statement of Financial Position is measured as the impact on net interest income (for a 12 month rolling period) of an isolated increase in LIBOR of one basis point (0.01%).

7.2.3 Basis Point Value (BP) Sensitivity

This measure calculates the change in value of the assets and liabilities resulting from a one basis point parallel shift in interest rates. Within the Treasury portfolio this is calculated and reported on a daily basis separately for each currency and at the full statement of financial position level on a monthly basis.

7.2.4 Repricing Gap Analysis

Repricing dates are analysed, primarily to avoid repricing risk concentrations – the situation where too great a proportion of the Group's assets and liabilities see the interest rates earned or charged on them resetting within a given time period. The aim is to prevent excessive volatility in the net interest margin that could arise if rates shifted adversely within a given time period, and since the Group cannot dictate interest rate movements themselves, the best approach is to limit the amount of assets or liabilities that are exposed in this way. The analysis identifies the net asset/liability repricing position across a series of time intervals. Positions are calculated using nominal amounts and exclude interest flows. General reserves, fixed assets and other liabilities are classified as having 'non-specific' repricing characteristics with a zero rate of interest.The measure is calculated as a reverse cumulative gap.

7.2.5 Stress Testing

For assessment of capital requirements, YBS models its interest rate exposure in three areas: mismatch risk (i.e. in relation to the repricing gap mentioned above), prepayment risk (i.e. the risk that through higher or lower than anticipated prepayment rates further mismatches are generated between the underlying balance and the associated funding) and basis risk. This stress testing involves the consideration of a range of upward or downward rate shocks and forms part of the ICAAP.

7.2.6 Interest Rate Risk Summary

The interest rate risk exposures through 2012 were as follows:

Table 17A - Interest Rate Risk Summary	**2012**			
£m	**Dec-2012**	**Average**	**Maximum**	**Minimum**
VaR	2.9	3.1	5.5	0.8
Basis risk	0.2	0.0	0.2	0.0
BP sensitivity (1bp)	0.3	0.1	0.3	(0.1)

Table 17A - Interest Rate Risk Summary	**2011**			
£m	**Dec-2011**	**Average**	**Maximum**	**Minimum**
VaR	4.2	3.5	7.6	0.7
Basis risk	0.1	0.0	0.1	(0.1)
BP sensitivity (1bp)	(0.1)	(0.1)	0.0	(0.1)

Table 17B - Interest Rate Risk Summary	**2012**		
£m	**> 1 year**	**> 5 year**	**> 10 year**
Repricing gap	(1,582)	(103)	(8)

Table 17B - Interest Rate Risk Summary	**2011**		
£m	**> 1 year**	**> 5 year**	**> 10 year**
Repricing gap	25	(5)	(12)

7.3 Pension Obligation Risk

The Group is exposed to pension risk through its two defined benefit schemes (the YBS scheme and the former Norwich & Peterborough Building Society scheme that was inherited on merger in November 2011) i.e. it has contractual obligations which vary through causes outside of its control. Both schemes are closed to new members, but a material degree of risk remains through obligations already in place. This means that whilst the risk appetite here is low, this is not reflected in the scale of risk already in place. This is mitigated by the closure of the scheme to new members and the intention to hedge the risks involved as far as it is sensible to do so.

The risk has been modelled, with the help of external actuaries, by identifying the key factors likely to affect future obligations to fund the existing liabilities, namely:

- Interest rates (the AA corporate bond yield)
- Implied inflation rates
- Life expectancy assumptions; and
- Asset values.

YBS has taken these assumptions and stressed them severely to assess the quantity of Pillar 2 capital requirement for pension obligation risk.

7.4 Concentration Risk

The Group routinely considers concentrations in products, geographies, channels, income streams and funding sources as part of its strategic planning and has stress tested any such concentrations as part of the ICAAP. A degree of concentration risk is inevitable given the Group's focus in the UK residential mortgage market.

Details of the controls in place to mitigate concentration risk in the mortgage portfolio are discussed within section 5.7 of this document.

7.5 Business Risk

Consideration is given to the risk that the Group is unable to pursue its short term business plan or longer term strategy. This includes the impact of shifts in the economic, market or regulatory environment that could fundamentally impact on the Group's key income statement and balance sheet metrics. It can include, for example, the impact of credit ratings downgrades on the Group's ability to raise funding at planned levels and cost.

7.6 Capital Planning Stress Test

A Capital Planning Buffer has been generated from the results of the Capital Planning Stress Test. This stress test is defined and articulated with the assistance of key business experts and is set at a severity level that is consistent with the FSA's "severe but plausible" requirement.

The test calculates the impact to both capital requirements and resources across the strategic planning period. Based upon the results (after management actions are considered) an additional amount of capital is held above the proposed regulatory minimum. This Capital Planning Buffer can, in extreme times of stress, be absorbed without breaching the regulatory minimum.

7.7 Other Risks

After detailed stress testing, no other risks were considered material from a capital perspective as part of the most recent ICAAP submission.

Glossary of Terms

Basel II Framework	The Basel Committee on Banking Supervision's statement of best practice that defines the methods by which firms should calculate their regulatory capital requirements to retain enough capital to protect the financial system against unexpected losses. The Accord is structured around Pillars 1, 2 & 3, became law in the EU Capital Requirements Directive, and was implemented in the UK in the FSA Handbook.
BIPRU	The Prudential Sourcebook for banks, building societies and investment firms which forms part of the FSA Handbook for Basel II.
Counterparty Credit Risk	Counterparty credit risk is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows.
CQS (Credit Quality Steps)	A credit quality assessment scale as set out in BIPRU 3.4 (Risk weights under the standardised approach to credit risk) and BIPRU 9 (Securitisation).
Credit risk	The potential to incur losses from the failure of a borrower or counterparty to meet its obligation to pay interest or repay capital on an outstanding loan.
Credit risk mitigation	Techniques to reduce the potential loss in the event that a customer (borrower or counterparty) becomes unable to meet its obligations. This may include the taking of financial or physical security, the assignment of receivables or the use of credit derivatives, guarantees, credit insurance, set off or netting.
ECAI	External Credit Assessment Institution. An ECAI (e.g. Moody's, Standard and Poor's, Fitch) is an institution that assigns credit ratings to issuers of certain types of debt obligations as well as the debt instruments themselves.
EEA parent institution	A parent financial institution situated in a Member State of the European Economic Area which is not a subsidiary of another financial institution also situated in the EEA.
FSA	Financial Services Authority. The financial services industry regulator in the UK.
Guarantee	An agreement by a third party to cover the potential loss to a credit institution should a specified counterparty default on their obligations.
ICA	Internal Capital Assessment – the document produced as a result of the ICAAP.
ICAAP	Internal Capital Adequacy Assessment Process. The process the Group follows to determine capital requirements under Basel II Pillar 2.
ICG	Individual Capital Guidance. The minimum amount of capital the Group should hold as set by the FSA under Basel II Pillar 2.
ILAA	Individual Liquidity Adequacy Assessment. The Group's internal assessment of the levels of liquidity that need to be held by the Society to meet its regulatory liquidity requirements.
Interest rate risk	Interest rate risk is the exposure of a firm's financial condition to adverse movements in interest rates.
ISDA	International Swaps and Derivatives Association is the global trade association for over-the-counter (OTC) derivatives, and providers of the industry-standard ISDA documentation.
LIBOR	London Inter-Bank Offered Rate.
LTV	Loan-To-Value. The ratio of current exposure value as a proportion of the value of the asset held as security (usually residential property) expressed as a percentage.
Maturity	The remaining time in years that a borrower is permitted to take to fully discharge their contractual obligation (principal, interest and fees) under the terms of a loan agreement.
Minimum Capital Requirement	The minimum amount of regulatory capital that a financial institution must hold to meet the Basel II Pillar 1 requirements for credit and operational risk.
Netting	The ability to reduce credit risk exposures by offsetting the value of any

	deposits against loans to the same counterparty.
Operational risk	Operational risk is the risk of loss arising from inadequate or failed internal processes, people and systems, or from external events; it includes the risk of non-compliance with laws and regulations, and the risk of internal or external fraud.
PIBS	Permanent Interest Bearing Shares. Unsecured, deferred shares that are a form of Tier 1 capital. PIBS rank behind the claims of all subordinated debt holders, depositors and creditors of YBS.
Pillar 1	The part of the Basel II Framework which sets out the regulatory minimum capital requirements for credit and operational risk.
Pillar 2	The part of the Basel II Framework which sets out the processes by which financial institutions review their overall capital adequacy. Supervisors then evaluate how well financial institutions are assessing their risks and take appropriate actions in response to the assessments. This includes all risks (including Pillar 1 risks) – ICG is an outcome from Pillar 2.
Pillar 3	The part of the Basel II Framework which sets out the disclosure requirements for firms to publish details of their risks, capital and risk management. The aims are greater transparency and strengthening market discipline.
Provisions	Amounts set aside to cover incurred losses associated with credit risks.
Resecuritisation	A securitisation transaction or scheme that includes at least one securitisation within its underlying asset pool.
RWA	Risk weighted assets. The value of an on- or off-balance sheet exposure adjusted under Pillar 1 rules to reflect the degree of risk it presents.
Securitisation	A transaction or scheme where assets are sold to a Special Purpose Vehicle (SPV) in return for immediate cash payment. That vehicle raises the immediate cash payment by issuing debt securities in the form of tradable notes or commercial paper to wholesale investors who receive an income from the underlying assets. Some risk is retained on the balance sheet while the remaining risk is transferred to investors. Securitisations may be purchased or retained.
SREP	Supervisory Review and Evaluation Process, the FSA assessment of a firm's own capital assessment (ICA) under Basel II Pillar 2.
Stress testing	Various techniques that are used to gauge the potential vulnerability to exceptional but plausible events.
Subordinated debt	A form of Tier 2 capital that is unsecured and ranks behind the claims of all depositors, creditors, and investing members (other than holders of PIBS).
The Standardised Approach (credit risks)	The standardised approach to credit risk, calculated by applying varying RWA percentages to credit exposures, depending on the underlying risk.
The Standardised Approach (operational risks)	The standardised approach to operational risk, calculated using three-year historical net income multiplied by a factor of between 12-18%, depending on the underlying business being considered.
Value at Risk (VaR)	A statistical technique to estimate the maximum loss that could be made for a given factor of confidence over a set time horizon under normal market conditions.