TUARASCÁIL ón gComhchoiste Fiosrúcháin i dtaobh na Géarchéime Baincéireachta

An tAcht um Thithe an Oireachtais
(Fiosrúcháin, Pribhléidí agus Nósanna Imeachta), 2013

REPORT of the Joint Committee of Inquiry into the Banking Crisis

Houses of the Oireachtas
(Inquiries, Privileges and Procedures) Act, 2013

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Ulster Bank
UB: Core Book 56

January 2016

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THEME: B1

Effectiveness of banks' board governance, client relationships and business models

LINE OF INQUIRY: B1d

Adequacy of board oversight over internal controls to ensure risk is properly identified, managed and monitored

Ulster Bank Ireland Limited

Minutes of a Meeting of the Board of Directors of Ulster Bank Ireland Limited
Held on 10th June 2004 at the Nuremore Hotel, Carrickmacross, Co Monaghan

Present

W J Burgess (Chairman)
M J Wilson (Deputy Chairman)
C M McCarthy
M G Torpey
J J McNally
J McDonnell
N Brennan

In Attendance

D J Peacock, Joint Company Secretary
J Collister, Joint Company Secretary

20/04 Apologies

Apologies were received from Mr Bamber.

21/04 Minutes of Previous Meetings

The Minutes of the Meeting of the Board of Directors held on 12th February 2004 were agreed and adopted.

The Minutes of the Meetings of the Sub-Committee of the Board of Directors held on 2nd March 2004 and 29th April 2004 were noted.

22/04 Matters Arising

Minute 3/04

It was noted that the report requested at the last board in relation to mortgages sanctioned outside the normal lending criteria would be covered under agenda item 12.

Minute 10/04

The Chairman referred the board to the Report by the Group Audit Committee Secretary which advised that this Committee had received a report from Group IT at its meeting on 20th May 2004 confirming that the rollout of the RBS Group Enterprise Security System was largely complete and that the Auditors had reviewed the implementation and were content to close off the audit management point.

Minute 19/04

Mr McDonnell advised that IT controls had been strengthened, with the introduction of an automated dual control which cannot be manually overridden. Mr Wilson queried whether customers had been aware that the file had not been processed. Mr McDonnell confirmed that affected customers had been notified but that the bank had not suffered any adverse publicity in connection with the incident.

Minutes of Sub-Committee of the Board on 29 April 2004

In response to a query from Professor Brennan, Mr Torpey briefed on the background to the board approval of an indemnity and various other documentation required in connection with the sale of Langella, a subsidiary of Ulster Bank Ireland Holdings, which had been used to facilitate the Group's exit from a structured finance transaction at the customers request.

23/04 **Chairman's Remarks**

The Chairman noted that Mr Houghton had resigned from the board following his appointment as Director of Development, RBSG Insurance. On behalf of the Board of Directors, the Chairman wished to place on record his gratitude to Mr Houghton for his contribution made to the Board during his term of office as Finance Director and latterly in charge of Integration.

The Chairman commented that at a time where financial institutions are receiving such bad press he had been pleased, when listening to a radio programme recently, to hear the Ulster Bank U First current account, credit cards and switcher mortgages offers being praised.

24/04 **Verbal updates from the Executive**

Mr McCarthy advised the board that both Retail and Corporate Banking & Financial Markets were performing well, with strong volume growth in the business centres and the switcher mortgage product, which was set against a background of net interest margin attrition.

It was noted that there has been an increased focus on fraud detection, following recent activity in this area. Both Manufacturing and Group Regulatory Risk have been concentrating on heightening staff awareness and a new senior fraud appointment has been made.

25/04 **Review of Q1 2004 Performance**

Mr Torpey introduced his report that had been circulated in advance of the meeting, which highlighted the main drivers for underlying income and cost movements relative to budget for the period.

Mr Torpey reiterated Mr McCarthy's view that the business was doing well but that margins were under competitive pressure. Mr Wilson, whilst noting that it was pleasing to see significantly increased market share in a number of areas, queried the proportionate improvement. Mr Torpey confirmed that the trend was positive but cautioned the board against placing too much emphasis on the size on the absolute numbers as the quality of market research data continues to evolve. In responding to a query from Professor Brennan as to the quality of new business Mr Torpey advised that the other banks have such a large market share that there is significant scope to take on new business without the quality of lending suffering. It was noted that all new business is subject to the normal RBS/UB credit control procedures. It was further noted that the reduction in Return on Equity as a function of margin and the mix of business, reflects the increased mortgage book.

After further discussion the report was noted.

26/04 **Board Committees – Matters Arising in Quarter 1 2004**

The Board noted the report from the Secretary to the Group Risk Policy & Controls Committee ("GRP&CC") advising reported regulatory or statutory compliance breaches.

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[redacted] In response to a query from Professor Brennan as to whether staff are required to sign a confidentiality agreement annually, Mr McDonnell advised that whilst a confidentiality agreement is only signed once, on commencing employment, the staff code of conduct is regularly reviewed and staff are required to confirm that they are aware of and adhere to the code of conduct when signing their annual performance appraisal. It was agreed that Mr McDonnell would consider outside of the meeting whether it would be appropriate to include an additional affirmation in relation to confidentiality within the annual performance appraisal sign off going forward.

After further discussion, the minutes of the GRP&CC meetings held during the period were noted.

The Board noted the reports from the Secretaries to the Group Asset & Liability Committee, Group Audit Committee and Group Investment Appraisal Committee.

27/04 **<u>IFSRA Related Matters</u>**

Review of Fees & Charges
Mr Peacock introduced his briefing memorandum in relation to the IFSRA review of fees and charges. It was noted that the bank had received a generic letter which had been sent to all financial institutions, and that a project team has been established by Mr Peacock, working in parallel with Group Internal Audit, to undertake necessary review work. It was further noted that the Irish Bankers Federation is going to establish a sub-committee in relation to the review. Mr Peacock confirmed to the Chairman that, based on current information, he was satisfied that the reporting submission date to IFSRA would be met.

Allegations of Misselling
It was noted that the bank had received a generic letter which had been sent to all financial institutions. Mr McDonnell briefed the board, confirming that comprehensive guidelines are in place, and that review work will focus on ensuring that the sales force have adhered to these rules.

Advertising of interest rates
The board noted that following receipt of a letter from IFSRA about the interest rates appearing on our website, the contents of the website had been amended.

Proposed IFSRA visit
Mr McDonnell briefed the board on the proposed visit by IFSRA commencing 12th July 2004 to review compliance with the Consumer Protection Codes.

28/04 **<u>Banking Licence Project</u>**

The Chairman referred to the project to rationalise the Ulster Bank Group's Republic of Ireland banking licences as part of the integration of Ulster Bank and First Active and the proposal to establish a sub-committee of the Board to avoid undue delay in the event that decisions are required outside of the scheduled board dates.

The Board considered the proposal as outlined by the Chairman and being of the opinion that such a sub-committee would be in the interests of the effective management of the integration project, IT WAS RESOLVED that the sub-committee be, and is hereby, approved and established, and that any two directors, as nominated by the Company Secretary be, and are hereby, authorised to convene the sub-committee as necessary and perform such delegated functions of the Board as may be appropriate in connection with the integration, subject to any restrictions or conditions placed on the sub-committee at any time by the Board.

29/04 Parental Guarantee

It was noted that Ulster International BV, a subsidiary of Ulster Bank Ireland Limited, is to be wound up as part of the continuing project work to rationalise the number of companies in the group. At the date of its last balance sheet this company had net liabilities and the bank was asked by the company's auditors to provide a parental guarantee, to cover this deficit, before the company is placed in voluntary liquidation. It was further noted that as the parental guarantee fell outside the ordinary course of business approval was sought and received from RBS Secretary's Office in accordance with the RBS Group policy and the guarantee issued by Group Secretariat in order to avoid causing undue delay to the liquidation proceedings. The Board considered the request and ratified the issue of the parental guarantee in respect of Ulster International BV for €3,247, in the form submitted to the board meeting.

30/04 High Level Controls Report

There was laid before the meeting a copy of the Ulster Bank Group High Level Controls Document ("HLC") as recently updated and approved by the board of Ulster Bank Limited. This updated version of the HLC, which is referred to in the Board's Terms of Reference, was noted.

31/04 Report on Mortgage Referrals

Mr McDonnell introduced the report which had been requested at the last board (minute 3/04 refers) and confirmed that he was content with the controls in place surrounding sanctioning procedures. Professor Brennan queried the level of sanctions outside limits, especially with regard to those which breached both the loan to value and the debt service ratio limits. In the interests of time it was agreed that Mr McDonnell would meet with Professor Brennan outside the meeting to provide her with additional background in relation to any questions she wished to raise. The Company Secretary agreed to consider whether it would be appropriate for similar reports to be tabled at the Ulster Bank Limited and First Active plc boards.

32/04 Appointment of Corporate Representatives

The Chairman introduced the briefing paper which had been circulated in advance of the meeting which contained a proposal to streamline the procedure for the appointment of corporate representatives to attend meetings of members and creditors, and to bring procedures in the company into line with the practice in Ulster Bank Limited.

After considering the proposal the Board resolved :

a. That pursuant to Section 139 of the Companies Act 1963 any two Directors of the Company, or any one Director and the Company Secretary, for the time being be and are hereby authorised to appoint such person from the staff of the Group as they think fit to act as the representative of the Company:
    - at any meeting of any body corporate of which the Bank is a member or at any meeting of any class of members of any such body corporate; and

- at any meeting of creditors of any body corporate of which the Bank is a creditor.

b. That any person so appointed be and is hereby authorised to exercise the same powers on behalf of the Bank as the Bank could exercise if it were an individual shareholder of the body corporate.

33/04 <u>Effectiveness of Internal Controls under Turnbull Guidance for the quarter ended 31 March 2004</u>

The Chairman introduced the papers that had been circulated in advance of the meeting, noting that the report for the three-month period ended 31st March 2004 had previously been considered in detail by the Group Risk Policy & Controls Committee ("GRP&CC") and subsequently approved on 14th April 2004 by a sub-committee of the Board of Directors of Ulster Bank Limited, on behalf of the Ulster Bank Group.

After discussion the report was noted.

34/04 <u>Powers of Attorney</u>

The following Powers of Attorney were noted as having been issued or cancelled since the last report to Board:

Subject	Issue	Expiry	Granted to:	Granted by:
BBNI to execute any deed or sign any document (full description available on request).	12/2/04	Until revoked, cancelled or annulled by the bank.	Alan Stewart, Henry Elvin, David McCartney, Richard Ennis, Kevin Kingston, Ciaran McAreavey acting jointly and severally.	Judith Collister, Andrew Blair
Business Centres of Ulster Bank Limited to sign commitment letters in respect of lending facilities extended jointed by the Bank and UBL for facilities upto €1.5 million or its equivalent in any other currency.	12/2/04	Until revoked, cancelled or annulled by the bank.	Any two persons of Manager level or above being office holders within the Business Centres of UBL, acting jointly.	Judith Collister, Andrew Blair
Outsourcing Clearing Operations from UBL and UBIL to Electronic Data Systems (Ireland) Limited ("EDSI")	23/3/04	31/5/04	John West, Paul Molumby, of UBIL	Deirdre Shannon, Michael Drew
To execute (1) Loan Agreement re €5 million facility to part fund acquisition of [redacted] amending existing [redacted] revolving credit facility.	22/4/04	30 days	James Lidierth Associate Director, UBIL	Deirdre Shannon, Michael Drew

Party to the Notarial Deed pledging 1,920 shares in the capital of Customer infor...	27/4/04	31/5/04	The following persons working at NautaDutilh N.V. Rotterdan. Veronica Geertruida van den Berg-Vollebregt, Adriana Berdina Cornelia Oskan, Jolette Rianne van Beusekom, Ilse Lucette Marie Wouterse, Josina Henriette Vegter, Stephanie Marie Louise Elisabeth Schoomhoven-Stoot, Elisabeth Jacoba Louwerier-Diepeveen.	Deirdre Shannon, Michael Drew

35/04 Certificate of Incumbency

It was noted that due to the departure of a number of persons previously included on the authorised signatory list for Financial Markets treasury related contracts, a number people needed to be removed from the list of signatories. After discussion the board RESOLVED that Mary McCarroll and Jo Hall be removed from the list of signatories authorised to execute on behalf of the Company any and all contracts relating to the business of the Financial Markets Division approved by resolutions of the board of directors at meetings on 17 June 2002 and 16 July 2003.

36/04 Application of the Company Seal

The Board **RATIFIED** the application of the Common Seal of the Company to 1,751 documents during the period 1st February 2004 to 28th May 2004.

37/04 Sanctions Greater than eq. £20m

The report on sanctions greater than eq.£20m was considered on an exceptions basis and noted.

38/04 Board Dates

The dates for the meetings of the Board of Directors during 2005 were noted as follows:-

Thursday 10th February 2005	George's Quay, Dublin
Thursday 9th or 16th June 2005	To be finalised
Friday 16th September 2005	George's Quay, Dublin
Friday 16th December 2005	George's Quay, Dublin

39/04 Any Other Business

There was no further business and the Chairman declared the meeting closed.

Chairman

Date 10.9.2004

Ulster Bank Ireland Limited

Minutes of a meeting of the Board of Directors of Ulster Bank Ireland Limited (the "**Bank**" or the "**Company**") Held on 12th September 2007 at the Ulster Bank Group Centre, George's Quay, Dublin 2

Directors Present

N Brennan (Chair)	M Bamber
C McCarthy	R Gallagher
J McDonnell	P Nolan (via tele-conference)

In Attendance

J Hickey, Group Financial Controller
J Collister, Joint Company Secretary

45/07 Apologies

Apologies were received from Messrs Bowen and Torpey.

46/07 Minutes of Previous Meetings

The Minutes of the Meeting of the Board of Directors held on 7th June 2007 were agreed and adopted.

The Minutes of the Meeting of the Board of Directors held on 17th August 2007 were noted.

47/07 Matters Arising

Tax Group Relief – Mr Hickey briefed the Board on the current status of discussions with the Revenue Commissioners in respect of tax group relief claims and other outstanding tax issues, with good progress having been made. Board noted management's expectation that this issue would be closed by the year end.

Financial MI – Mr Hickey confirmed to the Board that the production of financial management information by SSF had been restored from July 2007 reporting month end, with Ulster Bank management satisfied as to the quality of reporting. It was noted that SSF were currently undertaking a balance sheet assurance project which would be fundamental in building confidence in the validity of reported figures.

48/07 Chief Executive's Report and Review of Q2 2007 Performance (Management Accounts to 30.6.07)

Agenda Items 5 and 6 were taken together.

Mr McCarthy briefed the Board on the financial performance for the six months to 30th June 2007, with operating profit at €323m, being €9m, 3%, above budget. Board noted that the strong fee income from Capital Markets and Retail Direct had offset underperformance in net interest income arising from margin and volume pressure.

The Board deferred detailed discussion on operational issues at the Dublin Mortgage Centre ("DMC") to agenda item 12, but considered the impact of these issues on customer service levels. The Board noted that the Group was currently responsible for a significant proportion of customer complaints reported to the Financial Regulator relative to the Group's market share, primarily relating to mortgage operations, and this was being closely monitored by the executive within both Ulster Bank and RBS. It was further noted that a new concerns process had been established within DMC and this had recorded a fall in reported concerns in the previous month, but that it would be a number of months before a trend could be established. In view of the level of complaints, and the potential reputational damage associated therewith, the Board requested that a paper be presented to the December 2007 board meeting on customer concerns.

Responding to a query by the non-executives as to why there was not more evidence of the current market turbulence in the financial results, Mr McCarthy explained that the company was benefiting from the endowed effect of its balance sheet. The Board noted that whilst the company was still on target to meet the 6+6 reforecast outturn for the year, trading conditions were expected to be tougher in the second half of the year, with the increased cost of funds and margin pressure from increased competition in the mortgage market starting to come through.

Following a discussion on the company's performance relative to its competitors, during which the Board recognised that the Group was in its first year of a five year strategic plan and that it would take a few years yet to see the real benefits of the current business investment coming through in financial performance, the report was noted.

49/07 **Corporate Migration**

The Chairman welcomed Mr Hayes, Director of Change Management, to the meeting to present to the Board on the corporate migration project.

Mr Hayes referred the Board to the presentation tabled at the meeting and explained that the corporate migration was the last stage in integrating the Ulster Bank systems with the RBS operating platform. This phase had been previously deferred due to the complexities of the corporate systems and would be fundamental in achieving Corporate Markets ambition to be Number One Business Bank. Mr Hayes outlined the benefits to Ulster Bank and its customers, of increased functionality and enhanced competitiveness through a range of more sophisticated product offerings. Mr Hayes went on to explain the key steps in the programme, which would be delivered on a phased basis, completing Quarter 3 2008.

The Board discussed in detail the benefits of the programme, the staffing implications and the preparations, with particular regard to lessons learnt from finance issues experienced following integration in October 2006. The Board, having satisfied itself that these risks were being addressed, and that the programme was being appropriately governed under oversight of the Executive Steering Committee, determined that it was in the best interests of the Group to proceed with the corporate migration and accordingly, RESOLVED:

i. To approve in principle the proposal to extend the material outsourcing of Manufacturing functional responsibilities to RBS Group Manufacturing, to include the migration of the Ulster Bank Group's corporate technology systems to the core RBS Group IT platform and the associated £38.1m investment spend; and
ii. subject to regulatory clearance being received for the proposed material outsourcing, authorise a sub-committee of the Board of Directors, comprising any three directors at the discretion of the Secretary, of which not less than one is to be a non-executive director, to consider and, if thought fit, approve all matters in relation to furthering the corporate technology systems migration.

After discussion the report was noted.

50/07 **Preference Share Dividend**

Mr Hickey referred the Board to the briefing memorandum that had been circulated in advance of the meeting proposing the payment of an interim dividend.

Mr Hickey explained that it was proposed to pay a dividend to Ulster Bank Holdings (ROI) Limited, which would in turn pay a dividend to Ulster Bank (Ireland) Holdings, which would enable this company to pay a dividend to The Royal Bank of Scotland plc ("RBS") on the preference share capital held by RBS in that company.

The Board, having carefully considered the proposal, and satisfied themselves that the company had sufficient distributable reserves to pay the dividend as evidenced by the management accounts to 31st August 2007, RESOLVED that an interim dividend for 2007 of €17m be, and is hereby, approved for payment to the holders of the company's ordinary B shares by a date no later than 30th September 2007 at the discretion of Mr Torpey. In considering this proposal, and in view of the significant amount of capital restructuring over the past year, the Board requested that a capital planning paper be presented to the next meeting in December 2007, summarising the capital movements over the past year and forecasting forward for the following year to set in context the capital plans required to support business growth.

51/07 **Capital Injection**

The Board noted that in light of the current market turbulence it was unlikely that the planned €1.5bn corporate securitisation would proceed this year, which meant the company was likely to require a capital injection in November 2007 to maintain its regulatory capital ratio.

The Board, having considered the proposal, RESOLVED that a sub-committee of the Board of Directors be established, comprising any three directors, at the discretion of the Company Secretary, with authority to consider, and if thought fit, approve all matters relating to a proposed capital injection of up to €200m from Ulster Bank Limited to be transacted by 30th November 2007.

52/07 **Board Committee Reports on matters arising in Q3 2007**

The Board noted the Reports from the Secretaries of the Risk Management Committee ("RMC"), Group Investment Appraisal Committee, Group Audit Committee and the Group Asset and Liability Committee. The reports were taken as read and considered on an exceptions basis.

In response to a query from the Chairman, Mr McDonnell explained the role of the RMC, as the senior risk committee, in approving BASEL models.

Mr Hickey confirmed to the Board that the Shared Services Finance balance sheet quality assurance review referred to in the Group Audit Committee memorandum had commenced on 1 July 2007. The Board noted that the review was expected to be completed by the year end and that nothing of concern had been raised to date.

After further discussion the reports were noted.

53/07 **Mortgages**

Stress Testing Requirements

Mr McDonnell referred the Board to the paper on stress testing of residential mortgages that had been circulated in advance of the meeting.

Mr McDonnell explained that the Financial Regulator had been in consultation with the Irish Mortgage Council regarding revision of guidance on stress testing, the current guidance having been first introduced in 2001. The Board noted that following this consultation, and in light of market developments since that time, the Financial Regulator had issued credit institutions with revised standardised guidance on stress testing of residential mortgages, providing for stress testing at 2.75% above ECB base rate (previous to this, stress testing was carried out at 2% above the standard variable interest rate).

The Board, having considered the impact of the proposal on mortgage operations, and noting that it had been considered and approved by the Group Risk Credit Policy and Strategy Committee, RESOLVED to approve the introduction of stress testing at 2.75% above ECB base rate with effect from 30th September 2007.

Review of Policies/Exemptions

Mr McDonnell briefed the Board on mortgage policies reviewed over the course of the preceding year and mortgage lending approved outside policy by reference to the report that had been circulated in advance of the meeting.

In discussing the lending approved outside policy the Chairman expressed disquiet over the continued high exception rate for lending approved outside the Debt Service Ratio ("DSR") limit, notwithstanding the review undertaken by Credit Risk of the reasons for approval of such loans. Mr McDonnell confirmed to the Board that the level of exceptions continued to be closely monitored and that whilst the DSR exception rate was higher than he would like, he was satisfied with the reasons behind the approvals, and with the quality and experience of the underwriting team. The Board noted that following the increase in exception rate at December 2006 revised guidance had been issued in respect of income level requirements which had resulted in some reduction in exceptions.

The Board went on to discuss the arrears and provisioning performance. The Board noted that the company was being assisted in the management of arrears by specialists from RBS, with arrears levels expected to continue to be impacted by the operational issues at DMC until the year end. The Board requested that future reports include the monetary value of arrears in addition to the value of arrears as a percentage of the mortgage lending portfolio to aid analysis.

After further discussion of the mortgage policies reviewed over the course of the year, the report was noted.

IFSRA inspection of Mortgage Operations at DMC

The Board noted that the Financial Regulator ("FR") had carried out an onsite inspection of First Active plc mortgage operations in DMC. In issuing a letter to First Active plc detailing issues arising from this visit the FR had raised a number of points which were also applicable to Ulster Bank Ireland Limited.

After detailed discussion, during which the executive confirmed that these issues were being addressed, the response to the FR was noted.

Mr Nolan left the meeting at this point.

54/07 Equator Funding Offering

Mr Gallagher introduced the briefing memorandum that had been circulated in advance of the meeting.

Mr Gallagher explained that as part of the Ulster Bank Wealth strategy of providing access to the RBS Asset Management suite of investment products alongside Coutts investors, Ulster Bank Wealth was keen to provide Irish investors with access to the Equator Investment Programme. The Board noted that this is a comprehensive investment offering consisting of a range of long-only (traditional) unit trusts covering the major economic regions and asset classes. The Board further noted that in order for Irish investors to invest in this programme it would be necessary for them to invest through a nominee company. An existing Ulster Bank Group company, FNBS International Limited, had been identified as being suitable for this purpose.

The Board, having carefully considered this proposal, and noting that external legal advice had been received on the operation of the moninee company, RESOLVED:

(i) that the company acquire FNBS Finance International Limited from First Active Holdings Limited; and
(ii) that any two directors, or any one director and the company secretary be authorised to:
 - execute a share purchase agreement to effect the acquisition;

- agree the terms of the nominee services agreement between the company and FNBS Finance International Limited and to execute the agreement on behalf of the company; and
- agree and sign on behalf of the company any necessary shareholder consents as may be required to give effect to the foregoing resolutions.

55/07 **Secretariat Matters**

Adoption of Company Seal

The Board noted that the markings on the current company seal had worn away and that in replacing the seal it was proposed to include the RBS Group "snowflake" design in line with the Ulster Bank Limited company seal.

After discussion the Board RESOLVED that the seal, an impression of which apears in the margin of these minutes, be approved and adopted as the common seal of the company in substitution for the existing company seal of the company with effect from 13th September 2007 and that the die of the existing common seal be destroyed.

Application of Seal

The Chairman referred the meeting to the memorandum detailing the affixing of the Common Seal of the Company, which had been circulated in advance of the meeting and **IT WAS RESOLVED** that the affixing of the Common Seal of the Company to the documents numbered 07/29 to 07/47, as detailed in the memorandum laid before the meeting, be and is hereby ratified.

Register of Powers of Attorney

The following Powers of Attorney were noted as having been issued or cancelled since the last report to Board:

Subject	*Issue*	*Expiry*	*Granted to:*	*Granted By:*
Execution and delivery of documentation re Project [redacted] transaction	5 July 2007	31 July 2007	Declan McGrath, Sean Malone, Philippa Crawford, Dale Williams and Wilson McAlister.	Deirdre Shannon Clare Curran
Execution of Agreements [redacted]	10 August 2007	Midnight 31 October 2007	Gordon Pell	Judith Collister Michael Torpey

56/07 **Analysis of sanctions greater than GBP20m**

The report on sanctions greater than GBP20m was considered on an exceptions basis and noted.

57/07 **Quarterly Risk & Control Assessment Report**

Mr McDonnell briefed the Board on the risks facing the company by reference to the Risk and Control Assessment Report that had been circulated in advance of the meeting.

In discussing the recent significant media attention in respect of the refund of Personal Loan Protector Insurance, the Board noted that the Company still had one significant outstanding refund programme in respect of students which would be commenced shortly.

After further discussion, during which the Board requested that the graph showing risk issues aged analysis be spread out for greater clarity, the report was noted.

58/07 **Liquidity**

Issuance of Certificates of Deposit

Mr Hickey introduced the proposal for the company to launch a certificates of deposit ("CD") programme.

Mr Hickey explained that the Group already had CD programmes in both Ulster Bank Limited ("UBL") and First Active plc ("FA"), but that following a change in legislation it was now possible for private companies in the Republic of Ireland to issue CDs. The Board noted that issuing CDs directly out of the company would reduce its reliance on funding from UBL and thus reduce pressure on the intra-group limit.

The Board, having considered the proposal, determined that this represented a suitable way of raising funding, RESOLVED:

1. That the company launch a Certificate of Deposit Program with effect from Q4 2007 and
2. That the Certificates of Deposit Program shall have a limit of € 5 billion.
3. That any one Director, the Company Secretary, or Mr Donal Corbett be, and is hereby, authorised to approve the terms of the following agreements :
   - Deed relating to uncertificated units of a CREST eligible debt security;
   - Issuing and Paying Agent Agreement;
   - Application documents for CrestCo
   - Corporate Certificate for the Company;
   - Power of Attorney;
   - Agency Agreement;

   Including such additions or amendments to the documentation as they may deem necessary, and to authorise the signature, execution (as a deed or otherwise) and delivery of these documents and any document ancillary to or related to the above documents, or the Certificate of Deposit Program generally, or any additional agreement, notice or other document and take all such other action which may be required to give full effect to the transaction.

4. That the Company Secretary be, and is hereby authorised to sign the Issuer Application form for CrestCo.

Euro Commercial Paper Programme

The Board of Directors of the Bank noted that Ulster Bank Finance plc (**UBF**) established a €5 billion euro commercial paper programme (the **Programme**) on 2 November 2004 and that the maximum limit of the Programme was increased to €8 billion on 30 April 2007. The Directors further noted that the Bank acts as guarantor to UBF's obligations under the Programme pursuant to a resolution by the Board on 8th June 2006, the current maximum limit of the guarantee being set at €10 billion.

Mr Hickey explained that UBF proposed to increase the maximum limit of the Programme from €8 billion to €12 billion and that the maximum limit of the guarantee from the Bank would accordingly need to be increased to €12bn on the terms as outlined in the Programme.

After consideration of the proposal the Board RESOLVED that:

- the increase of the Bank's guarantee of the Programme to a level of €12 billion be approved ; and
- any one Director, the Company Secretary or Mr Donal Corbett, be and is hereby authorised, to approve and execute any and all documentation and take any steps required or desirable to facilitate the increase of the maximum amount of the

Programme and the Bank's guarantee of the Programme".

59/07 Sandyford

The Chairman introduced the proposal to vary the terms of the framework agreement for the sale of Sandyford that had been circulated in advance of the meeting.

The Board noted that the Board of Ulster Bank Limited ("UBL"), at its meeting on 6th September 2007, had approved a variation under the existing framework agreement under which UBL would receive guaranteed sales proceeds of €30m in exchange for removing the overage provision. The Board further noted that as the company leased the property from UBL it was party to the original disposal agreement and must therefore enter into the deed of variation.

After discussion the Board RESOLVED:

(i) to agree to the variation of the framework disposal agreement for Sandyford under which the overage provision would be removed in exchange for increasing the disposal proceeds by €10m; and

(ii) that any two directors, or any one director and the company secretary be, and are hereby authorised, to agree the terms of the variation agreement, in conjunction with the legal advisors, and to execute any documentation required in furtherance of the foregoing resolution.

60/07 Any Other Business

There was no further business and the Chairman declared the meeting closed.

Chairman Niall Bowen

Date 13 December 2007

For Approval

Memorandum to Board for its meeting on 12th September 2007

Proposal for Dividend payment by Ulster Bank Ireland Limited (UBIL)

Background
As part of a capital restructuring of the Ulster Bank Group earlier in the year, RBS Plc injected two issues of Preference shares in Ulster Bank Ireland Holdings (UBIH) for €150m and €435m. Dividends on these Preference shares were paid in June 2007. The next dividends payable will be due on 31 December 2007.

Currently UBIH does not have sufficient distributable reserves to make these dividend payments. It is therefore proposed to pay a dividend from Ulster Bank Ireland Limited (UBIL) to Ulster Bank Holdings (ROI) Ltd (UBHROI) in September 2007. UBHROI will in turn repatriate this dividend payment to UBIH in October 2007 to facilitate payment of UBIH Preference share dividends payable in December 2007.

Proposal
It is proposed to make a €17m Ordinary share dividend payment from UBIL to UBHROI in September 2007. UBIL's capital ratios can facilitate this dividend payment.

Our legal advisors have confirmed that UBIL is entitled to pay a dividend by reference to the most recent audited annual accounts laid before the AGM of the company, or, if these do not show sufficient distributable reserves, such interim accounts as are necessary to enable a reasonable judgement to be made as to the level of distributable profits available.

The August 2007 interim management accounts of UBIL (attached in appendix 1) show that UBIL had distributable reserves of €422m at that date.

On that basis, I am recommending that the Board proposes an interim dividend for 2007 of €17m to be paid to holders of UBIL's ordinary B shares.

Ulster Bank Group Tax have confirmed that there are sufficient excess foreign tax credits in the UK to shelter the tax that would otherwise arise on the repatriation of the reserves to UBHROI (circa. €3m, stg£2m).

Approval
Board is requested to approve an interim dividend for 2007 of €17m to be paid to the holders of UBIL's ordinary B shares, with the dividend to be paid no later than 30th September 2007, at the discretion of Michael Torpey.

Approval has been obtained from UB GALCo.

Michael Torpey
Group Finance Director
29 August 2007

THEME: B1

Effectiveness of banks' board governance, client relationships and business models

LINE OF INQUIRY: B1e

Appropiateness, management and control of Client Relationship activities

Ulster Bank

Ulster Bank Ireland Limited

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STRICTLY PRIVATE & CONFIDENTIAL
Ciarán Lynch, T.D.,
Chairman,
Joint Committee of Inquiry into the Banking Crisis
Leinster House
Dublin 2
By e-mail: biwitnessmanager@oireachtas.ie

2 March 2015

Re: Ulster Bank Ireland Limited ("UBIL")
Ref: [UBI-i-02a]

Delivery of documents pursuant to the Direction to give documents pursuant to Section 67(1) of the Houses of the Oireachtas (Inquiries, Privileges and Procedures) Act 2013 (the "Act")

Additional information sought on voluntary basis

Dear Chairman,

I refer to your letter of 19 February 2015 with respect to the above matter.

Insofar as your request is concerned, I confirm that UBIL, Ulster Bank Limited ("UBL") or First Active plc ("FA") (collectively "UBG") did not, for the relevant period (2004-2010) hold central registers for:

(i) corporate hospitality/entertainment/marketing (or equivalent) recording such activities provided to Clients/Contacts in the Property Sector and/or Government Departments or other State Bodies and Organisations, to include politicians; or,

(ii) all Hospitality / Gifts received by Staff in excess of €250.

I also confirm that UBG did not have a central policy in relation to the items at (i) and (ii) above or maintain a list of breaches. UBG did however have a Code of Conduct in the relevant period (the "Code") which included guidance on the acceptance of gifts by employees as well as the offering and acceptance of Hospitality. A copy of an extract from the Code as at 31 January 2006 is included with this submission which sets out the position in relation to Gifts and Hospitality.

Corporate hospitality / entertainment / marketing was undertaken by UBG in the relevant period. However, given the lack of a central register, it is not possible to identify with any specificity the information requested by the Inquiry.

In the period in question, for example, UBIL and FA within the Republic of Ireland and UBL in Northern Ireland, were involved and / or participated in various sponsorship initiatives, including:

- the RBS Six Nations Rugby Tournament;
- the Ulster Bank GAA Football Championship;
- The European Open Golf Tournament;
- the Ulster Bank Belfast Festival at Queens; and,
- the Ulster Bank Dublin Theatre Festival.

As part of these sponsorships, various clients and/or contacts in the property sector received event tickets and / or corporate hospitality including event tickets; however, as indicated above, no central register was maintained during the period.

On occasion, reports of marketing and sponsorship activities were prepared and, to the extent that they exist in the years 2004-2008, examples of same can be found in the board papers already furnished to the Inquiry in tranches 1 and 2.

Since July 2011 UBIL and UBL maintain a register of corporate hospitality in respect of corporate hospitality provided to clients as well as invitations received by UBIL and UBL staff to attend events hosted by clients and suppliers.

Should you have any queries in respect of the above, please do not hesitate to contact me.

Yours sincerely,

Bobbie Bergin
Company Secretary
UBIL

Encl/

Gifts and Hospitality

The aim of the Group's Gifts and Hospitality policy is to avoid prejudicing your objectivity, for instance, when a contract is in the course of negotiation.
The policy applies to gifts and hospitality received from or offered to customers, suppliers and other business contacts and is designed to avoid situations where a customer or supplier may seek to influence you. The policy also takes account of the law relating to the offering of gifts and hospitality to local authorities and other public bodies.

- Gifts
- Hospitality - Offering and Accepting
- Recording Gifts and Hospitality

Gifts

Small gifts - impersonal items of minimal financial value and often of a promotional nature such as a diary - from customers or suppliers (actual and potential) can be accepted and kept. Other gifts cannot be accepted without approval from your manager.
To avoid causing offence, you should explain to the person offering the gift that you are bound by the Group's policy on accepting gifts.
On no account should you accept gifts that by their nature have the potential to cause reputational damage or embarrassment to the Group. This may include cash, cash-convertible gifts or any payment, favour or inducement that might improperly influence an official transaction.
Back to top

Hospitality - Offering and Accepting

The majority of employees are **not** authorised to offer Group hospitality to customers, suppliers or other business contacts, or to accept any hospitality offered.
Where entertaining is essential to your role you may be authorised by line management to offer or accept hospitality. If you are offering hospitality you must operate within your approved budget for hospitality. If you are offering or accepting hospitality you must adhere to the following guidelines.
Any hospitality offered or accepted must be appropriate to the Group's business interests and should not be excessive as regards any contact, customer, supplier or other third party.
A common sense approach should be taken as to what is 'appropriate' or 'excessive', but the following principles must be borne in mind:

- The hospitality must not be allowed to develop into an inappropriate personal relationship, for example, where a host provides special discount arrangements for Group employees
- Your manager must be kept informed of the social aspects of a business relationship through normal reporting procedures
- Your manager must have given prior approval or general authorisation
- General authorisation is appropriate for business related hospitality, including working lunches that take place during business meetings, and for formal or professional functions such as those organised by the Institute of Bankers, by accountants or by chartered surveyors
- Specific authorisation by a senior manager is required for events such as a day at the races, Ascot, Wimbledon, Open Golf, International football or rugby matches and sporting occasions generally. The Group will not reimburse any gambling expenses incurred at such events

- In no event should hospitality be offered (or accepted), which by its nature (for instance "adult' entertainment) or scale (such as a trip overseas to the World Cup) has the potential to cause reputational damage or embarrassment to the Group
- In the case of potential customers or suppliers, your manager must have given prior approval or a general authorisation in line with the principles set out above. It is also essential that the manager is accurately briefed to prevent any suggestion that a Group employee has been unduly influenced
- When accepting hospitality, the donor is present in order to avoid situations where hospitality is offered solely as a gift rather than entertaining. Employees must not accept corporate membership of such organisations as sports clubs, health clubs, golf clubs, gyms or private clubs from a customer or other business contact.

Recording Gifts and Hospitality

Some Group employees are required to record all offers and receipts of gifts or hospitality. You will be personally informed by your manager if you are subject to this requirement and advised as to the duties and recording procedures that are in place in your business area.

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Page updated: 31 January 2006

Travel and Entertainment Expenses

Our Travel and Expenses policy sets out a common approach for all parts of the Group for managing business travel and controlling its associated costs.

If your role involves business travel you must familiarise yourself with the full terms of this policy.

When business travel is necessary, you should follow the principles of this policy and balance costs and time out of the office against the reason for travelling. At all times, you should strive for best value for money under advice from the Group's appointed agents.

For further information please speak to your manager, or refer to the Travel and Expenses Policy.

Page updated: 31 January 2006

THEME: B2

Effectiveness of banks' credit strategies and risk management

LINE OF INQUIRY: B2a

Appropriateness of property-related lending strategies and risk appetite

ULSTER BANK LIMITED

Minutes of the meeting of the
Group Asset & Liability Committee on 29 April 2004

Present:	**In attendance:**
M Torpey (Chairman)	P Leverick
G Murray	C Baird
M McKavanagh	M Irwin
G Brown	I Tyler
P Meahan (as alternate to P Wilson)	D Kissane
J McNamara (as alternate to A J McKeon)	C Kelly (Secretary)
	S Groarke

1) Apologies

Apologies were received from John McDonnell, A J McKeon, John McNally, Dom Williams, Michael Bamber, Olga Breen , Peter Wilson, David Morrison and Des Fitzgerald.

2) Minutes

The minutes of the meeting held on 31 March 2004 were agreed and adopted.

3) Matters Arising

Issue Log

➢ **IAS 39 Hedging & Measurement** See agenda item 7.1
➢ **UBG/First Active Integration – Include as Standing Item on GALCO Agenda** See agenda item 7.3
➢ **Concentration of Sectoral Exposures** Provide GALCO with update on status of request to IFSRA for dispensation of UBIL Belfast Branch from Property Sector Exposure requirement – UBIL near sectoral limits at end of March. IFSRA unlikely to give UBIL an exemption in the near future. Reliable Commercial Lending growth figures required from the business. Additional risk transfers required by end of April. RBS GALCo may need to approve increased limits for UBIL.
➢ **Include UBIL's actual sectoral concentration to Property sector within Monthly Briefing Pack (calculated on a quarterly basis)** Now included in the GALCo pack. Matter closed and removed from Issues log.
➢ **Monthly Briefing Pack – update GALCo on status of currency** FA's compliance with CBI 25% liquidity ratio now included on page 15 of the briefing pack. Matter closed and removed from Actions Log.
➢ **Monthly Briefing Pack – update GALCO on status of currency balancing line split between FA and UB, and suggest timescale for submission of formal request to GALCO for new balancing line limits for enlarged Group** FA's balancing line has been within limits for the past 2 months. Additional reconciliation work is currently being performed to reduce the balancing line further. To be updated at May GALCo
➢ **Personal Credit Balances – Provide reason for fall in retail personal credit balances since the year end** Email sent by CB following March GALCo explaining the decline. Matter closed and removed from Issues log.

4) Ulster Bank Group Monthly Briefing Pack

The Monthly Briefing Pack was noted by the Committee. The pack included First Active plc ("FA") unless where specifically referred to.

- It was noted that the Loans to Banks had increased by £500m over the month (page 1).
- There were no significant movements to report on the non-wholesale divisionalised balance sheets (Pages 3 & 4). House Mortgages RI continued to run well ahead of planned volumes. Favourable volume variances in Business Centres RI and Property were offset by adverse variance in Corporates.

- The capital ratios presented on Page 9 were all within regulatory limits for the month.
- It was noted that there was significant Euro surplus capital being maintained by UBG (page 10). I Tyler pointed out that under RBS policy, such Euro surplus capital should be maintained within 25 bps of total group target ratio. CB to draft paper on the capital position for the May GALCo.
- It was noted that the UBIL Property Sector Concentration was at 248%, close to the CBI limit of 250%, and that additional risk transfers would need to be undertaken to keep the ratio within IFSRA guidelines. It was noted that UBIL's corporate lending in Q1 had already exceeded the full year's projection provided by CB&FM Finance.
- Risk Weighted Assets (Page 11) - underlying RWA's increased on prior month.
- Structural Interest Rate Exposures (Page 12) - Additional swaps were required on both the Euro the STG book due to (i) requirement to reduce NII sensitivity levels (ii) the sell down of capital and (iii) the movement of some FA assets & liabilities from the Galco book to the FM book. It was noted that there is likely to be more hedging activity on the Euro book going forward.
- Structural FX (Page 13) – It was noted that the structural FX risk was €60m higher than reported due excess of capital issued to acquire First Active (€980m) over amount capitalised to date (€920m) not yet having been sold down for STG. A paper on the capital position will be brought to the May GALCo.
- Sterling Operational Liquidity – it was noted that the 1-30 day limit was nearly reached during the month.
- Currency balancing line (Page 15) – It was noted that there was a small breach in the cumulative mismatch report during March. This was reported at the March GALCo.

5) Economic Update

- EURO Rates - GM reported that recent economic data was suggesting that economic activity was picking up and that therefore it was unlikely that the ECB would reduce rates again in the short term. STG Rates – GM / PL reported that it was anticipated that there would be an imminent interest rate increases during the year and that if it did not occur in May it would be very likely to occur in June.
- It was noted that the Irish economy appeared to be picking up quicker than the rest of the EU and that should be positive for UBG's ROI lending targets for the year.

6) Margin Analysis

- M McKavanagh noted that the increase in UK interest rates should help to pick up STG margin. He also noted that the Finance Department have recently started providing some useful new business margin data, which has improved the ability to monitor and control new business.
- J McNamara noted that margins had not moved significantly month on month. Margins are behind plan in the Business Centres, ahead in corporate (ROI), and on plan in property and Corporate (NI).

7) Special Issues

7.1 IAS 39 – Hedging and Measurement Target Operating Model

- SG presented a paper outlining the proposed target operating model for UBG.
- A separate paper detailing the economic impact of the model will be produced for the next GALCo.
- It was noted that if bonds were to be used to hedge the Euro positions under IAS, that only high quality liquid bonds should be bought.
- It was noted that the fair value accounting route would be required for customer deals which fall outside of this model.
- SG to liaise with RBS in order to finalise and agree the optimal IAS 39 model.
- The paper was noted by GALCo

7.2 Stress Testing of Net Interest Income

- The paper set out the sensitivity of the GBP and EUR GALCo Balance Sheets for UBG (including FA) to changes in base rates (but ignoring lead and lag effects).
- It was noted that the impact of rate movements on the GBP book was largely immaterial.
- It was noted that the EUR book was particularly sensitive to base rate reductions, due to the fact that deposit products would increasingly be hitting floors.
- It was also noted that a further drop in the ECB rate was considered unlikely, however, GM was to consider strategies for immunising UB from further ECB rate reductions.
- In order to assess materiality of the NII sensitivity levels vis a vis total projected NII for the year, UB to revert to GALCO with plan NII figures, split between Stg & Euro.
- The paper was noted by the committee

7.3 Integration Update (Verbal)

- GM provided a verbal update.
- Work was now complete on the behaviouralisation of the FA balance sheet for Interest Rate Risk Management purposes, and the underlying process has been agreed with RBS.
- Documentation surrounding the A&LM integration process is currently being completed.
- It was noted that there will be an internal audit of this process over the coming weeks, although no firm date has been agreed (MT to follow up with Integration Committee).

7.4 First Active Fixed Bond Portfolio – Proposed Retention

- CK presented a paper proposing that the FA Fixed Rate Bond portfolio should be retained for the time being.
- It was noted that the holding of this portfolio was technically against RBS policy, however, under the proposed IAS39 target model, UBG would need to retain a sizeable fixed rate bond portfolio. The costs of selling the current portfolio now (in order to comply with RBS policy) and then reinvesting at the end of 2004 (in order to comply with IAS39 target model), has been estimated to be in the region of €1m.
- It was also noted that 1 or 2 of the fixed rate bonds would have to be sold in any event, as their credit quality was not sufficiently high.
- The committee approved the paper in principal, however, the issue would be revisited during the year.
- It was noted that this paper would not have to go to RBS GALCo.

8) Emerging Issues

- PL provided a verbal update.
- Requirement to issue report on FSA's requirements for Liquidity Systems and Controls by each RBS subsidiary, by the end of April for summary report to RBS GALCO on 10th May.
- PL noted that there would be a paper going to RBS GALCo on the > 1yr intra group funding lines. The paper covers the possibility of using UB Finance for wider group funding, which RBS are currently exploring in conjunction with G Murray.
- Basel – at the moment it is proposed that SOLO consolidation will continue under CAD III (Basel), however, there still remains the threat that solo-consolidation will be taken away under Basel, and that all intra-group exposures (including UK to UK) would have to be weighted for capital adequacy purposes. PL would continue to update GALCO on this.

9) Any Other Business

- **UIFCSC** - The current capital plan for UB involves the liquidation of the UIFCSC sub, however, Specialised Finance have a proposed structure, which will require the use of this vehicle. UB GALCO subcommittee has reviewed the proposal and David McNeice is now looking at alternative structures.
- It was noted that the monetary value of the internal UB buffer had increased since the FA acquisition, however so too had the monetary value of the 10% PNWT requirement. Consequently, alternative solutions for UIFCSC need to be considered.
- Discussions are currently underway with Deloitte & Touche, to see if the UIFCSC capital can be treated as debt and therefore Solo consolidation may not be required.
- **Intra Group limits > 1 year**. UB are currently using a significant portion of these limits due to the tracker bond structure. B Lynch currently looking at alternative swap structure in order to avoid using up these limits.
- **Executive Summary**. D Kissane asked for a 1 page summary of the key issues to be produced for future GALCo packs.

The chairman called the meeting to a close.

M Torpey
Chairman

GALCO Issues Arising From Previous Meetings

Date First raised (Minute reference)	Issue	Responsibility	Date to be reported back to GALCO (if applicable)
July 2003 (Item 5.3)	IAS 39 Hedging and Measurement Updated – to be included as a standing item on GALCO agenda going forward	CK	Ongoing
Oct 2003	UBG/First Active Integration to be included as a standing item on GALCO agenda going forward	CK	Ongoing
February 2004	Provide GALCO with update on status of request to IFSRA for dispensation of UBIL Belfast Branch from Property Sector Exposure requirement	GM	May 2004
February 2004	Monthly Briefing Pack – update GALCO on status of currency balancing line split between FA and UB, and suggest timescale for submission of formal request to GALCO for new balancing line limits for enlarged Group	SG / CK	May 2004
April 2004	Draft paper on UBG's capital position to be produced	CB	May 2004
April 2004	Details of UBG's planned P&L, split between Stg & Euro to be circulated to the committee.	CB / CK	May 2004
April 2004	1 page summary of the key issues to be produced for future GALCo packs.	CK	May 2004

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Group Risk Credit Policy and Strategy Committee [GRCP&SC]
Minutes of Meeting held Thursday 28th July 2005

DSE	Initials	GQ	Initials
Eugene McLoughlin	EMcL	Nigel Stewart	NS
Alan Laird	AL	Jonathan Milligan (Chairperson)	JM
Leslie Polson	LP	Stephen Gill	SG
Andrew Walker (Secretary)	AW	Gerry Reynolds	GR
Central Park	**Initials**	**Audio**	**Initials**
Sean L'Estrange (deputy for Des Fitzgerald)	SL'E	John Casey	JC
		Edinburgh	**Initials**
		Bill Livingstone	BL

Quorum (six required members) covered by EMcL, NS, JM, JC, SL'E, BL (six)

Chairperson's Overview

JM Welcomed all to the meeting and thanked all for attendance. He stated that the committee was to consider the 100% FTB Mortgage product and its extension to cover Ulster Bank ROI after previously being introduced to First Active and Ulster Bank NI.

He stated that there were two papers for consideration, the summary proposal from Retail ROI, being presented by John Casey, and the policy from Risk Policy.

Presentation

JM asked **JC** to present the proposed paper.

JC stated that the proposal was a mirror image of the recent First Active 100% FTB Mortgage. He noted that there was a slight change in chargeable interest rates on the tracker products. He noted that Permanent TSB had entered the market place and were likely to be more generous with their affordability rates, based on previous experience.

JC commented that it had been agreed to review the product when FA reached €300m approvals or six months had elapsed and he suggested that this should now be a Group wide review at this stage.

EMcL presented the Retail Credit view that as it was an extension of the product to the UB brand, with the same criteria he was satisfied with the proposal. He noted that the controls were reasonable, covering affordability, no exceptions to the Debt Service Ratio and the review after €300m approvals was reached or six months elapsed (as in FA).

He highlighted two important areas
- Ability to produce good MI at approval and draw-down stage and that there should be identification via separate product codes.
- The €300million approval level review demonstrated good governance and structure for review.

NS noted his agreement and confirmed **EMcL**'s request noting that in the review, profitability, bad debts, revenue totals, impact on P&L figures etc would be analysed, to comply with RBS Group requirements. This was agreed by **SL'E**.

SL'E commented that the product codes were in place and therefore mortgages could be monitored.

JM asked how the need for robust MI was to be addressed.

SG noted that although the codes were in place for FA there was a debate with Greenock in relation to NI.

SL'E gave the assurance that he would deal with the product codes (for Retail ROI and First Active) and MI requests in conjunction with Tanya Waters and Vincent Feeney.

BL noted that it would only take circa seven mortgages to default at an LGD of 25% from year 1 sales before all projected profitability would be eroded. He advised that UB needed to develop suitable MI covering bad debts / income levels to allow ongoing performance to be monitor and if necessary early corrective action to be taken.

EMcL added that his request for MI differential in approval and draw-down was to deal with this issue.

NS presented the Risk Policy, 100% FTB Policy. He noted that although weekly MI was to be produced, it was to be presented to the Heads of Credit on a monthly basis and to the GRCP&SC, quarterly.

He noted two issues
- Page 1 – "What is a first time buyer? - ...a person on his behalf..." – As this phrase, albeit taken from an IFSRA definition, did not add particular value and potentially could cause confusion, it was agreed that it could be removed.
- Exceptions – there would be no flexibility to exceptions.

GR asked if this potentially constricted the business and did not allow for particularly worthy cases to be considered (such as good existing UBG connections).

EMcL stated that since we had given the regulatory authority assurances that there would not be exceptions to our parameters then it would be inappropriate to weaken this stance, but that there were sufficient alternative products available that could be considered on a subjective basis. He added that previously the GRCP&SC had ratified the EMB decision for no permissible exceptions that that this should not be reversed now.

JM stated that he would not be in favour of varying the exception clause on the ROI product given
1. EMB approval is based on no exceptions
2. Differing the terms on the three products would not support the review process.
3. The assurances provided to the regulator, noting the press comments that morning from IFSRA.

JM asked **BL** for the group perspective.

BL reiterated his comments from the request for 100% FTB in the First Active brand that from a credit risk perspective the lack of MI made supporting this proposal difficult. However the recognised the EMB's authority and that this proposal was an extension of current policy in FA with no change in risk appetite and as such, from an RBS GRM perspective was prepared to ratify the decision.

Decision

JM summed up by confirming that all parties were in agreement to support the product – **BL** stated that the decision should be recorded as ratified as the product had already been released.

100% First Time Buyer Mortgage for Ulster Bank ROI was therefore ratified

Defining Our Ideas

one

Our Goals and Customer Strategies

From	In Financials	To
£600m	in Operating Profit	£1.3 Billion
£5 Billion	in new Mortgage Lending	£15 Billion
£10 Billion	in Credit Balances	£25 Billion
£17 Billion	in Business Lending Outstanding	£44 Billion

From	[illegible]	To
32%	Corporate Markets NI Share	40%
15%	Corporate Markets RI Share	30%
80,000	New Personal C/As P/A	250,000
40,000	Corporate Markets Customers	100,000
4th & 2nd	In Customer Service	1st

From	In Presence	To
273	Stores & Branches	303
32	Business Centres	54
680	Relationship Managers	1440
£2m	Telephony & Internet Income	£30m

From	Our People	To
6,000	People in UBG	10,200
Behind	RBSG in Staff Engagement	Ahead
Training	Our people	Teaching

RBS

Ulster Bank Group

ULSTER BANK LIMITED

Papers – "Board Paper - UBIL Capital Injection Request"

17th August 2007

For Approval

Memorandum to Board for its meeting on xx August 2007

Request for €430m Capital Injection into Ulster Bank Ireland Limited and cancellation of €4,525m contract notes between Ulster Bank Ireland Limited and Ulster Bank Limited

Background

In recent weeks, the Irish Financial Regulator (IFR), has increased Ulster Bank Ireland Limited's (UBIL) property sectoral limit from 250% to 500% of its regulatory capital base and may, following a diversification review scheduled for July 2007, be prepared to increase the limit further. This enables UBIL to cancel a series of contract notes which transfer some €4,525m of ROI property sector risk to Ulster Bank Limited (UBL). This excludes contract notes which are transacted for Large Exposure risk diversification purposes.

It will be necessary for UBL to invest a proportionate amount of capital, i.e. some €430m, into UBIL simultaneous to the risk weighted asset migration, to maintain appropriate capital ratios in both companies.

The UBG banks move onto the Basel 2 capital regime from 1st January 2008, and it may be advantageous to build some flexibility into UBG capital accounts to allow for "swing" in aggregate risk weighted assets as the pillar 1 credit and pillar 2 operational components start to become clear. This injection presents such an opportunity.

Proposal

It is proposed to cancel the existing property sector risk contract notes of €4,525m. The tax saving, on re-booking the risk-weighted assets into UBIL, is estimated at €12.7m pa (€4,525m x 1.6% NII x 17.5% tax differential).

To maintain appropriate capital ratios in UBL and UBIL a capital injection of €430m would be required. A capital adequacy analysis is presented in appendix 1 detailing the effects on UBL and UBIL capital ratios.

It is proposed that this injection would take the form of euro tier 2 loan stock. The tax leakage upon UBIL issuing a debt instrument is estimated at €3.5m pa (€430m x 4.6% coupon x 17.5% tax differential) over issuing equity. This expense is a cost of providing flexibility and is independent of the €12.7m tax savings on cancelling the risk transfers. The injection will be made directly from UBL into UBIL for simplicity. The usual legal and regulatory processes for inter-company injections of capital will be observed. UBIL has sufficient tier 2 capacity to include this form in its ratios.

It is proposed to transact this by the end of September 2007 and to complete both transactions simultaneously to maintain capital ratios. This will be completed as soon as practicable.

Approval Required

The Board is requested to approve the following:

- A capital injection of €430m, by way of dated subordinated debt (Lower Tier 2), direct from UBL into UBIL, by 30 September 2007.
- Cancellation of €4,525m property sector risk contract notes between UBL and UBIL.

Michael Torpey
Group Finance Director
01 August 2007

Appendix 1
Ulster Bank Group
Rolling Capital Adequacy Analysis

	1.4849	1.4493	1.4493	1.4493	1.4493	1.4493	1.4493
	Jun-07	**Jul-07**	**Aug-07**	**Sep-07**	**Oct-07**	**Nov-07**	**Dec-07**
Ulster Bank Limited							
Capital Base (£m)	1,225	1,404	1,405	1,406	1,407	1,346	1,337
Proposed Injection into UBIL (£m)			-297	-297	-297	-297	-297
Risk Weighted Assets (£m)	11,866	12,201	12,348	12,519	12,684	12,779	12,883
Proposed Contract Note Cancellation			-3,122	-3,122	-3,122	-3,122	-3,122
Capital Ratio Before Proposal	**10.32%**	**11.51%**	**11.38%**	**11.23%**	**11.09%**	**10.53%**	**10.38%**
Capital Ratio After Proposal	**10.32%**	**11.51%**	**12.01%**	**11.80%**	**11.61%**	**10.87%**	**10.66%**
Ulster Bank Ireland Limited							
Capital Base (€m)	2,275	2,311	2,350	2,373	2,412	2,601	2,640
Proposed Injection into UBIL (€m)			430	430	430	430	430
Risk Weighted Assets (€m)	22,586	23,409	24,381	24,387	25,271	26,024	26,635
Proposed Contract Note Cancellation			4,525	4,525	4,525	4,525	4,525
Capital Ratio Before Proposal	**10.07%**	**9.87%**	**9.64%**	**9.73%**	**9.54%**	**9.99%**	**9.91%**
Capital Ratio After Proposal	**10.07%**	**9.87%**	**9.62%**	**9.70%**	**9.54%**	**9.92%**	**9.85%**

THEME: B2

Effectiveness of banks' credit strategies and risk management

LINE OF INQUIRY: B2B

Appropriateness of credit policies, delegated authorities and exception management

5. Lending Outside Criteria

Detailed below are the percentages of lending (€) in excess of agreed policies for residential mortgage products.

Ulster Bank Republic of Ireland

Date	LTV Outside Policy	DSR Outside Policy (Previous policy)	DSR Outside Policy (Revised policy)
2004	6.5%	23.9%	
Q1 05	5.5%	29.5%	
Q2 05	5.3%	25.6%	
Q3 05	5.2%	23.4%	
Q4 05	4.7%	26.7%	
Q1 06	2.6%	30.0%	
Q2 06	7.0%	33.0%	
July 06	8.0% (€15.7m)	32.4% (€67.9m)	
Aug 06	7.3% (€13.0m)	25.7% (€49.2m)	
Sept 06	7.3% (€12.1m)	32.2% (€57.5m)	11% (€13.2m)
Oct 06	7.2% (€12.1m)		11% (€24.1m)
Nov 06	7.0% (€13.0m)		13.9% (€34.4m)
Dec 06	6.1% (€11.8m)		24.8% (€37.3m)*
Jan 07	8.2% (€13.1m)		18.7% (€27.7m)
Feb 07	9.0% (€18.9m)		17.5% (€18.9m)
Mar 07	13.6% (€29.3m)**		15.1% (€30.8m)

* The UBIL DSR exception rate for December was higher than expected. Following a review by Retail Credit a more conservative approach has been adopted post December.

** The UBIL LTV exception rate has increased due to system technical issues regarding the inputting of property valuation data. The reasons are being investigated and we have brought to the attention of Dublin Mortgage Centre.

First Active

Date	LTV Outside Policy	DSR Outside Policy	DSR Outside Policy (Revised policy)
2004	2.2%	4.9%	
Q1 05	2.0%	5.7%	
Q2 05	2.5%	5.3%	
Q3 05	3.1%	4.7%	
Q4 05	3.3%	6.2%	
Q1 06	4.3%	8.8%	
Q2 06	6.3%	10.8%	
July 06	6.6% (€24.1m)	11.7% (€28.5m)	
Aug 06	6.6% (€22.5m)	16.8% (€15.7m)	
Sept 06	8.3% (€18.6m)	9.9% (€6.1m)	
Oct 06	8.7% (€18.1m)		7.8% (€17.2m)
Nov 06	8.5% (€20.5m)		7.8% (€30.6m)
Dec 06	10.3% (€19.3m)		6.9% (€14.8m)
Jan 07	8.1% (€18.6m)		7.0% (€17.7m)
Feb 07	7.0% (€19.3m)		8.8% (€18.4m)
Mar 07	7.2% (€20.6m)		6.0% (€14.2m)

THEME: B2

Effectiveness of banks' credit strategies and risk management

LINE OF INQUIRY: B2C

Analysis of risk concentration in the base, the adverse economic scenarios and the impact on capital structure

Provisions & Arrears Board Paper

Ulster Bank Group Credit Risk
September 2008

RBS

Ulster Bank Group

Overview

The credit environment is very challenging at present and is expected to remain so at least until late 2009 or more likely into 2010. This is being driven by:

Credit Environment

- International Credit Crunch
- House Prices
- Commercial Property Prices
- Stock Markets
- Unemployment
- Interest Rates
- Oil Prices
- Inter Bank Liquidity
- Risk Appetite
- Government Tax Take

Results

The impact of the above on our impairment charge for 2008 is that:

Our ytd impairment charge is £64m resulting in an adverse variance to plan of £14m (£1m favourable to 6+6).

The Retail and Corporate Divisions account for £6.3m and £7.5m of the adverse to plan variance respectively.

The Corporate adverse variance is driven by higher defaulted Property exposures in BB NI and Business Centres RI

The Retail adverse to plan of £6m is due to higher Mortgage and Personal bad debt flows than forecast

Outlook

6+6 has forecast an increase in the impairment charge from 17bps to 28bps (4+8: 21bps).

Details of the changing outlook during 2008 is set out overleaf.

Refer to Appendix 1 and Appendix 2 for detail

2008 Impairment Charge Outlook

Executive Summary

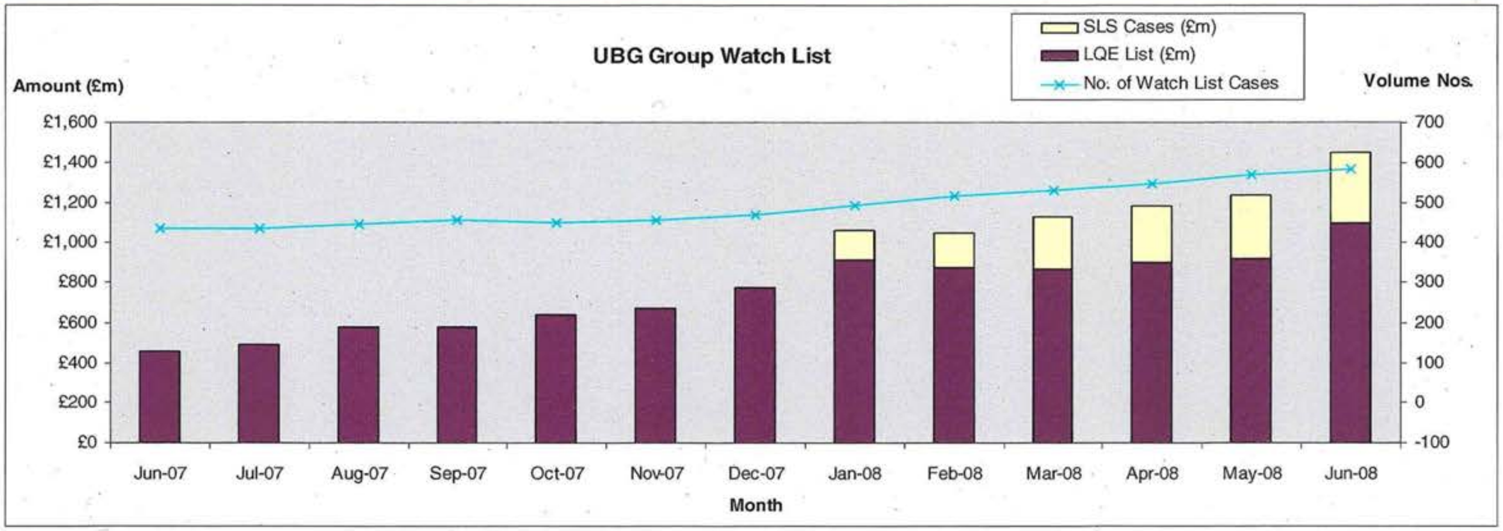
Fx Rate =1.3049	Plan 08	4+8	6+6
	£'m	£'m	£'m
P & I Charge	**2008**	**2008**	**2008**
Total Retail Markets	36.32	33.36	33.36
Total Corporate Markets	49.13	71.57	100.91
Total UBG	**85.45**	**104.93**	**134.28**
Vol's	£'m	£'m	£'m
Total Retail Markets	22,035	19,521	19,842
Total Corporate Markets	29,569	29,463	27,812
Total UBG	**51,604**	**48,984**	**47,654**
BPS	%	%	%
Total Retail Markets	0.16%	0.17%	0.17%
Total Corporate Markets	0.17%	0.24%	0.36%
Total UBG	**0.17%**	**0.21%**	**0.28%**

Provisions & Impairment KPIs

Key Performance Indicators

	Dec-06 £'m	Dec-07 £'m	Jun-08 £'m	Jul-08 £'m	MoM £'m	YTD £'m
Loan & Receivables	35,934	44,581	49,853	49,927	74	5,345
Risk Elements in Lending	432	606	815	841	26	236
Provision Balance	250	322	379	382	3	60
Provision Charge YTD	72	79	57	64	7	64
Annualised YTD Impairment Charge	0.20%	0.18%	0.23%	0.22%	-0.01%	0.04%
Provision (% of L& R)	0.70%	0.72%	0.76%	0.77%	0.01%	0.04%
Provision Coverage of REIL	58%	53%	46%	45%	-1.05%	-7.68%

Corporate Markets Watch List



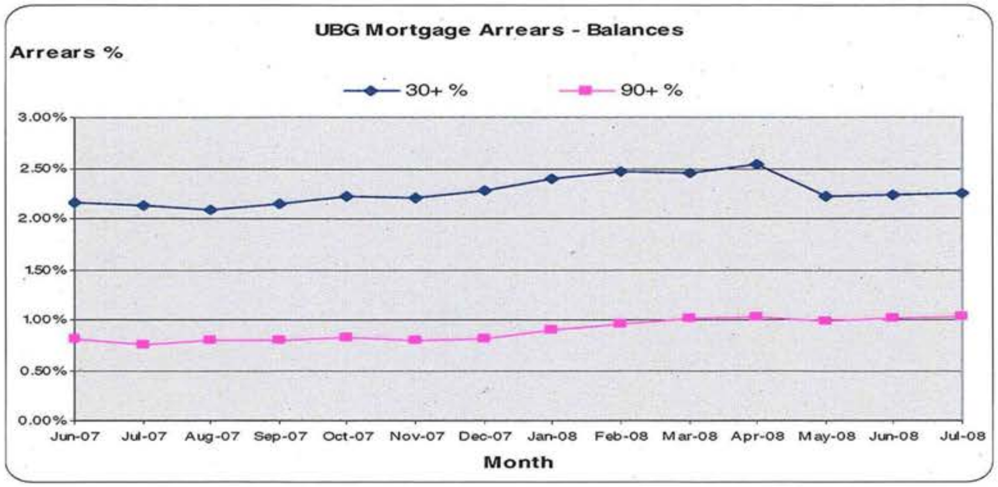
Watch List includes impaired loans and those accounts where impairment has not occurred and case is receiving close attention, portfolio totalling c.£1.4bn.

In addition, an "Early Watch" process has been implemented focussing on cases requiring attention that have not yet breached Watch List criteria. This portfolio represents a further £2.7bn.

Watch List ytd growth (190% in value, 34% in case volume) has been driven by widespread reviews across all portfolios with dedicated Credit and Business teams in place. Difference in growth in value and cases highlights number of larger developers "under watch".

Adverse developments in debt and capital markets and downturn in NI/RI economies have resulted in liquidity pressures and reduction in some capital values. Corrective market action to mitigate oversupply is apparent.

Mortgage Arrears Trend



Mortgage Arrears

The increasing arrears trend evident across all portfolios in Q1-2008 has stabilised and reversed in Q2-2008 as a result of significant improvements in collections operations. This includes a significant increase in collections resources.

Further improvement is targeted in H2 as some of the infrastructure improvements start to take effect; however the prevailing context is of a more challenging arrears environment going forward.

Peer Comparison

Impairment Charge (bps)	Actuals 2007	Banks 2008E	Brokers 2008E	Brokers 2009E
UBG	18	28*	26 (C.)#	31 (C.)#
AIB^	9	35	40 (ML)	78 (GS)
BOI^ (year end 31/03)	17	25~	38 (N)	66 (GS)
Anglo (year end 30/09)	10	13-18	70 (C.)	70 (GS)

* 6+6 reforecast (assuming model changes benefit of £35m otherwise forecast will be 36bps)

^AIB and BOI are Group numbers

~ BOI did not re-iterate this early guidance at their recent AGM

Latest estimates not in line with our peers

N : NCB Brokers ML: Merrill Lynch C: Broker Consensus GS: Goldman Sachs

Stress Testing of Impairment Charge

	2008 FY	2009 FY	2009 FY	2010 FY
Loan Growth		0%	0%	0%
Normalised Impairment Charge (£'m)	134	264	264	215
Impairment Charge Bps	**28**	**55**	**55**	**45**
STRESS TEST		**Scenario 1**	**Scenario 2**	
Property Prices				
Resi Mortgages	-10%	-10%	-20%	-10%
Corporate & Property	-20%	-10%	-20%	-10%
Stressed Impairment Charge (£'m)	-	51	142	152
Total Impairment Charge (£'m)	**134**	**315**	**406**	**367**
Impairment Charge Bps	**28**	**66**	**84**	**76**
AIB plc (bps)	35	100	100	100

- 2008 9+3 to be finalised. While the market is getting even more challenging, at this point we are not increasing the provisions from the 6+6, based on obtaining expected benefit (c£35m) from Model Changes currently being discussed with RBS. However, this position is being kept under constant review. Assumption of negligible growth 2009/10.
- Forecast 2008 outturn incorporates a further 10% reduction (20% from peak) in house prices and 20% (from peak) in Corporate & Property asset values (including residential developers). Note corporate cases have also been stressed which is a conservative approach.
- The 2009 normalised charge assumes crystallisation from stress loss into impairment (stress loss refers to cases under strain where impairment has not yet occurred).
- Under 2009 Scenario 2 a further 20% reduction (40% from peak) has been incorporated into 2009 against residential and corporate with fall in values predicted to slow in 2010.
- Under 2009 Scenario 1 stress we are guiding a charge of 66bps, in line with AIB's views of 60-80bps (normalised). Scenario 2 is marginally more conservative at 84bps ***on a stressed basis***.

Appendices

1. UBG Impairment Charge YTD July 2008
2. Legal Entity Impairment Charge YTD July 2008

1. UBG Impairment Charge YTD July 2008

Jul-08	Actuals Ytd	Plan 2008 Plan	Plan 2008 Variance	Reforecast 6+6	Reforecast Variance	Bps Annualised	YoY (Constant FX) Jul-07	YoY (Constant FX) Variance
Retail	£'000	£'000	£'000	£'000	£'000	%	£'000	£'000
Personal Banking	10,320	8,163	(2,157)	9,700	(619)	2.42%	6,532	(3,788)
Mortgages	10,940	6,771	(4,169)	9,968	(972)	0.09%	8,921	(2,019)
Cards	6,288	6,303	15	6,279	(9)	3.86%	5,985	(304)
Retail Accrual							37	37
Total Retail	**27,548**	**21,237**	**(6,311)**	**25,948**	**(1,600)**	**0.22%**	**21,475**	**(6,073)**
Corporate Markets								
BBNI	15,149	9,711	(5,438)	15,810	661	0.29%	4,345	(10,804)
Corporate Banking RI (incl. UBIF)	2,338	4,892	2,554	2,233	(105)	0.10%	240	(2,098)
Property	2,699	2,761	62	3,638	939	0.06%	3,590	891
Business Banking RI	16,292	11,560	(4,732)	17,526	1,234	0.37%	1,562	(14,730)
Corporate accrual							14,427	14,427
Total Corporate Markets	**36,478**	**28,923**	**(7,554)**	**39,207**	**2,729**	**0.22%**	**24,164**	**(12,314)**
Total	**64,026**	**50,161**	**(13,865)**	**65,155**	**1,129**	**0.22%**	**45,639**	**(18,387)**

2. Legal Entity Impairment Charge YTD July 2008

Jul-08	Actuals	Plan 2008		6+6 Reforecast		YoY (Constant FX)	
	Total	Plan	Variance	Forecast	Variance	Jul-07	Variance
UBL	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Retail Markets	7,965	7,009	(956)	7,667	(298)	5,613	(2,352)
Corporate Markets	15,149	9,711	(5,438)	15,810	661	4,345	(10,804)
Accrual						14,464	14,464
	23,114	16,719	(6,395)	23,478	363	24,422	1,308

	Actuals	Plan 2008		6+6 Reforecast		YoY (Constant FX)	
First Active	Total	Plan	Variance	Forecast	Variance	Jul-07	Variance
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Retail Markets	6,981	5,466	(1,515)	6,687	(294)	8,129	1,148
Corporate Markets	(79)	(298)	(219)	359	438	(272)	(193)
	6,902	5,167	(1,734)	7,046	144	7,857	955

	Actuals	Plan 2008		6+6 Reforecast		YoY (Constant FX)	
UBIL	Total	Plan	Variance	Forecast	Variance	Jul-07	Variance
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Retail Markets	12,602	8,763	(3,839)	11,594	(1,009)	7,696	(4,906)
Corporate Markets	21,408	19,511	(1,897)	23,038	1,630	5,664	(15,744)
	34,010	28,274	(5,736)	34,632	622	13,360	(20,650)
UBG Total	64,026	50,161	(13,865)	65,155	1,129	45,639	(18,387)

C2(b)

Ulster Bank Group

Commercial and Residential Real Estate Sector Review 2007

Issued to members of the
Group Risk Committee
4 April 2007

FOR NOTING

Authors:	Paddy O'Driscoll Head of Property Credit (RoI) UBG
	Ronnie Hanna Head of Credit (NI) UBG
Approved for submission to GRC by:	Michael Feeney Head of Credit, UBG
	John McDonnell Chief Risk Officer, UBG
	Robert Gallagher Chief Executive, Corporate Markets, UBG
	David Coleman Group Chief Credit Officer

Purpose

This paper presents a review of the Ulster Bank Group (UBG) property lending business and marketplace and provides an overview of:

- The UBG property lending portfolio strategy;
- Macroeconomic environment, drivers and outlook in Northern Ireland (NI) and the Republic of Ireland (RoI) property markets;
- Property transaction parameters (focussing on liquidity and transparency of sponsors' net worth and structure); and
- Speculative Financing approach in the context of the NI/RoI planning regimes.

Portfolio Overview

The property lending portfolio under review (£12.86bn[1] as at Jan 2007) represents 29% the UBG's total portfolio (2.46% of RBS Group Risk Assets) with a CAGR of 35% (RoI) and 46% (NI) over the last 2 years. The portfolio is spread across RoI (focusing on residential) and NI (dominated by commercial investment) with a diversified client base of c950 in RoI and c360 in NI. Demographic concentrations continue to shape UBG geographic split and ability to diversify away from the Greater Dublin and Belfast regions. While UBG's regional property businesses are expanding alongside market participants, concentrations will persist around the two major centres, with investments also in UK mainland. The UBG property portfolio is split:

	Limits – based on 80% sample of each Portfolio					
	RoI	**%**	**NI**	**%**	**Combined**	**%**
Residential property						
Development	£1.75 bn	28%	£0.19 bn	4%	£1.94bn	19%
Land	£1.42 bn	22%	£1.22 bn	31%	£2.64bn	25%
Investment	£0.27 bn	4%	£0.02 bn	1%	£0.29bn	3%
Total Residential	**£3.44 bn**	**54%**	**£1.43 bn**	**36%**	**£4.87bn**	**47%**
Commercial property						
Development	£0.31 bn	5%	£0.21 bn	5%	£0.52bn	5%
Land	£0.23 bn	3%	£0.20 bn	5%	£0.43bn	4%
Investment	£2.39 bn	38%	£2.10 bn	54%	£4.49bn	44%
Total Commercial	**£2.93 bn**	**46%**	**£2.51 bn**	**64%**	**£5.44bn**	**53%**
Total Residential & Commercial	**£6.37 bn**	**100%**	**£3.94 bn**	**100%**	**£10.31bn**	**100%**

The weighted average LTV is below 64% on the development side, but with specific investment LTV's averaging 70% and above. The PDs and LGDs, outlined below reflect the varying personal and corporate borrowing structures and the secured nature of the portfolio respectively. The weighted average interest cover on the commercial investment portfolios is 1.2 times, with a weighted ICR on the development side less meaningful due to the provision of interest roll-up in many of the limits.

	Limits	**LTV**	**LGD**	**PD**	**ICR**
NI Residential	£1.43bn	61%	5.11%	1.62%	N/a
NI Commercial	£2.51bn	71%	5.67%	1.50%	1.20
RoI Residential	£3.44bn	64%	11.95%	1.53%	N/a
RoI Commercial	£2.93bn	69%	7.59%	1.41%	1.21
Combined weighted average	£10.31bn	67%	8.23%	1.50%	N/a

[1] For consistency, all exposures are quoted in UK pounds and, where appropriate, converted at €1.50 : £1

Property lending continued to be a driver of income growth for UBG in 2006 with Property Finance business in RoI contributing £87m and Property NI contributing £44m. This represents 13% of UBG income in 2006.

Economic overview

The ROI economy is forecast to grow by 5% to 6% in 2007 in line with 2006 figures reflecting strong consumer spending and buoyancy in house construction and investment. Growth is expected to be lower in 2008 as housing slows and the boost to consumer spending from maturing Special Savings Incentive Accounts[2] (SSIA) dissipates. The economy is expected to remain in full employment with jobs growth fuelled by continued strong immigration. The product of the economic upturn and strong population growth has been increased residential and commercial property demand, supply shortages, accelerating property values, rising rents and falling yields. The supply response has been 88,000 completions in 2006 for a population of 4.1m – in 1993, completions were just 21,000.

Forecasts are moderated by recent (Feb 2007) economic data showing decelerating activity. By end 2006, supply and demand were coming into balance as annualised monthly housing inflation was down to one per cent. This substantiates UBG Economics' view of a slowdown in the ROI housing market driven by higher interest rates. A fall in January 2007 new ROI Housing Starts/Registrations and weak PMI readings imply that developers have already anticipated slower demand out to 2008.

NI housing continues to outpace both RoI and UK averages with inflation in excess of 30% in 2006 – moderation to 10% to 20% is forecast for 2007. The NI trend is of falling unemployment and continued strengthening of the economy.

Land availability, local planning, tax incentive schemes, strong incomes growth and high immigration levels are all set to sustain prices and absorb output both North and South.

Alongside the key macroeconomic risks of rising unemployment, interest rates and faltering global growth, key risks come from downsizing in the construction labour force, wider unemployment and worst-case forecasts of c-20% house price correction. In this scenario, the areas of most concern would be the buy-to-let sector and regional apartment developments. However, UBG central view is clearly for a slowdown in housing output and price inflation (anticipated by the market) with continuing good growth and employment. These features of low inflation, low interest rates and low unemployment distinguish the Irish property markets from conditions that led to the late 1980s housing market collapse in the UK.

Property Strategy and Competitive Environment

UBG Corporate Markets, Property Finance businesses in RoI manage UBG residential and commercial development (>€5m) and investment (>€10m) property financing, with the NI Property Teams managing property connections with limits >£5m. UBG overall strategic direction is to continue to grow the portfolio, which has been a significant and remunerative engine of growth for the division for more than 10 years.

[2] Government supported monthly savings scheme over 5 years with maturity between May 2006 and April 2007

The RoI property finance market is highly competitive with Anglo, Allied Irish Bank, Bank of Ireland and Bank of Scotland (Ireland) targeting sections of the market. In NI, BoI is the strongest challenger. With a long track record, UBG have maintained market profile by continuing support to major property companies/individuals with a clear and consistent property strategy within their wider market interests. Competition for these relationships is intense with stretching LTVs, interest roll-up and equity release common features of landbank and development facilities, particularly in RoI, with NI showing some similar features, albeit less frequent.

UBG Credit and Front Office are finalising for Divisional Risk Committee a granular review of the RoI residential development sector which expands on the property review in the RoI Business Banking review presented to GRC in August 2005, with a further NI paper to be prepared for Divisional Risk Committee in 2007. Credit risk appetite in the current review remains positive towards well structured transactions which fit within the overall business strategy. The key lending assessment criteria are: the asset financed (quality, location, product); understanding the deal structure and its ability to stand on its own (cashflow analysis, refinance risk, demand); and the borrower/sponsor (track record, equity contribution and substantiating their net worth/liquidity and ability to provide support in cases where there could potentially be reliance on that worth).

Net Worth / Liquidity

The borrowing structures employed by developers, particularly in RoI, are tax driven including, for example, land in private names (attracting CGT on gain at 20%, rather than company non-trading income tax at 25%) and work in progress in companies (attracting corporation tax at 12.5%, rather than higher rate personal tax at 42%). JVs, SPVs, co-ownership agreements and syndicates feature in both markets with the NI experience being predominantly led by corporate vehicles. Due to differences in the customer structure in RoI, a lack of audited financial information can present a challenge in substantiating net worth and liquidity whilst NI customers generally have the expected audited information.

UBG obtain Independent Net Worth Statements (NWS) and direct statements from sponsors but recognise that both information sources are reliant on provision of information by the customer. In cases where there is a requirement for recourse/reliance, UBG looks to critically assess the net worth position to understand the sponsor's wider portfolio and the financing and liquidity of that portfolio with this underpinned by additional audited and un-audited financial and project information as appropriate.

In order to enhance the report details, UBG have initiated a Client Net Worth enquiry form outlining the information RM should be seeking. However, the reality in competitive markets is that some customers will be reluctant to provide full disclosure, as they will not be required to do so by our competitors. Based on the RM's ability and client's willingness to substantiate net worth (net of guarantees to other institutions), UBG will assess net worth in the context of whether there is low, medium or high reliance on that worth, with this to be explicitly commented on in submissions to Credit Committee.

A further consequence of the business models/structures employed is the complexity of the web of inter-connected relationships, and the resultant challenges of aggregation, analysis and approval of transactions. UBG Front Office and Credit have addressed this in a review to enhance the information and its presentation to Credit Committees.

Speculative Financing

In line with Group policy, UBG caps speculative commercial property financing without suitable risk transfer at 3% of the UBG commercial property portfolio. Current utilisation of £108m on the portfolios under review, equating to 2% of the commercial element only, is well spread to a diversified range of counterparties. Historically, UBG have excluded the residential element of the portfolio (the financing of unzoned land which is purchased/held for ultimate residential development) from their calculations, but propose moving to align UBG with RBS in this regard. This will have a broadly neutral impact on headroom for speculative financing, but will give consistency of approach across divisions.

Local land development regulation differs from UK mainland where the concept of zoned land does not exist. Overviews of NI/RoI planning regimes have been prepared as part of this review. For clarification, in RoI zoned land is excluded from the cap, whilst unzoned lands are included in cases where suitable risk transfer is not available. In a NI context residential sites are excluded from the cap. A site is deemed to be suitable for residential development if it has been appropriately zoned, either exclusively for residential purposes or if deemed suitable by the Planning Service for general development within a city or town's development limit (known as "white land" where there is a residential planning imperative). There is a very low level of financing of un-zoned land (NI 0.5%/RoI 4% of the sample) and this is typically to existing clients with portfolios of property providing cross collateralisation/risk transfer and/or other recourse.

Conclusion and Recommendations

The combined portfolios are characterised by satisfactory LGDs and PDs across all segments and are underpinned by acceptable LTVs. Whilst there has been strong growth across the market, the bad debt experience is excellent over the last 10 years. The strong Basel 2 metrics confirm that growth has been achieved without compromising credit quality standards, and leave the Bank well placed to continue its growth strategy in the competitive environment.

GRC is asked to note the UBG property lending review, the enhancements to the Credit Risk Management process, and the strategy for continued growth; specifically:

- Enhancements to credit risk assessment and presentation of property developers claimed Net Worth.
- Treatment of residential lands within UBG Speculative Property Policy.
- Ongoing growth in this market supported by the continuing satisfactory economic position in RoI and the strengthening economic outlook in NI.

The Royal Bank of Scotland Group

Ulster Bank Group Sector Review – Property Portfolio

Issued to members of the Group Risk Committee July 2008

Author: Rosemarie Donnelly, Nick Cooper , Margaret Sweeney

Sector Review Approved by: John McDonnell

Sector Outlook: Cautious

Summary Sector Review approved for submission to GRC: John McDonnell

Purpose

This paper presents a review of the Ulster Bank Group Corporate Markets Property Portfolio for Group Risk Policy and Strategy Committee (GRPCC) and seeks approval of the credit risk app etite detailed within.

Executive Summary

UBG propose an overall **Cautious Credit Risk Appetite** towards the Property Sector in general over the next 12 -18 months, with **a negative appetite for specific sub sectors / segments** . This is driven by the adverse developments in debt and capital markets and the downturn in the ROI, NI and UK economies (where the majority of our counterparties are based), which have resulted in a reduction in asset values and pressure on cashflow/liquidity for counterparties operating in this sector. The proposed lending guidelines reflect the current risks for market participants and are designed to ensure early identification of problem cases and active management of the portfolio through this period of the business cycle.

While an overall cautious appetite is appropriate in the current market conditions, we maintain an appetite to selectively underwrite well-structured proposals that meet credit guidelines, in particular where strong cashflow/liquidity positions are evident and a long-standing track record provides mitigation. The focus for business development is expected to be in growing our Investment Portfolio by providing support to key counterparties who are in a position to take advantage of the opportunities available in the current market.

Portfolio Summary

Property Portfolio Segment	Credit Limits (£m) June 06	Credit Limits (£m) June 08	Growth (£m) June 08	CAGR % (2 years)	Share Property Portfolio	Share CM Portfolio	PD % June 08	LGD % June 08	EL % June 08
Investment Residential	£407m	£691m	£284m	70%	3%	2%	1.44%	14.65%	0.20%
Investment Commercial	£5,417m	£8,881m	£3,464m	64%	42%	25%	1.31%	14.55%	0.18%
Development Residential	£5,568m	£7,564m	£1,996m	36%	36%	21%	1.79%	12.33%	0.23%
Development Commercial	£1,946m	£3,078m	£1,132m	58%	14%	9%	1.67%	12.22%	0.22%
Contractors/Building Suppliers	£1,418m	£1,121m	-£297m	-21%	5%	3%	1.12%	33.54%	0.31%
Property Sector Book	**£14,756m**	**£21,335m**	**£6,579m**	**45% (31%*)**	**100%**	**60%**	**1.53%**	**14.09%**	**0.22%**
Corporate Markets Book	**£25,149m**	**£35,524m**	**£10,375m**	**41%**	**N/A**	**100%**	**1.41%**	**21.81%**	**0.27%**

*Actual growth in limits, n et of sterling movements .

UBG Corporate Markets Property Portfolio at June 08 represents 60% of the Corporate Markets Balance Sheet and 34% of the UBG Balance Sheet. Property Portfolio RWAs amounted to £7.8bn at Mar ch 08, which represents 42% of Corporate Markets RWAs. Basel II Return on Capital (on an operating profit basis) amounted to 31.32% at May 08.

Portfolio CAGR (over last 24 months) at 45% is inflated due to the appreciation of the Euro against Sterling. Actual growth in limits, net of sterling movements, amounted to 31%. Growth occurred predominantly in the 18 months from June '06 to December '07 driven by a low interest rate environment and strong econom y in both ROI and NI during this period. Lending activity has scaled back in the last 6 months with pressure on asset values and limited market demand reflecting the challenging economic outlook and negative market sentiment.

Credit impaired balances (NAL), £228m / 1.1% of loan book, have risen significantly over the last 6 -12 months. Portfolio Provisions amount to £110m of which £62m relate to individually assessed cases. We expect that the number of cases at the margins will continue to increase while t he negative market sentiment prevails.

Market Outlook

The ROI and NI economies are experiencing simultaneous slowdowns in private sector activity and proposed reduction in public expenditure growth, along with a sharper than expected correction in the housing market, which have led to a sharp slowdown in economic activity. This has been compounded by the credit crunch and the continued increase in inflation and combined these factors are expected to negatively affect business and consumer confidence and spending well into 2009.

Key risks in the UBG Property Portfolio

Key issues / concerns for the portfolio include:

- Falling capital values, with particular concern for assets in secondary locations.
- Lack of liquidity, particularly within the development market for land-banks and finished product.
- Weak demand for residential properties due to (a) over supply, (b) tighter lending parameters resulting in difficulties for buyers obtaining mortgages and (c) lack of consumer confidence.
- Pressure on the debt covenants, particularly LTV covenants for deals completed at top of the market.
- Increasing financial incentives required to secure tenants and increase in breaks on new lease terms evident.
- Downturn in the Retail Sector due to slowdown in consumer spending and the possible effects on tenant cashflow.
- Increased refinance risk and reduced ability to distribute debt due to liquidity issues in the market.

- The Investment Property book, which represents 45% of exposure, is well placed to withstand the downturn with focus on underlying cashflows and robust covenant protection. Residential portfolio interest cover amounts to 1.26x and average LTV stands at 64% (June '08). Commercial portfolio interest cover amounts to 1.29x and average LTV stands at 67% (June '08). Exposure where LTV>90% accounts for less that 3% of the book.
- Speculative Funding of Commercial Property is controlled through the 3% portfolio cap. Unmitigated speculative limits amounted to £237m at June '08. This exposure is well spread with only seven connections having exposure over £7m. The largest exposure £19.5m relates to a business park and hospital site in the RI Midlands. Quality of the book is satisfactory with four connections totalling £7m managed by LQE, one SLS case £2.4m. There are no provisions marked against this portfolio.
- The Residential Development portfolio is under pressure, with minimal market appetite for either land-bank or completed product. The level of construction work being undertaken has declined significantly, with very little ongoing speculative build. Where developers continue to build, there are mitigating circumstances, in particular pre sales. In general, developments which have discounted correctly have attracted buyers albeit success is driven by significant price discounts, i.e. up to 20% on 2007 figures. The expected reduction in housing starts in both RI and NI in the period 2008/2009 should assist in reducing supply and as such supply / demand is expected to revert back to equilibrium by 2010.
- Despite the curtailment of supply in the RI residential market, it is estimated that there is an overhang of c.35,000 completed units. At present, Property Finance RI stock of completed residential property amounts to c.4,547 units of which 2,872 (63%) remain on the market. This exposure is being proactively managed through close involvement in the sales process, with price reductions to shift stock encouraged as appropriate. All connections are reviewed on a monthly basis, with cases showing early signs of distress reported to Senior Management. Supply and demand equilibrium is not anticipated until 2010 and we have therefore implemented strategies which seek to manage through the current period (discussed below).
- In NI, the economic slowdown and ongoing uncertainty in the housing market has resulted in a significant reduction in transactions in the market and subsequent build up of stock. However, statistics imply pent up demand in the market, indicating that 200,000 units will be required by 2015. A review of the largest residential developers by exposure, accounting for 52% of total Property Finance NI residential development book, splits underlying risk in the portfolio 34% (£0.47bn) WIP and 66% (£0.9bn) landbank. Completed stock to hand is c.1,000 units of which c.70% remains unsold (average house sales 12,000 p.a.). The key focus now is liquidation of completed stock, and while we expect the stock to continue to reduce in the medium term, we have in place strategies for management of the book through the interim period (discussed below).

Management and Control of Risk in the Current Climate

While we retain appetite to selectively underwrite well-structured proposals, our key focus is on management of the existing portfolio. We have increased our interaction with customers and renewed front-line focus on credit stewardship. Procedures for the identification and escalation of early distress cases have been revised and an enhanced governance process has been introduced. Where facilities are being re-structured to provide liquidity in the short-medium term, this is being undertaken within an appropriate pricing governance structure. The more vulnerable customers are highlighted on watch lists and are being actively managed within the LQE and SLS process.

Given the scale of industry wide issues, asset sale or refinance are generally unsuitable short term strategies and manage through solutions are required for stretch cases, particularly as regards site finance where no resale market currently exists. The level of support is being determined on a case by case basis, within the following general framework:

- Key objective is to determine short-medium term strategy early in conjunction with the customer, with any work out to be managed / monitored tightly in accordance with agreed action plan.
- Detailed appraisal of cashflows and requirements undertaken to bring asset to appropriate maturity point to facilitate eventual sale or refinance. Pre sales are a key determinant of appetite.
- Top tier customers, i.e. major operators with strong co operative relationships with the bank, are being positively considered for accommodation, e.g. interest roll up, extension of terms, etc.
- Accommodation above senior debt parameters to include back-ended fee, equity interest via joint venture profit share or payment in kind note dependent on leverage.
- Accommodation typically offered for a 12 month period, but generally may require renewal, subject to further return ratchet.
- Rigid adherence to terms and conditions of sanction, i.e. tight monitoring, regular reviews, etc.
- Following build out, borrowers are being given limited tolerance as regards timing and extent of price discounting required to exit (where pre sales were not in place).
- Restructure used to maximise the Bank's position, e.g. further recourse, additional security, cross-collateralisation.
- Basel 2 / Capital implications of any restructure considered.
- SLS actively engaged and consulted as appropriate, i.e. consideration of buy-in mechanisms where a long-term asset hold strategy is required.

Credit Risk Appetite

- **UBG Property Portfolio appetite is cautious; however a negative stance is being adapted to specific sub sectors / segments as appropriate.** Appetite for each sub sector of the portfolio is outlined within the appendices of this paper. Key points of note are:
  - Negative to Speculative Funding of Residential and Commercial Property.
  - Negative to Investment and Development Funding for apartments outside metropolitan areas.
  - Negative to Medium / Small Sized Customers with single assets and limited visibility on cashflow and liquidity.

- We have an <u>increasingly cautious</u> approach to development funding supporting only key counterparties where there is a transparent and acceptable relationship and effective asset management with confirmation of strong sustainable cashflow / liquidity, pre sales, low gearing, and in particular acceptable exposure to land-bank risk.

- We have a strong preference for dealing with counterparties with a proven management team in terms of through the cycle experience and close co operation with the Bank. We remain open to New to Bank Relationships on an increasingly selective basis where strong due diligence confirms that counterparties meet above average requirements when assessed against key risk drivers.

- We retain appetite to selectively grow the investment portfolio by supporting experienced counterparties where there is a transparent and acceptable relationship and effective asset management, clear evidence of strong sustainable cashflow / liquidity from a high quality asset and tenant base.

- Our appetite remains to write well structured transactions, on a selective basis, showing the following characteristics:
  - Sustainable cashflow/liquidity and debt servicing ability.
  - Deal structure, pricing for risk and refinance risk
  - Portfolios with quality lease agreements and limited rental volatility.
  - Strategic location of land banks.
  - Development only where strong demand exists, i.e. against pre sales.
  - Robust covenant structures and ratchets over term sought.

Recommendation

The credit risk appetite is recommended for approval. Appendices presented provide a portfolio overview along with sub sector management information, key risk drivers, credit risk appetite and lending assessment guidelines. Group Economics commentary is also included.

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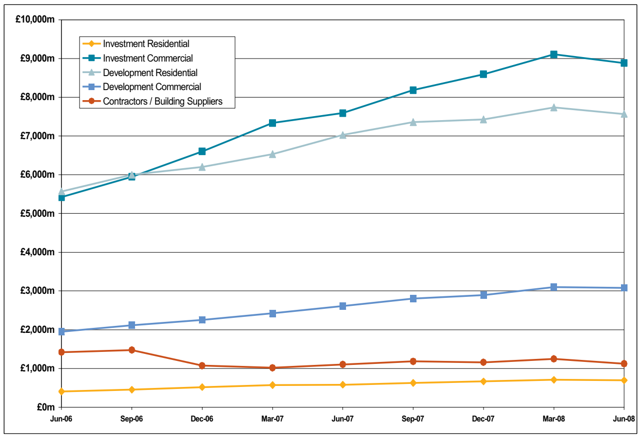
Risk Appetite	Definition
Positive	The prime focus for new business, we wish to develop our portfolio primarily in these areas.
Cautious	Areas where we are prepared to take new business, but on a more selective basis.
Negative	We do not wish to take new business in this area: and only exceptional cases, benefiting from exceptional risk mitigation, will be considered.

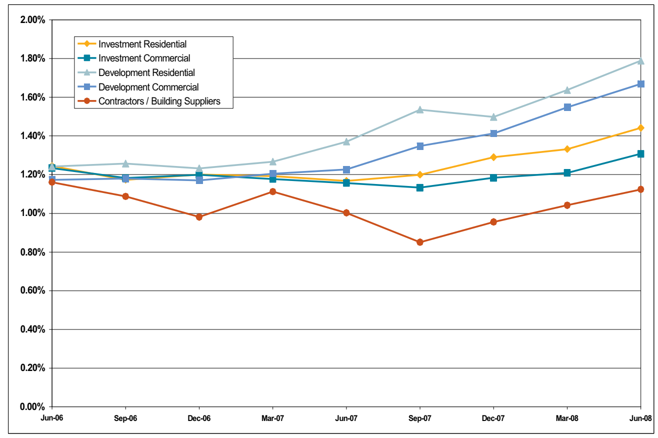
1. UBG Property Portfolio

1.1 Portfolio Summary and Management Information

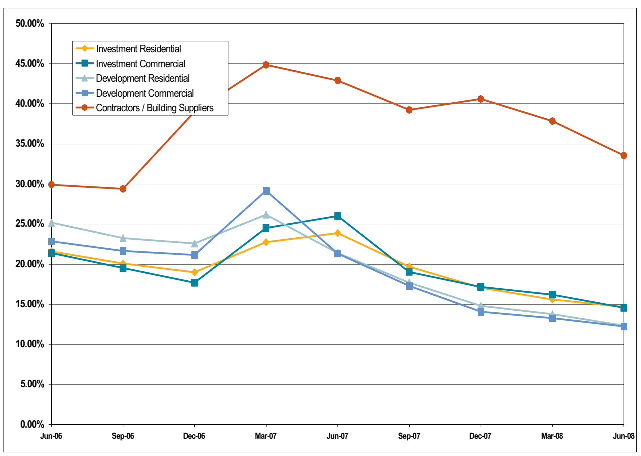
Credit Limits (£m)



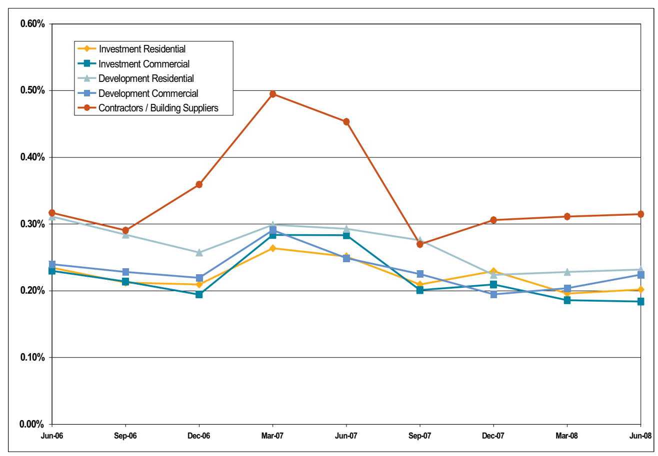
Probability of Default (PD)



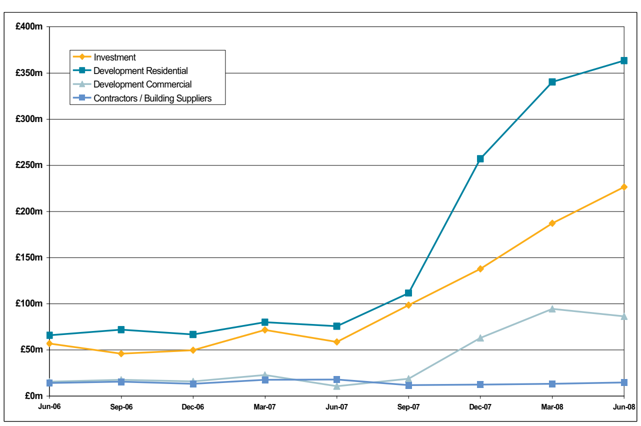
Loss Given Default (LGD)



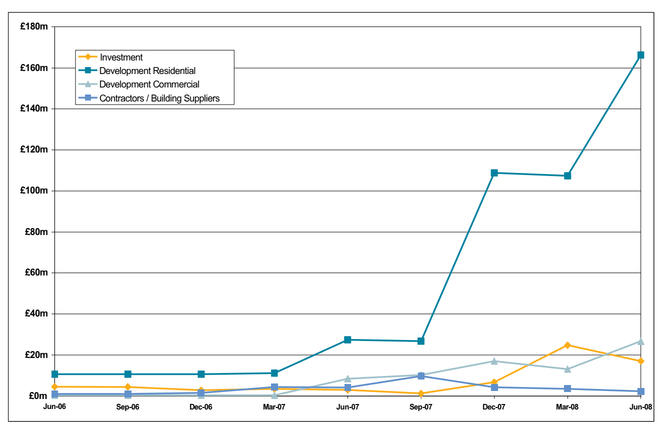
Expected Loss (EL)



LQE Limits (£m)



SLS Limits (£m)



1. UBG Property Portfolio

1.2 Portfolio Analysis

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*Actual growth in limits, n et of sterling movements .

Limits: £21.3bn	This sector represent s 60% of the Corporate Markets Balance Sheet and 3 4% of the UBG Balance Sheet.
Growth: CAGR 45% (31%)	CAGR over last 24 months amounts to 31% when effects of exchange rate movements on the ROI Portfolio are stripped out. Growth occurred predominantly in the 18 months to Dec '07. The impacts of the credit crunch and the slow down in the property market have resulted in an effectively static position in the portfolio in the first 6 months of 2008, with growth rate of 3% driven for the most part by the increased sterling value of the ROI Portfolio due to exchange rate movements.
PD: 1.53% 30bps increase	The average PD 1.53% is equivalent to a D2 Credit grade, having increased from 1.23% at June 06, reflecting the increased risk profile of counterparties operating in this market .
LGD: 14.09% / £3bn 973bps decrease	In common with other RBSG Divisions, UBG experi enced significant volatility in the LGD values in last 18 months due to a combination of system errors (e.g. collateral behind inter company guarantees not being applied to borrower), process errors (e.g. breakdown of security l inkages) and the introductio n of more conservative recovery rates for some types of security (e.g. debentures). Significant remedial work has been undertaken to address these issue s, including system fixes, data clean up and awareness programmes. As a result, average sector LGD is 14.09% (decreased from 23.82%). LGD in absolute terms amount s to £3bn. While security values are not index linked, property values are being reviewed on a case by case where problems are identified and considered / challenged at annual review.
EL: 0.22% / £47m 5bps decrease	EL is in line with historical figures despite significant increase in PD. The static position is a direct result of the reduction in LGD due to actions undertaken to improve data quality. EL in absolute terms amount s to £47m.
Provisions: £110m	Property Portfolio Provisions amount to £110m of which £62m is for individually assessed cases. Provisions are currently being reviewed and a n upward trend is expected over the short to medium term given the current market conditions. Credit Impaired Balances (NAL) £228m represents 1.1% of sector balances. Development sector accounts for £124m, Investment £77m and Contractors / Building Suppliers £26m. LQE designated connections amount to £6 90m. SLS have taken on management of counterparties acc ounting for £2 12m of sector exposure in the last twelve months , of which exposure to the residential development sector account s for £166m.

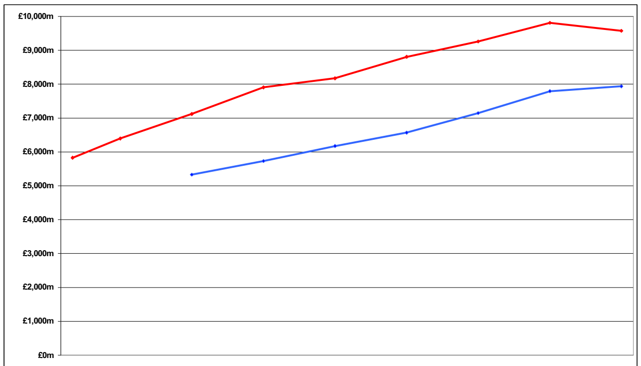
Stressed Provisions: £271m	Sector Concentration Forum has undertaken stress testing analysis by focusing on the provision impact of a downturn in the Irish Property Market assuming a 10 -20% reduction in national house prices over a 12-18 month period. The results indicate potential for additional stressed provisions of £271m on the wholesale book. Most recent stress testing (a severe macro economic shock lasting 2.5 years) carried out on the balance sheet indicates that provisions could increase to 60bps (currently 21bps). We are currently working with Group Enterprise Risk on integrated stress testing of the Commer cial and Residential Property Portfolio which is to be presented to GRC August 2008. Provision levels will be reviewed in light of these results.
Concentration	Top-20 counterparties are listed below. Overall exposure to this group account s for 23% of the sector portfolio. This level of concentration is considered acceptable given the calibre of clients and close working relationships which we have developed over the years. The portfolio is concentrated on the Island of Ireland, with c.10% exposure to the UK market, predominantly within the investment portfolio.

Top 20 Counterparty	Limits £k	Grade	Avg PD	Avg LGD	Avg EL	Avg LGD £k
[redacted]	£566,185	C2	0.47%	12.34%	0.06%	£69,888
	£422,804	C3	0.70%	1.59%	0.01%	£6,713
	£360,115	C3	0.72%	6.64%	0.05%	£23,894
	£358,582	C3	0.58%	3.61%	0.02%	£12,961
	£314,637	D1	0.85%	10.79%	0.09%	£33,962
	£306,735	D2	1.15%	17.80%	0.21%	£54,603
	£277,120	C1	0.32%	5.01%	0.02%	£13,894
	£254,157	D2	2.05%	5.16%	0.12%	£13,111
	£250,261	D2	1.08%	4.59%	0.05%	£11,486
	£228,994	D2	1.29%	5.02%	0.06%	£11,495
Redacted for Relevance	£225,992	C3	0.64%	9.36%	0.06%	£21,152
	£214,471	D2	1.40%	4.49%	0.07%	£9,631
	£171,826	D2	1.40%	11.51%	0.16%	£19,781
	£169,553	D1	0.98%	5.10%	0.05%	£8,646
	£162,665	D3	2.56%	5.00%	0.13%	£8,133
	£159,592	C3	0.64%	6.23%	0.04%	£9,942
	£155,494	D1	1.01%	14.75%	0.15%	£22,935
	£142,637	D1	1.07%	6.44%	0.07%	£9,185
	£130,500	C3	0.64%	16.34%	0.10%	£21,324
	£128,102	C3	0.68%	5.00%	0.03%	£6,405

2. Investment Portfolio (Commercial and Residential)

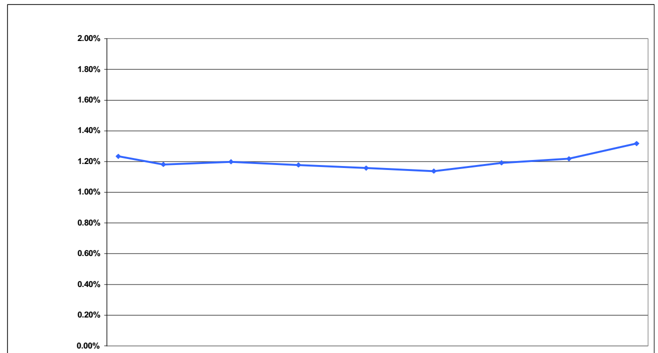
2.1 Portfolio Summary and Management Information

Credit Limits and Utilisations (£m)



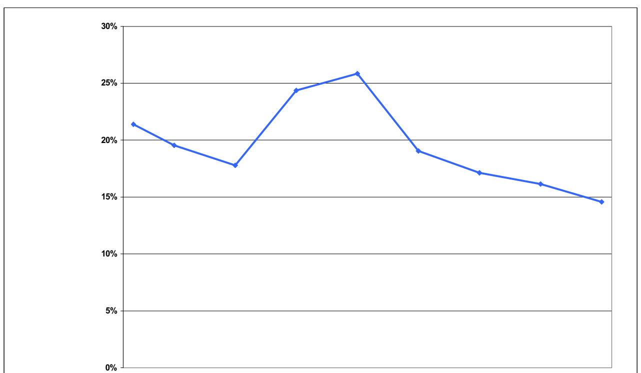
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Limits	5,825	6,395	7,118	7,904	8,171	8,805	9,260	9,810	9,572
Utilisation			5,328	5,728	6,170	6,569	7,142	7,792	7,934

Probability of Default (PD)



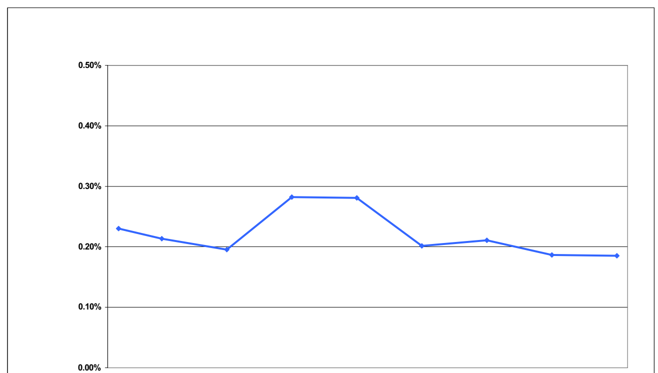
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Probability of Default	1.23%	1.18%	1.20%	1.18%	1.16%	1.14%	1.19%	1.22%	1.32%

Loss Given Default (LGD)



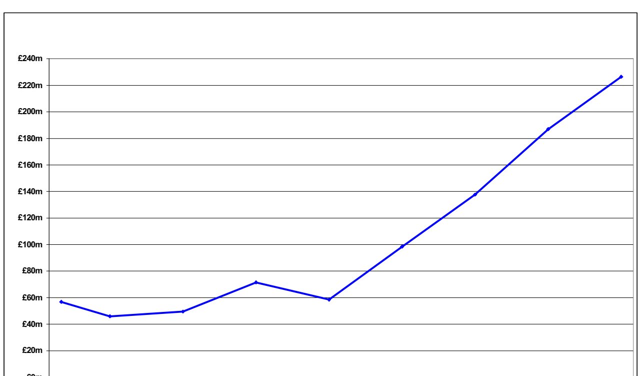
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Loss Given Default	21.38%	19.54%	17.78%	24.36%	25.85%	19.06%	17.13%	16.15%	14.56%

Expected Loss (EL)



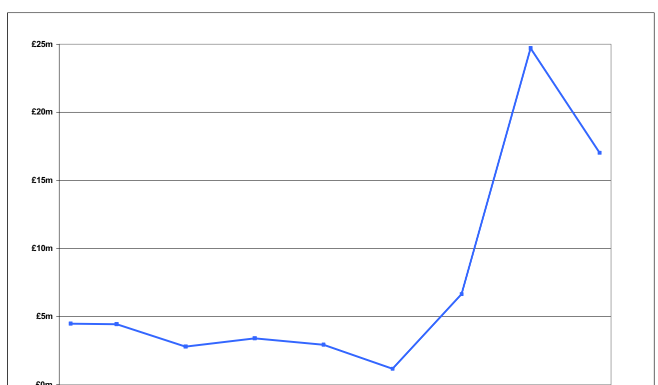
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Expected Loss	0.23%	0.21%	0.20%	0.28%	0.28%	0.20%	0.21%	0.19%	0.19%

LQE Limits (£m)



	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Limits	57	46	50	71	58	98	138	187	226

SLS Limits (£m)



	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Limits	4	4	3	3	3	1	7	25	17

2. Investment Portfolio (Commercial and Residential)

2.2 Appetite Statement / Client Selection Criteria

Commercial Investment	Key Risk Drivers	Positive	Cautious	Negative
Term finance provided on a secured basis against portfolio of commercial assets with associated rental stream.	Location / Infrastructure Asset Quality Tenant / Lease Profile Management / Counterparty Refinance / Resale Value	Office space let to prime tenants in major metropolitan* areas meeting investment financing criteria**.	Office space let to secondary tenants and/or in secondary locations with long-term lease agreements meeting investment financing criteria**.	Office space where leases do not meet investment financing criteria**.
			Belfast Office Space (Workplace 2010***)	
		Retail / Shopping centres let to prime tenants in major metropolitan areas* meeting investment financing criteria**.	Retail / Shopping Centres / Parks / Warehousing with secondary tenants and/or in secondary locations meeting investment financing criteria**.	Assets meeting the speculative policy criteria, not meeting investment financing criteria**.
		Modern industrial units in prime locations close to key infrastructure and let to prime tenant(s) meeting investment financing criteria**.	Multi let industrial units let to secondary tenants and/or in secondary locations meeting investment financing criteria**.	Aged industrial units in secondary locations and/or not meeting investment financing criteria**.
			Single let industrial units with secondary tenant meeting investment financing criteria**.	
Residential Investment				
Investment Facilities Term finance provided on a secured basis against portfolio of residential assets with associated rental stream.	Location Asset Type Market Demand / Competition Tenant / Lease Profile Management /Counterparty Refinance / Resale Value	Mature diversified BTL portfolios demonstrating satisfactory debt servicing and amortisation.	Portfolios that consist of new build apartments in metropolitan* areas.	Portfolios that consist of new build apartments outside metropolitan* areas.
			Developers seeking residential investment facilities to alleviate liquidity pressures where current relationship exits.	Developers seeking residential investment facilities to alleviate liquidity pressures where no current relationship exits.
				Portfolios which are reliant on asset sales for debt servicing.
				Portfolios in locations where rental growth unproven.

*Definition of Metropolitan: Dublin, Belfast, Galway, Cork, Derry, Limerick

**Investment Criteria: A financing scenario where the ability of the borrower to pay all contracted principal and interest payments and / or refinance at contractual maturity is covered by contractual rental obligations / sales which allow an Investment Model payout in line with guidelines.

***Work Place 2010: The planned divestment by the Northern Ireland Civil Service of c.70 properties in its portfolio. Planned as a phased release it will potentially impact on the future demand in the Belfast office market through the greater availability of re-useable space which in turn will affect future rental growth.

2. Investment Portfolio (Commercial and Residential)

2.3 Key Risk Drivers

Investment Commercial	
Location / Infrastructure	• Prime office property is either centrally located in the cities, or in key suburban locations where there is direct access to good public transport and road networks. • Retail space is similar, with highest demand for prime shopping streets in city centres and concentrated out of town areas with strong footfall and public transport. • Demand for industrial space is focused on proximity to good road networks or sea ports depending on the nature of the business, e.g. near to the M1 / M50 motorways.
Asset Quality	• Quality is driven by age, size, specification, flexibility of use and condition relative to competing properties and varies widely from new / modernised to sub-standard, functionally obsolete to over-specialised. It is essential that asset is in keeping with established occupier demand in the location.
Tenant and Lease Profile	• Sustainable cash generation from rental income should reflect lease maturity profile, credit quality of the tenant/s and contractual terms of lease. Where there is significant lease expiry during the term, the assessment may need to be balanced against the other key drivers of location, asset quality and counterparty recourse. • Traditionally, leases in Ireland were on a standard long term (20 -25 year) FRI basis, but there has been a shift in terms in recent years, including shorter lease periods, turnover rents, reviews linked to CPI and more frequent break clauses. Note that onerous conditionality and departure from FRI standard terms impacts on marketability of the asset.
Management / Counterparty	• Key points include nature of business, management experience, track record, borrowing and corporate structure and level of recourse including access to other assets / liquidity. • Consideration should be given to the management intensity of the asset (s).
Refinance / Resale Value	• Refinance risk is directly impacted by the level of sustainable cashflow from the asset beyond facility maturity with further consideration for both interest rate and yield movements during the term. • Refinance risk has increased and ability to distribute debt has reduced due to liquidity issues in the market. As such, robust assessment of sustainable cashflows is crucial in the current climate. • Resale value should be assessed relative to the type and volume of investors likely to be interested in the property under stressed conditions. • Mixed portfolios or portfolios of shorter lease structures require more active management and maybe in lower demand from an individual investor perspective.
Investment Residential	
Location / Asset Type	• Preference is to lend against assets in locations where there are both a high volume of tenants and potential for growth in capital value / rental income, i.e. in cities and large towns. • A spread of assets in the portfolio is attractive, once the asset type and quality is of a modern standard. Caution is required on assets in deprived areas and note that appetite is lower for portfolios with a concentration of new build city centre apartments, particularly if bulk purchased in a single development.
Market Demand / Competition	• Demand is strongest in cities and large towns as tenants favour proximity to employment, universities, public transport and amenities. Majority of demand is for average sized, well located property, with limited opportunities in the corporate market. • It is essential to consider both current rental stock and future supply as some markets are oversupplied with rentals falling and void periods increasing.
Tenant and Lease Profile	• Sustainable cashflow from rental income, should reflect lease maturity profile, credit quality of the tenant/s and contractual terms of lease (as above).
Management / Counterparty	• Preference for promoters with a proven track record of managing residential portfolios, including dealing with tenants, maintenance of the properties and minimising the void periods. The level of experience required will depend on the number / spread of assets within the portfolio.
Refinance / Resale Value	• In recent years, interest cover on residential investment portfolios has been tight except where advances are at low LTVs. The primary repayment source has often come from sales of the assets following capital appreciation rather than by amortisation from asset rental income. This reinforces the importance of adopting a portfolio / connection view where the bank needs to be satisfied with overall liquidity / asset profile in order to achieve refinance / repayment. • A spread of asset types and locations will reduce resale risk and to ensure adequate asset cover, satisfaction will be required that provision has been made for voids, management costs, maintenance and insurance when assessing the relationship between gross and net rental.

2. Investment Portfolio (Residential and Commercial)

2.4 Lending Assessment Guidelines

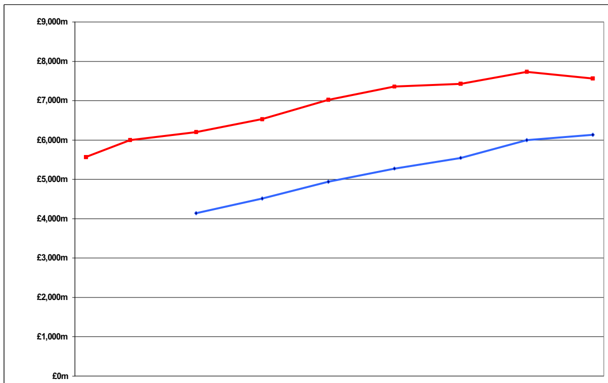
Investment Commercial	
Competitive Environment	• Preference for good quality buildings in areas of high demand (major metropolitan areas) or where there is currently a restricted supply (e.g. regeneration projects) and low rental volatility. • Professional Valuation to include commentary on current levels of investor demand, ERV and supply / demand balance.
Strategy/ Business Model	• Clear management strategy evidenced for the portfolio/property being financed. Management should have an appropriate mix of through the cycle experience and technical skill as well as a track record of active management. • Management must demonstrate appropriate consideration for shift in market conditions/trends and consistent approach to risk-appetite. • Appropriate use of professionals is a key success factor.
Financial Analysis	• Key focus should be in debt service capacity and interest cover. ICR 1.25x, with minimum 1.1x. • Cashflow / liquidity analysis should be based on details of the specific terms of each lease, including lease term, terms and timing of rent reviews, break clauses, notice periods. Details of the tenant background are also required in order to confirm financial strength and track record. Tenant risk to be assessed against overall quality and diversity. • Modelling assumptions again to reflect the specific details of each lease agreement, including adequate allowance for lease expiry, re-letting periods and rental reviews. Consideration to be given to ensuring the property does not become over-rented, as in the event of tenant failure, the rents achievable would return to market level. Only committed rental increases should be included at each review. Allowance for interest rate volatility, beyond any hedging period to be included. • Refinancing Risk to be assessed against the rental income required to amortise the facility over the remaining useful life of the asset. Modelling should also build in residual land value using aforementioned risk assumptions and a default interest rate when hedging expires. • Exit yields provide an indication of whether asset disposal is a feasible repayment option .
Transaction Structure / Tenor	• Tenor should take into account the timing of lease expiries and rent reviews. Guideline typically 5-7 years, with longer tenors considered for the strongest counterparties only and where there is a long lease in place to a high quality tenant. • Covenant Structure to include, but not limited to, LTV, Interest Cover and Debt Service. Guideline covenants of 1.25x ICR (minimum 1.1x), and LTV of 70%. • Bullet facilities to be assessed in conjunction with refinance risk commentary . • Personal guarantees to be corroborated with Net-Worth Statements which outline Guarantors assets, liabilities, income and expenditure. • Hedging strategy should be an integral part of the transaction with consideration given to level, term, rate, and break options. While interest rate hedging can minimise volatility, analysis should also consider the impact on breakage costs for long-dated swaps. Note that refinance risk may be improved if the tenor of hedging exceeds the loan tenor (subject to a credit break, and sufficient security cover to offset breakage costs). Where hedging expires at the point of refinance, consideration should be given to other mechanisms that protect the Banks exit, i.e. covenants, amortisation, etc.
Terms and Conditions	• Banks interest should be protected through strong covenant structure and standard documentation clausing, e.g. interest cover, loan to value, negative pledge, change of ownership, etc. • Right to call for updated valuations to be confirmed in facility documentation. • Rental income to be mandated to the Bank. • Equity/3rd party debt providers positions to be fully subordinated to the Bank debt. • Insurance provisions in compliance with the Bank's Policy.

Investment Residential	
Competitive Environment	• Market demand should be established by way of (a) professional opinion (specific panel estate agent), and/or (b) published market commentary/outlook, and/or (c) local knowledge, and/or (d) Bank's internal research. • Professional Valuations incorporating location profile commentary should be obtained. We need to be satisfied that properties are well located in areas of stable or improving profile. Outlook for current rental stock and future supply should be assess ed as some markets are oversupplied with rentals falling and void periods increasing.
Strategy/ Business Model	• Concentration in a particular location should be avoided or mitigated by other factors which on a portfolio or connection basis mean the Bank is funding an acceptable mix of assets.
Financial Analysis	• Cashflow / liquidity should be assessed on rental income streams and allow for breaks, expiry, voids, management costs, maintenance and insurance when arriving at net rental income. • Details of other income streams and other financial commitments / taxation obligations should be included when arriving at an overall liquidity position. • Repayment capacity should be based on overall cashflow / liquidity taking account of asset profile by reference to (a) interest cover, (b) ability to amortise to an acceptable residual over a 20-year term from rental income alone, (c) loan to value and (d) potential for capital appreciation / repayment of facility from asset sale where a spread of asset types and locatio ns will reduce sales risk.
Transactions Structure/ Tenor	• Tenor should take into account the timing of lease expiries and rent reviews. Longer tenors considered for the strongest counterparties only where re-letting risk is minimised through spread of assets / income and/or where there are leases in place to a high quality tenants. • Covenant Structure to include, but not limited to LTV, Interest Cover and Debt Service. Guideline LTV 75%. • Personal guarantees to be corroborated with Net-Worth Statements which outline Guarantors assets, liabilities, income and expenditure. • Whilst interest rate hedging can minimise volatility, analysis should also consider the impact on breakage costs for long-dated swaps. Note that refinance risk may be improved if the teno r of hedging exceeds the loan tenor (subject to a credit break, and sufficient security cover to offset breakage costs).
Terms and Conditions	• Right to call for updated valuations to be confirmed in facility documentation. • Rental income to be mandated to the Bank. • Equity/3rd party debt providers positions to be fully subordinated to the Bank debt. • Insurance provisions in compliance with the Bank's Policy.

3. Development Residential

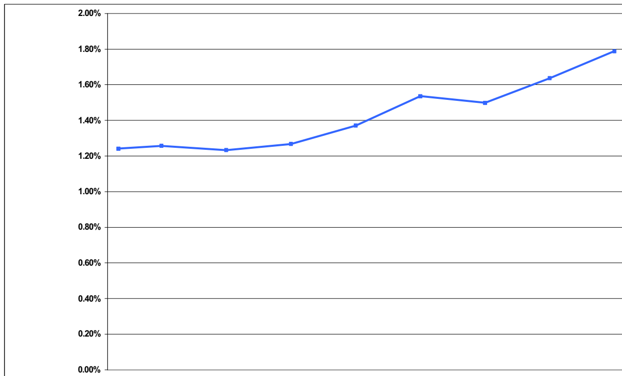
3.1 Portfolio Summary and Management Information

Credit Limits and Utilisations (£m)



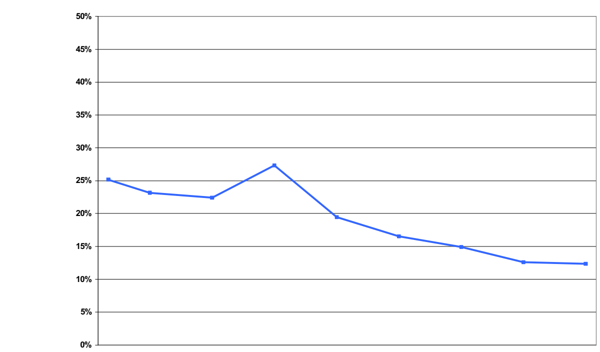
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Limits	5,568	5,997	6,201	6,530	7,023	7,358	7,427	7,735	7,564
Utilisations			4,139	4,513	4,940	5,273	5,544	5,998	6,132

Probability of Default (PD)



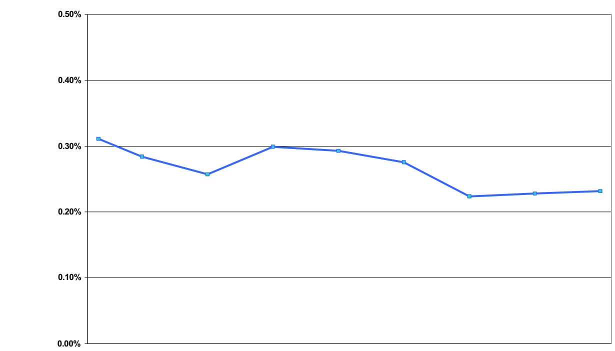
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Probability of Default	1.24%	1.26%	1.23%	1.27%	1.37%	1.54%	1.50%	1.64%	1.79%

Loss Given Default (LGD)



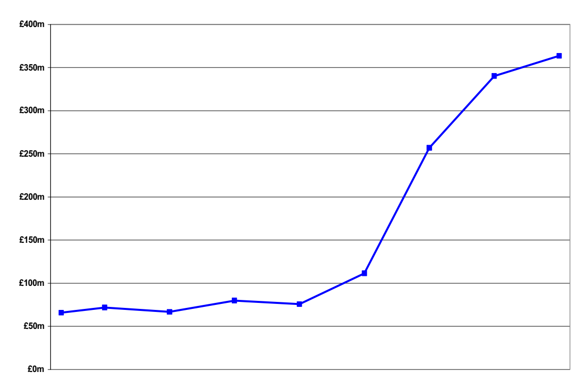
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Loss Given Default	25.15%	23.16%	22.40%	27.31%	19.46%	16.52%	14.90%	12.59%	12.33%

Expected Loss (EL)



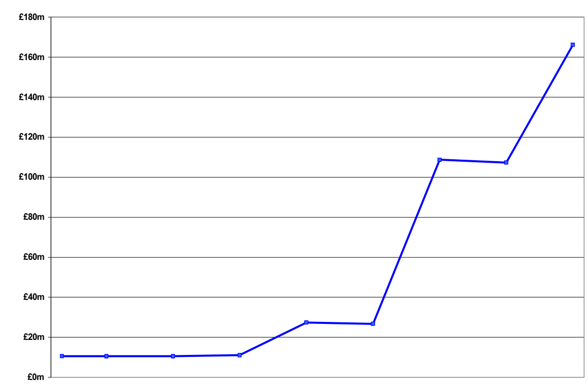
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Expected Loss	0.31%	0.28%	0.26%	0.30%	0.29%	0.28%	0.22%	0.23%	0.23%

LQE Limits (£m)



	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Limits	66	72	67	80	76	111	257	340	363

SLS Limits (£m)



	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Limits	11	11	11	11	27	27	109	107	166

3. Development Residential

3.2 Appetite Statement / Client Selection Criteria

Segment	Key Risk Drivers	Positive	Cautious	Negative
Major Operators • 200+ units p.a. • Diverse sites & geographical concentrations. • JV & SPV structures.	Counterparty / Management Land bank strategy / location / asset / quality / planning approval Market demand / Pre-sales Financial Strength Development Controls	Established operators with multiple sites at varying stages of cashflow.	Secondary or single site locations.	Large apartment schemes outside of major metropolitan* areas.
			JV & SPV transactions without parental recourse.	Investors looking for rights / second charges
		Evidence of sustainable cashflow and liquidity.	Secured facilities with no shareholder recourse.	Equity releases on-non incoming producing assets.
Small & Medium Sized Operators • <200 units p.a. • Fewer sites & geographical concentrations. • Transactions typically site and WIP funding. • JV & SPV structures.	Counterparty / Management Project specific strategy / location / assets quality / planning approval. Market demand / Pre-sales Financial Strength Development Controls	Primary locations with good infrastructure in place.	Secondary or single site locations.	Large apartment schemes outside of major metropolitan* areas.
		Evidence of sustainable cashflow and liquidity.	Planning challenges.	Proposals where total reliance is placed on external professionals.
			Developers seeking Residential Investment facilities to alleviate liquidity issues.	Equity releases on non-incoming producing assets.
			New to Bank developers must have demonstrable track record.	Proposal with no recourse to promoters.
Land bank traders.	Location Financial Strength		Strategic land holdings - zoned with services or with planning permission. Evidence of sustainable cashflow and liquidity.	Unzoned land / White land / Land within development limit (except where acceptable alternative income streams or track record mitigate).

*Definition of Metropolitan: Dublin, Belfast, Galway, Cork, Derry, Limerick

3. Development Residential

3.3 Key Risk Drivers

Counterparty / Management	• Borrowing and corporate structures appropriate to scale of operations and levels of recourse to other assets / available liquidity sources, including a full picture of all other projects / liabilities. • Strong management ability with a broad spread of skills & experience, a clear strategy based on sector & market risks, including a proven track record in managing the planning process and through the cycle risks. Strong land buying and planning team can be a key differentiator. • Access to tradesmen and other skilled / semi-skilled labour can help to minimise cost inflation and avoid construction delays particularly where competitors compete for labour in a tight market.
Land Bank Strategy / Location / Asset Quality	• Primary and strategic locations with good infrastructure in place are key to success. • Effective land bank management strategy, incorporating excellent site assembly ability, is a hallmark of successful residential developers. • Risks of potential oversupply in specific geographical areas exist so that knowledge of the local planning approval profile and existing / proposed developments is required. • Impact of topography or environmental issues need to be considered, in addition to detail on availability and capacity of access and services. • Quality and appropriateness of the units to the location will impact the demand for completed units from home-buyer and investor perspectives.
Planning / Other Regulations e.g. Social & Affordable Regulations	• For sites zoned but without planning, track record in achieving viable planning approvals is key. Noting that the priorities and objectives of Planning Authorities may differ from each other and the differing location and zoning designations, a planning report from an independent consultant may be required. • Planning details should be established by reference to the Planning Approval. The Approval will also set out obligations in relation to Local Authority contributions and provision of Social & Affordable housing units or financial contribution in lieu. • Compliance with relevant building regulations, development controls and bonding requirements are key to successful exit.
Market Demand / Pre-sales	• Demand will be influenced by the current economic climate, market conditions, location and infrastructure quality. Achievement of pre-sales is key in establishing market demand with the ability to repay debt dependant on market demand holding up as the development nears completion.
Financial Strength	• Balance Sheet strength and ability to access alternative funding sources will be a key success factor against downside risks. In the current climate, alternative funding sources are likely to be restricted, therefore close control & monitoring of cash flow is crucial. • Borrower should evidence ability to co-ordinate the development pipeline and sales process to ensure sufficient liquidity to meet commitments. • Borrowers will have to control gearing, including contingent obligations, and have good supply chain arrangements to cushion weakening cash flows.
Development Controls	• Development funding to be agreed on the basis of satisfactory pre-sale arrangements of the completed project or particular phase in a phased scheme. • The objective should be to finance projects where we have visibility to sufficient demand for the units such that bank funding will be repaid at 75% completion stage. • Appropriate controls / rights are required to effectively manage development risk, e.g. signed contracts, experienced contractor, monitoring surveyor, collateral warranties, step-in-rights and cost overrun recourse. • Development should be controlled by way of Projected Cashflow Forecast based on realistic assumptions and accompanied by Building Schedule and Costings. Appraisals should include a contribution to overheads and ensure that VAT receipts / payments are fully taken into account. • Material slippages in sales or costs will impact liquidity and contingency needs to be included within projects costs together with acceptable recourse for cost overruns. • Monitoring Surveyor to report monthly where appropriate with regular visits by Relationship Manager also recommended in the current climate.

3. Development Residential

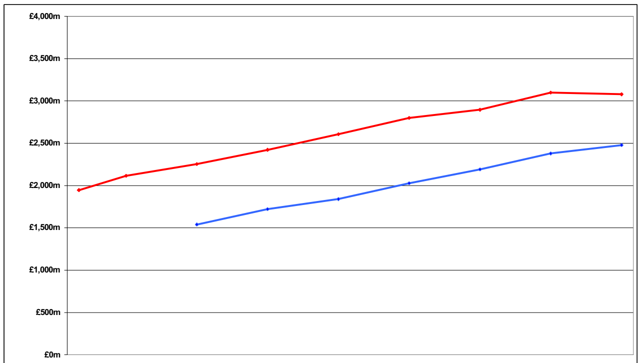
3.4 Lending Assessment Guidelines

Competitive Environment	• House prices continue to fall in both ROI and NI and this trend is expected to continue further into 2009 before levelling off. There are still considerable variances across the island in terms of prices being achieved and it is important to ensure product mix and pricing on development schemes are appropriate and include sensitivities. Niche markets must be monitored noting particularly that a) holiday homes slowdown is likely to continue b) demand for apartments likely to continue to fall outside of major metropolitan areas c) first time buyer and buy-to-let market is constrained by lack of finance. • Knowledge of local planning policy and monitoring of planning granted is essential. Over-zoning in NI western regions has led to a risk of de-zoning. Consultation on the reform of the NI development plan is to take place in H2 2008. There is high planning risk on sites with an over-reliance on significant density uplifts. • Planning Consultants reports on site to be considered where OPP only in place and additionally where there is a risk of de-zoning. • Access to the site and provision of services also critical to appetite. • Product should be comparable to competing schemes and acceptable to the locality, e.g. demand is limited for large apartment schemes outside of major metropolitan areas.
Strategy / Business Model	• Consider sales strategy, appropriate product and pricing mix. Acceptable level of pre-sales are required to validate demand assumptions. • Management should have a proven track record of delivery and ability to react to adverse/changing market conditions. • Assess evidence of succession planning / strong second tier management team and use of external professionals.
Financial Analysis	• Development appraisal should include scheme cashflow with suitable levels of contingency and realistic build costs. • Cashflow assessment should include appropriate level of sensitivity analysis for events such as market slowdown, land-bank holding costs, delays in obtaining planning, change in funding structure and increased cost of raw materials. • Cashflow should be provided at the outset to evidence contribution and reviewed regularly on a rolling basis. Pre-sale deposits should be acknowledged in cashflow but not considered as equity.
Transaction Structure / Tenor	• Tenor per stated timeframe for development plus sales period. >36 months would only be considered for large (200+unit sites). • Loan to Cost (LTC) < 70% which includes land, construction, finance and professional costs. A lower leverage for land-banking should apply in all cases. • Funding should be structured to provide visibility and aid monitoring, with specific loans for land, development and finance. Repayments to come from <75% of unit sales. • Visibility is essential for all Contingent Obligations, e.g. Performance Bonds. Consider amounts, beneficiaries and terms (should generally include a long-stop date). • Debenture and Legal Charge to be taken over whole site. Cautious to deals involving tri-partite agreements or step-in rights only. • Hedging to be taken on core debt level where there is a significant land-bank holding relative to overall facility level.
Terms and Conditions	• Pre-sale deposits should be sufficiently material to discourage purchasers from breaking the contract. Bank should also seek right of veto on multiple pre-sales to one entity/individual on larger schemes funded. • Professional Valuation to be instructed from Panel Valuer as appropriate. Facility documentation to ensure right to revalue at Bank's discretion. • Independent Monitoring Surveyor (IMS) to act for the Bank on all schemes >20 units or where GDV>£5m. IMS to review costs before initial drawdown and provide periodic updates thereafter to ensure undrawn balance of facility is greater than costs to complete at all times. Cost overruns to be reported immediately. • Cost overruns to be for the clients account and acceptable recourse to be held from a satisfactory counterparty (suitable Balance Sheet / TNW). • Personal guarantees to be corroborated with Net-Worth Statements which outlined Guarantors assets, liabilities, income and expenditure. • Bank satisfaction with chosen contractor is conditional. Assess ability to deliver and financial strength. Charge to be taken over the build contract and step-in rights to feature. Collateral Warranties in an acceptable format and to be reviewed by the Banks Solicitor. • Bonds / Guarantees provided against counter-indemnity including clauses allowing Bank to call for cash cover if required and cross-default as appropriate. • Satisfactory insurance cover should be in place, covering public liability, contractors all risks, etc.

4. Development Commercial

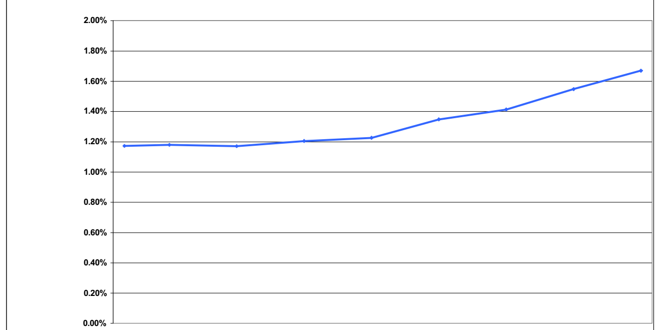
4.1 Portfolio Summary and Management Information

Credit Limits and Utilisations (£m)



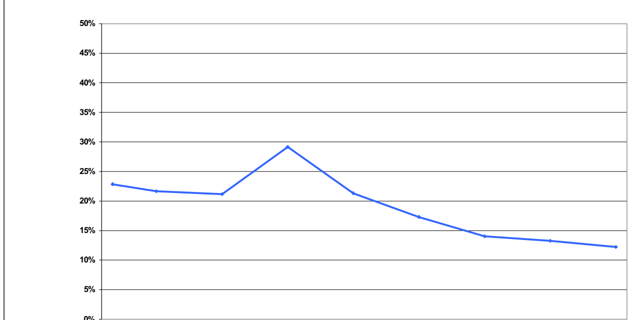
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Limits	1,946	2,116	2,253	2,422	2,607	2,799	2,895	3,098	3,078
Utilisation			1,539	1,721	1,839	2,027	2,190	2,379	2,478

Probability of Default (PD)



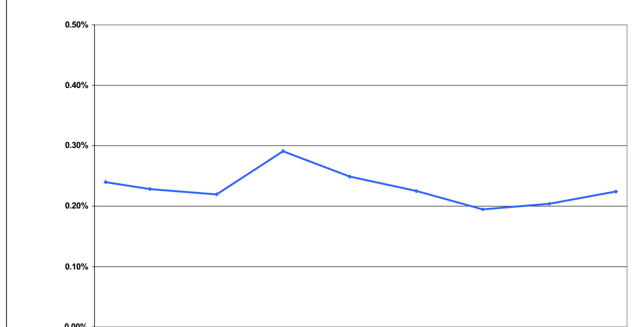
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Probability of Default	1.17%	1.18%	1.17%	1.20%	1.23%	1.35%	1.41%	1.55%	1.67%

Loss Given Default (LGD)



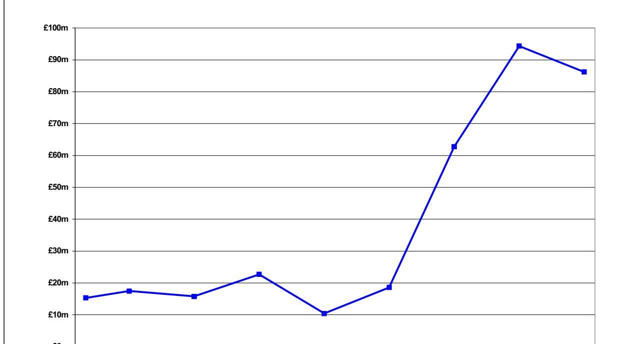
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Loss Given Default	22.83%	21.64%	21.16%	29.14%	21.31%	17.29%	14.04%	13.25%	12.22%

Expected Loss (EL)



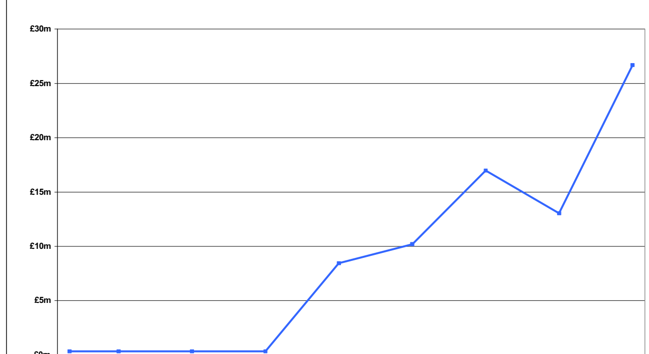
	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Expected Loss	0.24%	0.23%	0.22%	0.29%	0.25%	0.23%	0.19%	0.20%	0.22%

LQE Limits (£m)



	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Limits	15	17	16	23	10	19	63	94	86

SLS Limits (£m)



	Jul-06	Sep-06	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08
Limits	0	0	0	0	8	10	17	13	27

4. Development Commercial

4.2 Appetite Statement / Client Selection Criteria

Segment	Key Risk Drivers	Positive	Cautious	Negative
Finance provided for land and/or development of commercial assets.	Counterparty / Management Location / Asset Quality Planning Risk Complexity of Construction Financial Strength Development Controls Exit / Refinance Risk	Unconditional pre-sale to a known / strong counterparty	Zoned land with services / land with planning permission with suitable mitigants in compliance with Speculative Policy.	Land / Developments meeting the speculative policy criteria.
		Pre-let property meeting Commercial Investment positive appetite criteria.	Pre-let property meeting Commercial Investment cautious appetite criteria.	

4. Development Commercial

4.3 Key Risk Drivers

Counterparty / Management	• Key considerations include the nature of business, strategy based on sector & market risks, management experience, track record (i.e. evidence of completion of projects of similar nature, planning process, building type, size and complexity), borrowing and corporate structure and level of recourse to other assets / available liquidity sources, including a full picture of all other projects / liabilities.
Location / Asset Quality	• Location and asset quality will directly impact on the demand for the completed assets from both investment and tenant perspective. There are risks of potential oversupply of properties in specific geographical areas. • Local infrastructure can have a significant impact on demand and hence valuation. • Consideration also needs to be given to any topography and/or environmental issues, in addition to detail on availability and capacity of access and services.
Planning Risk	• For sites without planning, counterparty track record is key, in addition to the strength of the professional team engaged. Depending on the location and zoning designation, a planning report from an independent consultant may be required.
Complexity of Construction	• Satisfactory site investigation report, environmental report, detailed planning approval and consideration of the skills and experience of the professional design and engineering team for the project are essential to establish risk profile. • Owner builder or a third party contractor must have experience of both scale and complexity for proposed project. Where contractor employed, track record and financial stability are core considerations. • The type/detail of the building contract signed for each specific project will vary and Bank's QS should highlight gaps or potential for variations upfront, in order to allow for sufficient contingency to be included within the budget.
Financial Strength	• Balance Sheet strength and ability to access alternative funding sources will be a key success factor against downside risks. In the current climate, alternative funding sources are likely to be restricted, therefore close control & monitoring of cash flow is crucial. • Level of gearing, including contingent obligations, maintenance of liquidity, and good supply chain arrangements are key to cushion weakening cash flows. • Management and co-ordination of the development pipeline and sales process essential to maintaining liquidity to meet commitments, including contingent obligations.
Development Controls	• Appropriate controls / rights are required to effectively manage development risk, e.g. signed contracts, experienced contractor, monitoring surveyor, collateral warranties, step-in-rights and cost overrun recourse. • Projected Cashflow Forecast based on realistic assumptions and accompanied by Building Schedule and Costings are key control tool. Appraisals should include a contribution to overheads and ensure that VAT receipts / payments are fully taken into account. • Material slippages in sales or costs will impact liquidity and contingency needs to be included within projects costs together with acceptable recourse for cost overruns. • Monitoring Surveyor to provide regular report with regular visits by Relationship Manager also recommended in the current climate.
Exit / Refinance Risk	• Exit / refinance risk can be minimised on the basis that (a) pre-let arrangements of the completed project can meet investment financing criteria and/or (b) an unconditional pre-sale agreement is in place. In both cases, satisfaction with the financial strength of the counterparty, terms of the lease/contract and yield profile in the market will need to be established. • Where pre-lets/pre-sales are insufficient to place the debt on an investment financing basis, funding maybe considered for known creditworthy counterparties with the ability to amortise the debt from other income streams.

4. Development Commercial

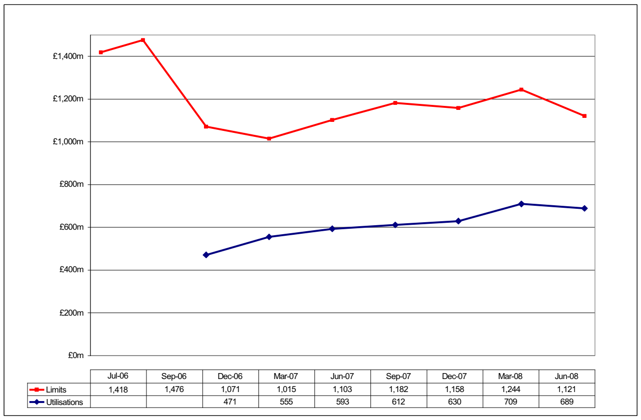
4.4 Lending Assessment Guidelines

Competitive Environment	• Location, infrastructure, and nature of development are key to demand for finished product. • Prime office property is either centrally located in the cities, or in key suburban locations where there is direct access to good public transport and road networks. • Retail space is similar, with highest demand for prime shopping streets in city centres and concentrated out of town areas with strong footfall and public transport. • Demand for industrial space is focused on proximity to good road networks or sea ports depending on the nature of the business, e.g. near to the M1 / M50 motorways.
Strategy / Business Model	• Consider sales strategy, appropriate product and pricing mix. Pre -sale/let or acceptable investment take-out, e.g. into a wider portfolio of properties, assessed per investment f inancing criteria. • Assess management proven track record of delivery on size/scale of project being undertaken. • Assess evidence of succession planning / s trong second tier management team and use of external professionals.
Financial Analysis	• Development appraisal should include scheme cashflow with suitable levels of contingency and realistic build costs. • Cashflow assessment should include appropriate le vel of sensitivity analysis for events such as market slowdown, land-bank holding costs, delays in obtaining planning, change in funding structure, increased cost of raw materials . • Cashflow should be provided at the outset to evidence contribution and reviewed regularly on a rolling basis. Pre-sale deposits should be acknowledged in cashflow but not considered as equity. Financial strength of pre -sale purchaser / pre let tenant should be confirmed.
Transaction Structure / Tenor	• Acceptable tenor generall y 1.5 to 3 years. • Funding should be assessed on a LTC basis which should usually result in an LTV lower than that for typical investment financing reflecting the development risk, i.e. <70%. • Phasing of equity contributions may be agreed only where the equi ty investor is considered undoubted. • Visibility is essential for all Contingent Obligations, e.g. Performance Bonds. Consider amounts, beneficiaries and terms (should generally include a long -stop date). • Debenture and Legal Charge to be taken over whole si te. Cautious to deals involving tri -partite agreements or step-in rights only. • Hedging to be taken on core debt level where there is a significant land -bank holding relative to overall facility level.
Terms and Conditions	• Professional Valuation to be instructed by Panel Valuer with confirmation of exit value where appropriate. Facility documentation to ensure right to revalue at Bank's discretion • Other conditions precedent might include but are not limited to (1) detailed planning consent, (2) independent professional development appraisal , (3) appropriate construction contract (4) assignment of development/build contract, (5) strong cost overrun recourse, (6) step -in rights / collateral warranties and (7) satisfactory lease agreement and/or sales agreement. • Independent Monitoring Surveyor (IMS) to act for the Bank on all schemes and to review development appraisal before initial drawdown and provide periodic updates thereafter to ensure undrawn balance of facility is greater than costs to complete at a ll times. Cost overruns to be reported immediately. • Cost overruns to be for the clients account and acceptable recourse to be held from a satisfactory counterparty (creditworthy Balance Sheet / TNW) or evidenced by comprehensive assets / income statement. • Personal guarantees to be corroborated with Net -Worth Statements which outlined Guarantors assets, liabilities, income and expenditure. • Satisfaction with contractor to be a condition of agreement with same to be assessed based on track record and financial strength relevant to the contract size. Legal team to ensure that collateral warranties and performance bonds are obtained in order to protect the Bank. • Bonds / Guarantees provided against counter -indemnity including clauses allowing Bank to call for cash cover if required and cross -default as appropriate. • Satisfactory insurance cover should be in place, covering public liability, contractors all risks, etc.

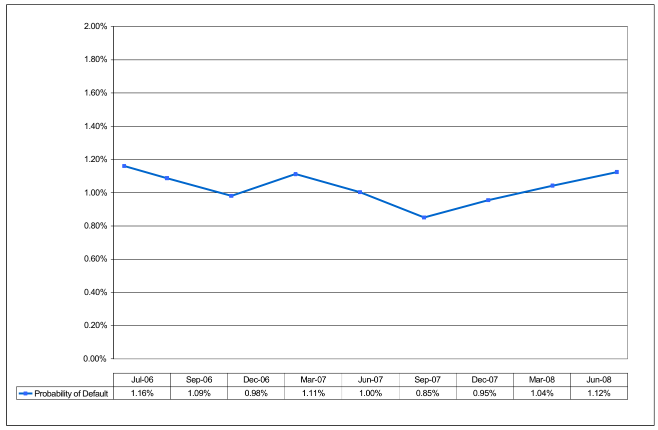
5. Contractors / Building Suppliers

5.1 Portfolio Summary and Management Information

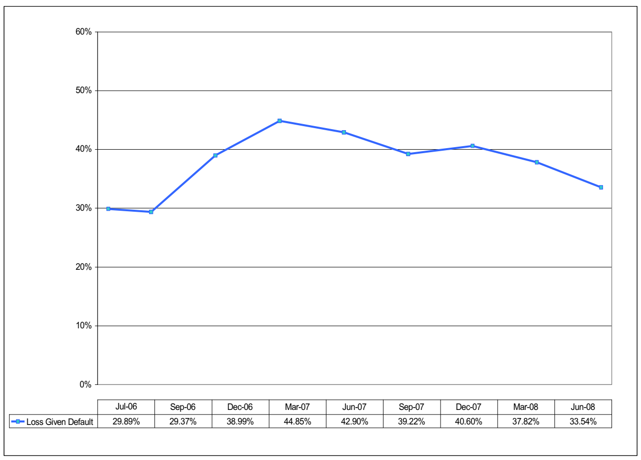
Credit Limits and Utilisations (£m)



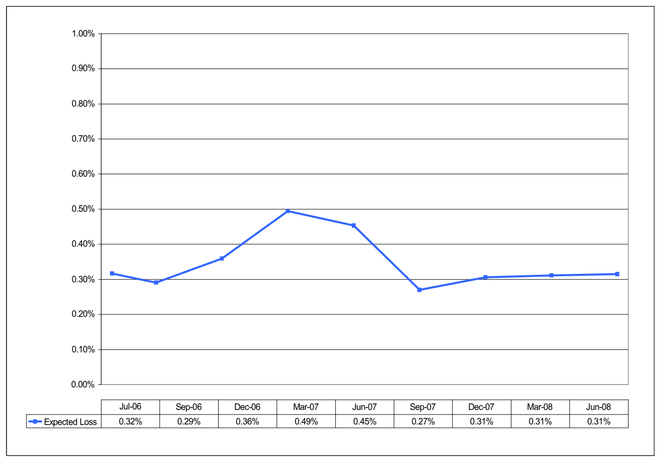
Probability of Default (PD)



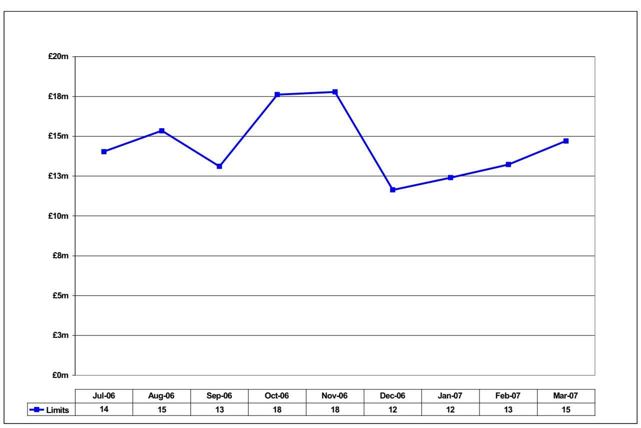
Loss Given Default (LGD)



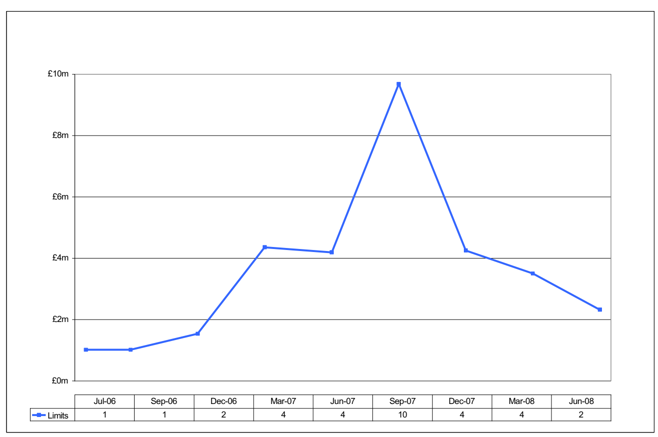
Expected Loss (EL)



LQE Limits (£m)



SLS Limits (£m)



5. Contractors / Building Suppliers

5.2 Appetite Statement / Client Selection Criteria

Segment	Key Risk Drivers	Positive	Cautious	Negative
Core activity – building contractors / material supplies, rental equipment businesses and/or specific trades e.g. plumbers, electricians, etc. Smaller scale operators (family owned).	Diversity of core activities and earnings. Scale and technical abilities. Contract risk management capability. Contract pricing Cashflow Management / Cost Controls / Balance Sheet Reputation. Resource Management	Experienced operators with track record, ability and expertise to win and retain profitable contracts.	Order book heavily concentrated by sector, client or contract type.	Weak relationships with local contractors / subcontractors and weak forward order book.
		Accurate costing of projects and track record on delivery of same.	Evidence of contractual disputes and/or cost-overruns.	A lack of proven success over a sustained period of time.
		Evidence of risk management processes and project control disciplines.		Evidence of taking-on big or complex contracts without necessary experience.
				High incidence of Health and Safety issues.
				Unresolved contracts disputes and frequent calls on bonds.
		Conservative accounting policies and low gearing.	Less conservative accounting policies but low gearing.	Weak balance sheet / high gearing.
		Good quality assets determined by modernity and specification.	Medium quality assets determined by modernity and specification.	Low quality / aging assets determined by modernity and specification.

Contractors / Building Suppliers

5.3 Key Risk Drivers

Diversity of core activities / earnings.	• Scale and diversification of client base reduces risk and generates stable levels of income. However diversification brings risk in management and operational stretch.
Scale and technical abilities.	• The ability to acquire and retain the appropriate contracts commensurate with operating model and capabilities should be evidenced via successful delivery of projects of an appropriate size and complexity.
Contract Risk Management Capability.	• Operators who take primary contractor positions or leading procurement roles are better placed than the smaller less influential firms who will likely occupy sub -contractor positions only. • The forward order book will evidence ability to win wo rk in a competitive environment both when there is a buoyant market and where contracts are scarce. • Robust risk management and control systems are particularly important when involved with more complex projects. Health and Safety record should be carefully assessed.
Contract Pricing	• Consistent accurate costing of projects is a key success factor. • Early locking in of sub contractors essential to maximise profitability. • Fixed price contacts can give rise to difficulties particularly in a highly competit ive market where tendering process may lead to under-pricing and cost overruns. Cost-plus contracts can reduce risk particularly in period of high inflation (although may result in lower margin).
Cashflow Management / Cost Control / Balance Sheet	• Cashflow management and cost control is critical at all levels but particularly important for the smaller operators as cashflow and balance sheet strength are likely to be less robust (with inability to absorb shocks). • Cash conversion is key and level of adv ance payment should be assessed. Ability to effectively manage supply chain/input costs to optimise contract values is essential. • Contingent liabilities, predominantly performance, likely to feature at most levels. Frequent calls on performance bonds / retentions should be considered warning signs.
Reputation	• Reputation issues within the construction industry can have far reaching long term business impact. An established track record of project delivery to time, cost and specification is key success factor. • Membership of relevant industry trade bodies is considered a positive feature (some trades a requirement).
Resource Management	• Demonstrated ability to attract, develop and retain excellent people can help win contracts and increase profitability.

5. Contractors / Building Suppliers

5.4. Lending Assessment Guidelines

Competitive Environment	• Consider the economic regional conditions and the outlook for end user, e.g developers, infrastructure, housing market. • Public infrastructure/procurement spend will a key factor in future demand. In general, those in a position to secure public contracts should be best placed to withstand the downturn. • Track record for delivery of projects will be a key differentiator of operators in a more competitive market. • Rising energy prices and cost inflation for raw materials, e.g. cement and steel, are impacting on ability to compete. There is increased risk in taking on fixed price contracts in the absence of appropriate raw material hedging.
Strategy / Business Model	• Market position relative to peers is key including areas of particular expertise e.g. roads, facilities management, Public Private Partnerships (PPPs) , etc. • Diversification should be assessed on a number of levels: (a) location, (b) client base (across a variety of market segments), (c) contract type, i.e. fixed price v cost plus/partnering (d) income type, i.e. construction, PPP/PFI, consultancy or other recurring revenue streams. • Strategy in terms of business mix moving forward and wider implications needs to be understood; e.g. a move to PPP or similar type projects will involve up-front bid costs and equity commitments which could represent a significant cash commitment. • Expansion outside of known areas of expertise and / or locations carries inherent risks that need to be considered and managed. Our preference is to see controlled well-researched expansion, executed through JV undertakings in partnership with established local operators. • Evidence of rapidly expanding orders and gaining new contracts at the expense of competitors is often a key warning signal and the drivers need to be understood. • Extent of out-sourcing relative to in-house skills and personnel and the risks of failure of key sub contractors / third party service providers to be considered. • Evaluate Control & Risk Management systems where appropriate. • Consider management of Corporate and Social Responsibilities noting increased focus on energy usage, resource usage, waste generation, recycling, water consumption and general impacts on the environment.
Financial Analysis	• An understanding of accounting principles being utilised is required. In long-term contract accounting, the underlying principles for profit recognition under IFRS are: (a) Where the outcome of a contract cannot be estimated reliably, no profit should be recognised; (b) Where a contract is expected to be loss-making, the full estimated loss should be expensed immediately; (c) Revenue and expenses are recognised relative to the stage of completion on the contract e.g. costs incurred to date. • Depreciation policy needs to be understood regarding plant and machinery assets, which are often a significant balance sheet component. • Working capital requirements should be assessed on the basis of cashflow projections taking account that advance payments and cash conversion throughout the period of a contract should be clearly defined and evidenced. Ready release of retentions key to strong cashflow. • Divergence between earnings and cash generation need to be understood. • Operating profit margins tend to be low, and need to be assessed in the context of the relevant peer group. • Gearing is a poor indicator in this sector given thinly (or negatively) capitalised balance sheets . • Balance Sheet impact of a major contract failing should be assessed. • Contingent liabilities (tender / bid obligations and retention / bonding) are likely to be significant. Full details of cover, providers and utilisation need to be obtained and claims history understood. • Disputed contracts should be assessed.
Transaction Structure / Tenor	• Covenant structure to include, but not limited to, cashflow tests, e.g. EBITDA/Net Debt Leverage, Interest Cover, and Balance Sheets tests, e.g. maximum gearing. Non-financial covenants as appropriate, i.e. Change of Control, Pari-Passu, Negative Pledge, cross-default and material change clause. • Bonds to be provided on a demand basis or fixed maturity date basis or committed subject to appropriate financial covenants. • Asset Financing will vary depending on asset type. Tenor typically 5-7 years structured as an operating lease, finance lease or lease purchase as appropriate.
Terms and Conditions	• Satisfactory insurance cover should be in place, covering public liability, contractors all risks etc.

6. Economic Outlook

ROI Economic Outlook	• ROI growth is set to contract by 0.3% in 2008 (from 4.1% in 2007). A return to positive growth of 0.5% is predicted for 2009, followed by 3. 2% in 2010. • The main external factors are global growth forecasts for 2008 have been lowered sharply, the dollar and sterling have each fallen making it more difficult to export, oil and food prices are up significantly and interest rates have risen sharply, eroding disposable income. • The key domestic factor in the turnaround is investment, which is driven by housing, and which is subtracting more than 4% from growth this year. • Market turmoil remains virulent, curbing bank lending, sapping confidence and looks set to continue into 2009. • The 2008 inflation forecast is 5% CPI and 3.9% HICP *. The 2009 outlook is for a sharp fall in the CPI to 3.5%, assuming no more interest rate increases. The HICP * is forecast at 2.7%. • The original 2008 Budget deficit was 0.9% but is likely to overshoot substantially to c. 2.9%. Major cuts in spending will be required to keep the 2009 deficit at the EU 3% limit and the government have embarked on a plan to achieve this . • Housing starts were exceptionally weak in the first six months of 2008. Housing forecast is now 44,000 units for 2008 and 2009 has been lowered to 30,000 (2007 = 78,000). Lower output for a few years is necessary to eliminate the overhang of unsold new houses, currently guesstimated at 35,000 units. • In May, house prices were 11.5% below peak. We expect the m to fall by a further 5% before levelling off. There is a significant risk that price falls could be greater given the recent deterioration in sentiment, higher mortgage rates and reduced credit availability. However, falling prices have boosted affordability. • The outlook for commercial property is similar, albeit that its cycle is about 18 months behind residential.
NI Economic Outlook	• The slowdown in economic activity is evident across all sectors, notably construction, with forward looking indicators such as the Ulster Bank PMI signalling private sector contraction for the first 6 months of 2008. • As a result, economic growth is expected to slow sharply from 2.5% (estimate) in 2007 to just 1.0% in 2008. Economic growth is expected to remain at 1.0 % -1.5% in 2009. • The NI labour market remains remarkably resilient to the current slowdown with Q1 2008 representing another record high for employment. However the rate of employment growth is slowing and job losses, particularly in construction, are expected to accelerate duri ng the second half of 2008. • The unemployment picture has been somewhat mixed. NI's unemployment rate has halved over the last decade and at 3.9% remains below the UK average of 5.3%. However this figure has been quite erratic of late and the claimant coun t measure (those on unemployment benefit) has risen for the last 4 months in a row. The unemployment rate is expected to push through 5.0% this year, although this still remains low by historic standards. • NI house prices peaked August 2007. Since then, house prices have fallen in seven of the last nine months, shedding over 13% to £215k (May 2008). However, it is our opinion that this figure under-represents the true scale of the ongoing correction. Residential property prices have been aggressively reduced, however the lack of housing transactions has kept the average house price figures artificially high. The number of new mortgages fell in the first quarter of 2008 to their lowest level since the late 1970s. Our central view is for NI house prices to fal l by a further 20% which would take the average house price to c.£175k. This would take NI house prices back to 2006 prices which is the level at which estate agents are currently pricing properties. • Falling house prices have improved affordability for t he first time buyers in theory, however, the reduced availability of credit (e.g. lower LTVs) and increasing cost of mortgages is thwarting their entry into the market. For example, average mortgage rates (2yr fixed 95% LTV) are currently around 2% higher than in at the start of 2006 prior to the investor driven boom. Furthermore, the continued surge in energy and food inflation is eroding household disposable incomes. • The NI economy will arguably feel the squeeze more than most other UK regions as NI has the lowest levels of household disposable income after the North East of England.

*HICP: EU Harmonised Index of Consumer Prices which is a measure of internationally comparable inflation (excludes interest ra tes).

THEME: B3

Effectiveness of banks' funding, liquidity strategies and risk management

LINE OF INQUIRY: B3A

Appropriateness of funding sources - the mix, maturity profile and cost

ULSTER BANK LIMITED

Minutes of the meeting of the
Group Asset & Liability Committee on 25th October 2006

Present:	**In attendance:**
M Torpey(Chairman)	B Rickard
C Baird	D Galbraith (Secretary)
P Wilson	
O Breen	

1) Apologies
Apologies were received from Jim Hickey, Colin Kelly, Robert Gallagher, AJ McKeon, Mike Bamber and Dom Williams.

2) Minutes
The minutes of the meeting held on 27th September 2006 were approved.

3) Matters Arising
Issue Log

➢ **Currency Operational Liquidity Reconciliation to Statutory Accounts** DG noted that UB Group Treasury are currently performing reconciliation work reconciling the new UBG liquidity model to the old model. A full reconciliation to statutory / management accounts is to be performed at the 2006 year end. DG noted that a timetable has been discussed with RBS Group Treasury in relation to the new IFR reporting requirements to be discussed under agenda item 7.2.
➢ **UBG Intra Group and Inter Divisional Transfer Pricing Policy** It was previously agreed that review of the UBG policy document would be deferred until later in the year. Issue carried forward to November 2006.
➢ **Currency Operational Liquidity Limits** See agenda item 7.6. Issue closed.
➢ **UBG Interest Rate Risk Management Policy / NII Stress Testing** It was previously noted that review of the UBG Interest Rate Risk Management Policy and NII Stress Testing was to be delayed until post BIC migration to allow for review of new product remappings on the RBS Caustic system. Issue carried forward to November 2006.
➢ **GALCo Monthly Reporting Pack** DG noted that all balance sheet and funding gap analysis has now been updated to include 9&3 reforecast balances plus 2007 reforecasts. Changes to the format of the balance sheet reports are to be considered after review of post BIC migration MI. DG noted that RBS Group Treasury have sent RBS balance sheet analysis for consideration in this review. BR noted that RBS were reviewing the format of RBS GALCo balance sheet analysis and that UB should wait until this was finalised before completing any format changes. Issue carried forward to November 2006.
➢ **GALCo Monthly Reporting Pack** DG noted that capital adequacy analysis has been updated to include 9&3 reforecasts for the next reporting month, December 2006 and June 2007. Issue closed.
➢ **UBG Funding Gap Update** See agenda item 7.7. Issue closed.

4) Ulster Bank Group Monthly Briefing Pack
The Committee noted the monthly briefing pack.

- Spot Balance Sheet (Page 2) – DG highlighted the key spot balance sheet movements and noted that comments on spot movements would be noted in the balance sheet and funding gap analysis sections on pages 8 and 9. Key movements included the following:

Cash & Items in Transit	+£414m (mainly BOE deposit required to be held over September spot month end which fell on a weekend.)

Non Wholesale Loans to Customers	+£1,044m (mainly UBIL corporate lending, UBIL / FA mortgages plus increase due to movement on the euro / stg exchange rate.)
Debt Securities	-£173m (due to reduction in UBL FRNs.)
Intra Group Assets	-£119m (decrease due to reduction in euro funding provided to RBS subsidiaries netted with increase due to movements on the euro / stg exchange rate.)
Deposits by Banks	+£1,264m
Wholesale Customer Accounts	-£619m (change in deposits by banks and wholesale customer accounts reflective of change in mix of FM funding available at spot month end)
Shareholders Funds	+£157m (reflective of circa £100m capital injection transacted in September 2006 and monthly profits.)
ECP Programme	-£194m
Other Debt Securities in Issue	-£230m (primarily due to a reduction in UBL CD issuance.)

- NI Divisionalised Product Analysis (Page 4) – DG noted that assets remain ahead of plan primarily due to significant positive variances in BBNI Corporate & Property and Business Centre lending. Retail mortgages were ahead of plan for the month of September but remain marginally behind plan average year to date. Customer accounts are ahead of plan with marginal increases noted in all divisions.
- RoI Divisionalised Product Analysis (Page 5) – DG noted assets are significantly ahead of plan primarily in the Corporate Markets divisions. Retail mortgages remain ahead of plan however behind plan for the month of September. Customer accounts also remain ahead of plan with major growth in Business Centres and Retail Personal.
- FA Divisionalised Product Analysis (Page 6) – It was noted that First Active loans to customers and customer accounts continue to remain significantly behind plan. It was noted that the strategic plan had assumed that FA corporate lending would be run down rolling off onto the UBIL book.
- Funding Gap Analysis (Page 8) – DG noted that the balance sheet and funding gap now includes 9&3 reforecast balances with key movements to be highlighted on agenda item 7.7. BR queried if forecast balances included SAP initiatives. DG noted that the forecast balance sheet information presented was BAU but that there should be no significant differences as SAP's mainly related to H2 2007 – 2011. MT noted that SAP initiatives had yet to be signed off.

  The UBG non wholesale funding gap has increased £1,263m in the month primarily due to the £372m increase in spot month end cash, £680m increase in corporate lending and £396m increase in mortgages. Changes include increases due to movement on the euro /stg exchange rate.

  The FA funding gap analysis was presented on page 9. It was noted that the FA non-wholesale funding gap had increased by €171m in the month primarily due to an increase in mortgages in the month.
- Key Wholesale Ratios (Page 10) – It was noted that there has been no significant movement in the key wholesale ratios in the month however reliance on wholesale borrowing continues to increase. DG noted that the change requested to this analysis to exclude long term funding e.g. securitisations, FRNs and focus on short term funding less than one year along and the inclusion of forecast balances had yet to be made.
- Capital Adequacy (Page 11) – DG noted the following capital adequacy balances that were not available when the monthly reporting pack was circulated:

Ulster Bank Ireland	Tier 1 Ratio	9.03%
	Total Ratio	9.34%
First Active	Tier 1 Ratio	7.39%
	Total Ratio	10.76%
UBIL Property Sector Concentration		237.4%

It was noted that UBL Solo and UBG balances had yet to be finalised including PNWT balances. DG noted that a full updated reporting pack would be circulated to GALCo including any outstanding balances that had yet to be finalised.

DG noted that the UBG and UBL(Solo) ratios would now include the £100m stg equivalent capital injection transacted in September with partial downstream to UBIL. It was noted that there have been £63m net new contract notes transacted in the month from UBIL to UBL. DG noted that UB Group Treasury are currently reviewing a capital adequacy contingency plan for the year-end with RBS Group Treasury in the event that the

€4bn UBIL securitisation is not transacted in December 2006 as planned. It was noted that an update paper would be submitted to GALCo once finalised. BR / PW queried when a final call would be made on whether the UBIL securitisation would transacted in December 2006 as planned. MT noted that this should be known with certainty by November 2006 mid month. BR requested that GALCo should review the 9&3 reforecast UBG capital plans. DG noted that forecast capital plans would be added to the capital adequacy update paper.

- Risk Weighted Assets (Page 13) – DG noted that risk weighted asset numbers had yet to be finalised.
- Structural Interest Rate Exposures (Page 14) – DG noted that there had been no breaches in the Stg interest rate risk positions. It was noted that Euro interest rate risk positions have yet to be finalised.
- Structural Fx Exposure (Page 15) – DG noted that the increase in the structural fx exposure represents euro profits for the month of September in UBIL and FA, a €100m capital injection transacted in September 2006 plus a conversion of €414m loan stock to ordinary shares in UBIL, UBIH and UBHROI under Project Windswept.
- Sterling Operational Liquidity (Page 16) – No breaches were noted.
- Currency Operational Liquidity (Page 17) – No breaches were noted.
- Top Ten Depositors (Page 18) – DG noted that the [redacted] was UBG's largest depositor at September 2006 month end comprising 5.81% of total deposits. PW queried the deposit classified as Demand and also queried if CBOI repo should be presented on the top ten depositors' analysis. DG agreed to resolve this offline with PW. BR noted that RBS had a database of large depositor information, which enabled analysis by depositor to be undertaken. BR agreed to provide examples of the analysis and also arrange for PW to gain access to the database.

5) Economic Update

- EURO Rates – PW noted that the ECB repo rate had increased 0.25% in October 2006 as expected. It was noted that the market was geared to another increase of 0.25% in December 2006 with another 0.25% 2 months later. PW predicted that the ECB repo rate would peak at 3.75% with most increases completed by Q2 2007. Beyond this it was expected that rates would be flat.
- STG Rates – PW noted that the UK base rate was expected to increase again by 0.25% in November 2006 however it was unclear if the UK base rate would increase further. It was noted that inflation numbers published last week supported this assumption.
- US Rates – PW noted that there was no anticipated changes to US rates however the market were considering a downward movement on rates. PW predicted that US rates would be expecting a period of stable rates.

6) **Margin Analysis**

- Due to apologies from AJM no corporate markets update was provided.
- CB noted that a €850K saving was made in ROI due to the ability to move on ROI product rates a week earlier than planned due to the postponement of the BIC cutover weekend. CB noted that deposit margins had widened however it was expected that these would be held into 2007. CB noted that FA mortgage margins were under pressure. It was noted that there had been a reduction in CAM mortgage margins by 0.14% due to migration changes, which would have an annual cost of €2.5m. It was noted that SVR mortgage gross rates had been increased by 0.25%, which would incur an annual cost of €4.5m. CB noted that NI margins remained steady. MT queried if the pricing of deposits would be expected to have any impact on the deposit volume base. CB noted that UB depositors did not tend to be significantly rate sensitive and no significant reduction in volumes was anticipated.

7) Special Issues

7.1 UBG Deposit Growth Initiatives

- PW noted that volume increase in wholesale deposits in 2006 had been well sustained with a potential increase in deposits for the remainder of 2006. PW noted that AJM was championing deposit growth initiatives with immense pressure in the intensely competitive market. PW noted that the corporate markets teams were reviewing fixed rate deposit products over the coming month with the intention to rebrand and repackage existing products.

7.2 IFR Liquidity Regulatory Requirements

- DG highlighted the timetable established by Group Treasury in relation to ongoing work to cater for the new IFR liquidity requirements. BR expressed concern over the timetable particularly in relation to training and the position UBG would be in at 01 January 2007. MT queried when changes would be live. BR highlighted that the IFR required reporting to begin from 01 January 2007 but UBIL and FA would not become subject to the limits until 01 July 2007. BR noted that discussions were still ongoing in relation to obtaining limit exemptions for UBIL and FA as part of the integrated RBS group with both the IFR and FSA still to reach agreement on the issue.

7.3 UBG Funding Gap Review

- See agenda item 7.7.

7.4 UBL / UBIL Risk Transfers / Sectoral Concentration

- DG noted that the project manager had met with the project sponsors (MT and John MCDonnell) with a paper to be submitted to EMB in the next month. It was noted that work had commenced refining SIC code classifications with a workshop to be scheduled to review what AIB and BOI are doing. It was noted that once the EMB paper is completed that this would be circulated to GALCo for review. MT added that the ongoing work formulating classification rules had yet to be bottomed out and was a slow task, but highlighted the importance of this piece of work that would be under scrutiny going forward.

7.5 UBG Corporate Structure Review

- DG noted that as part of the Project Windswept restructuring process, during September, UBHROI distributed the majority of its reserves (£178m) up to UBIH. It is expected that UBIH will then dividend these reserves along with the remainder of UBIH's reserves up to UBL during the course of October and November.
- DG noted that on the 28th September UBIL made an early repayment of €414m Tier II capital to UBHROI and issued an equivalent amount of ordinary shares which has been subscribed for by UBHROI. UBHROI have also repaid €414m Tier II capital to UBIH and issued an equivalent amount of ordinary shares which has been subscribed for by UBIH on the same day.
- It also planned UIL will transfer its shareholding in UBIH to UBL during the course of October / November in order to streamline the ownership of UBIL and ensure that no inappropriate gearing will result upon cessation of solo consolidation treatment. Reorganisation of the Ulster Bank Group will be considered in 2007 to identify the optimal structure.

7.6 UBG Operational Liquidity Cashflow Limit Request

- PW presented the paper following on from the temporary increase in limits approved in Q2 2006. PW noted that limits had been agreed with Graeme Niblock (RBS Head of Global Money Markets) with a phased clawback of UBF limits agreed with PW, BR and CK following decisions to reduce the level of euro funding provided to RBS subsidiaries from the ECP programme. PW requested GALCo to approve the limits as highlighted on the paper.
- GALCo approved the limit changes.

7.7 / 7.8 UBG Funding Plan Update

- DG noted that as highlighted on the update paper retail mortgages and corporate markets lending is forecast to grow at significant levels over the next 5 years albeit at reduced growth levels to 2006. It was noted that this was not coupled with growth in customer accounts, which continue to lag behind asset growth. Key funding strategies to bridge the growing funding gap were highlighted:
  - (a) A net €1bn increase in FRN issuance over the next 5 years.
  - (b) Continued utilisation of securitisations. Over the next 5 years it is expected that UBG will raise a net £22bn of funding from securitisation. Imminent forecasts include the €4bn UBIL securitisation to be completed in December 2006, a further FA Celtic deal of €2.5bn in Q2 2007 plus a €1bn FA buy to let deal.
  - (c) Increase in Mortgage Backed Promissory Notes.
  - (d) Reduction in euro funding provided by the ECP programme to RBS subsidiaries for use within UBG.
  - (e) Corporate markets deposit initiatives totalling £9bn over the 5 year forecast.

- DG noted other sources of funding and key risks associated with the funding plan.
- BR queried the risks associated with securitisations and UBG's ability to generate suitable assets for securitisation given the level of MI required for this. BR also noted that the £9bn target set for raising corporate markets deposits was challenging. BR however did highlight that there may be additional scope for ROI companies to borrow from UK companies within the RBS Group going forward. Currently intra group lending outwith the UK was governed by breaking the rest of the world into 4 blocks. The RBS integrated UK Group can then lend a given amount to each block. However, RBS had formally applied to the FSA to increase the number of blocks from 4 to 6. This increases the overall quantum of lending by 50% although lending to each block is still restricted to 75% of the UK capital base. The FSA's response is awaited. DG noted the other sources of funding that could be potentially used to mitigate these risks such as the €5bn increase in the ECP programme, US Commercial Paper and FRN issues.

- BR also highlighted the RBS were currently reviewing funding potential within the group with assessments to be undertaken on the reliance on unsecured short term funding. BR also highlighted the stress testing requirements under Pillar II of BASEL II and noted that work would be commencing on reviewing stress-testing scenarios in relation to funding. OB noted that CK had already set up a meeting to discuss this issue.
- MT queried the future of the securitisations market under BASEL II and their continued use within RBSG in the long term. BR noted that RBS were looking at different structures such as covered bonds. It was noted that work was ongoing with concentration on Nat West and RBS books at present.
- MT also noted that the BAU forecast balance sheets had been signed off however the SAP element of the forecast had yet to be signed off and it would be unlikely that this would be finalised by next week.

7.9 UBG Project Derby

- MT presented the paper for approval highlighting that the proposal did not change the risk positions of the group re the indemnities.
- GALCo approved the proposal.

8) Emerging Issues

- BR noted that work had commenced reviewing BASEL II stress testing as highlighted earlier in the meeting. It was also noted that capital plans and intra group limit consolidated plans were currently being reviewed by RBS.
- BR also noted that Paul Stanley (AIB) would be giving a presentation to ALMA in relation to the introduction of new liquidity requirements and agreed to send details to DG/CK for consideration.

9) Any Other Business

- DG noted that currently FA and UBIL prepare capital on a consolidation basis only. Under the new IFR Capital Requirements Directive it would appear that this consolidation will no longer be readily available and application would have to be made for Solo Consolidation similar to FSA rules. DG noted that draft documentation issued in May/June 2006 had implied that UBIL and FA could continue under the existing consolidation basis however the revised requirements are more vague. It was noted that UBG are currently in discussion with the IFR in relation to this which could be effective as early as 31 December 2006 however this would be pushed backed strongly and a dispensation applied for to delay implementation to June 2006. DG noted that the key issue arose on foreign owned subsidiaries where any dividend of capital up the reporting group would result in tax leakage e.g. FA UK which could result in a £50/£60m loss of capital temporarily within the FA capital returns. DG noted that a further update would be given to GALCo once final confirmations received from the IFR. DG noted that UB Group Treasury was investigating possible solutions to this issue.
- DG also noted that consideration was being given to move the scheduled UBG GALCo meetings to the first Wednesday of the next reporting month to enable collation of final capital adequacy MI. UB GALCo members agreed to this proposal. BR agreed to raise this within RBS to consider if this created any issues for RBS Group Treasury.

The chairman called the meeting to a close.

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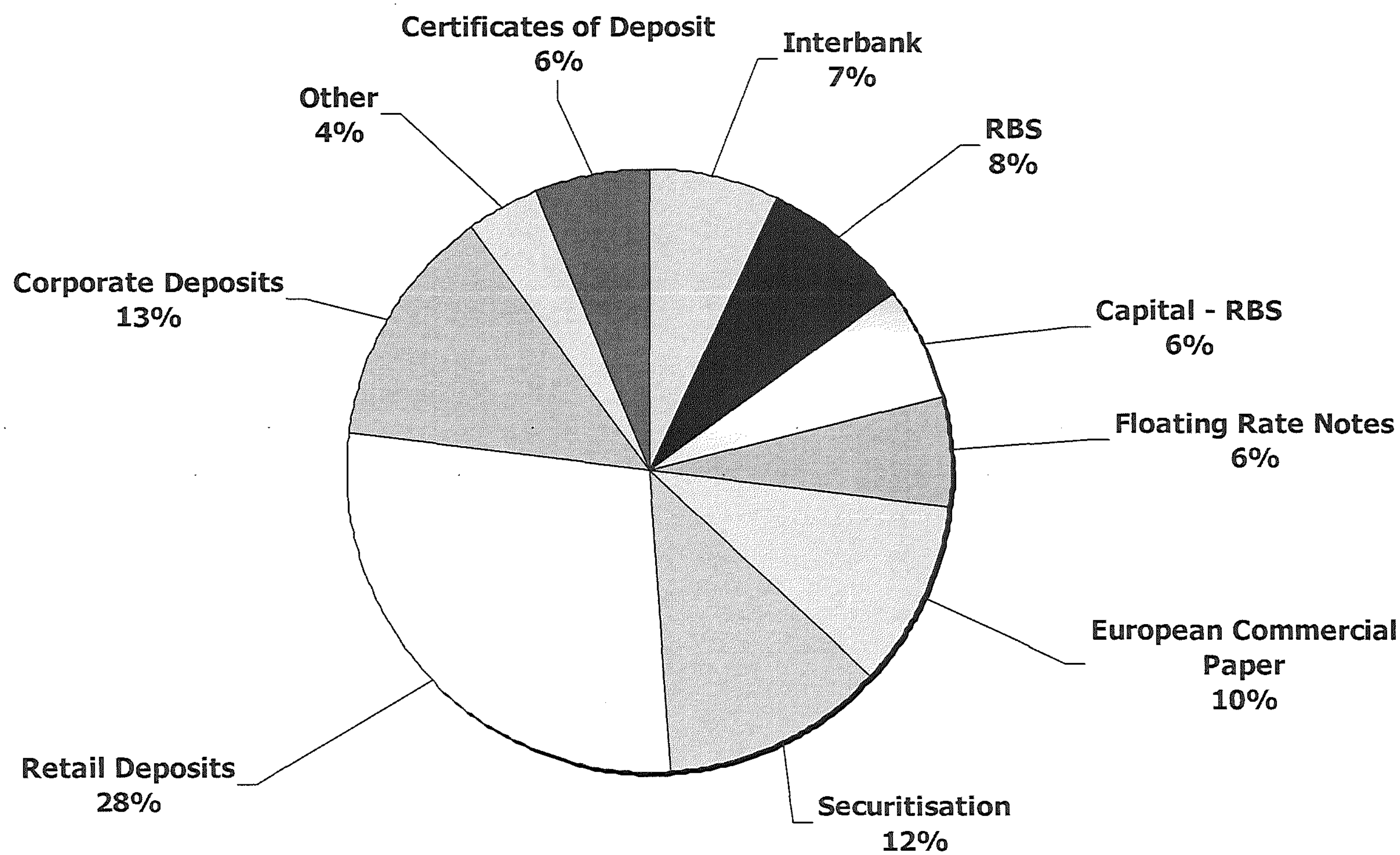
M Torpey
Chairman

GALCO Issues Arising From Previous Meetings

Date First raised (Minute reference)	Issue	Responsibility	Date to be reported back to GALCO
Apr 2005	Currency Operational Liquidity Reconciliation to Statutory Accounts – DG noted that UB Group Treasury are currently performing reconciliation work reconciling the new UBG liquidity model to the old model. A full reconciliation to statutory / management accounts is to be performed at the 2006 year end. DG noted that a timetable has been discussed with RBS Group Treasury in relation to the new IFR reporting requirements to be discussed under agenda item 7.2. Issue open under reconciliation work completed.	CK / DG	November 2006
Apr 2006	UBG Intra Group and Inter Divisional Transfer Pricing Policy - It was previously agreed that review of the UBG policy document would be deferred until later in the year. Issue carried forward to November 2006.	DG / PL / BR	November 2006
July 2006	UBG Interest Rate Risk Management Policy / NII Stress Testing – It was previously noted that review of the UBG Interest Rate Risk Management Policy and NII Stress Testing was to be delayed until post BIC migration to allow for review of new product remappings on the RBS Caustic system. Issue carried forward to November 2006.	DG	November 2006
August 2006	GALCO Monthly Reporting Pack – DG noted that all balance sheet and funding gap analysis has now been updated to include 9&3 reforecast balances plus 2007 reforecasts. Changes to the format of the balance sheet reports are to be considered after review of post BIC migration MI. DG noted that RBS Group Treasury have sent RBS balance sheet analysis for consideration in this review. BR noted that RBS were reviewing the format of RBS GALCo balance sheet analysis and that UB should wait until this was finalised before completing any format changes. Issue carried forward to November 2006.	DG	November 2006

UBG Funding Breakdown – September 2007



Total Resources Stg£51bn

Ulster Bank Group

Minutes of the meeting of the
Group Asset & Liability Committee on 10th September 2008

Present:	In attendance:
M Bamber	S McMonagle (Secretary)
O Breen	G Roseingrave
D Corbett (Chairman)	
R Gallagher	
P Tancred	

Apologies

Apologies were received from John McDonnell, Senan Murphy, Bill Rickard and Peter Wilson.

1. Previous Meeting

a) Minutes

- DC noted that the FRN approved at the June meeting did not proceed due to lack of investor appetite and it is probable that this transaction will proceed in 2009.
- The minutes of the meeting held on 16th June 2008 were approved.

b) Actions

- May 2008 (1.3) – Calculation of ROCE:
  - DC noted that the calculation of ROCE has been completed but that the final calculation needs to be confirmed with David Hourican and Claire Baird.
  - Action carried forward.
- June 2008 (1.5) – FRN/Securitisation Timeline:
  - DC noted that a maturity profile has now been incorporated into the GALCO pack. DC confirmed that a repricing timetable will be brought to the October meeting.
  - Action carried forward.

2. Balance Sheet Management

a) Balance Sheet Forecast

- MB requested that the current and forecasted funding gap (which will include use of the Intra Group Limit line) be clearly shown. Action added to Action Log Ref 1.6.
- MB questioned if there is a possibility that the funding gap at 2008 year end will be larger than that at 2007 year end. DC explained that this is a possibility. DC to revert with an updated view on this at the next GALCO. Included in Action Log Ref 1.6.

b) Liquidity & Funding

(ii) Contractual Funding Maturity & Funding Contingencies

- DC noted that approx 60% of Ulster Bank Group's liabilities mature within 1 year and therefore is very short dated funded.
- RG questioned how UBG compares to RBS. DC noted that RBSG is in a short dated funded position also therefore a new Liquidity Policy has been drafted to improve the position. (See Section 4(a) for further discussion)
- RG noted that securitisations should run off over the life of the transaction and this is not shown in the matrix. DC agreed and noted that this would be incorporated in October's GALCO pack. Action added to Action Log Ref 1.7.
- MB requested that a plan be included to show how UBG intend funding the maturing liabilities. Action added to Action Log Ref 1.8.
- MB noted that pledging of securitised assets to the ECB was listed under the funding contingencies and questioned if it was probable that the ECB would impose restrictions to this line of funding as a result of recent media reports. DC noted that the ECB have announced that they will issue funding at 88% of collateral pledged with effect from February 2009 (previously 98%). DC noted that it is possible that the ECB will bring in other restrictions in the future.
- MB questioned the cost of pledging securitised bonds to the ECB. PT noted that UBG have not yet drawn funding and that the recent auction for funding from the ECB was circa 4.61% for 3 months i.e. 3 month Euribor - 0.30%. DC noted that having these bonds gave liquidity benefit and allowed UBG to fund at shorter maturities i.e. 1 month Euribor.
- MB requested a paper be brought to GALCO on the various elements of funding in order to improve understanding and the funding strategy of UBG. Action added to Action Log Ref 1.9.

(iii) Celtic 14 – First Active and UBIL Securitisation

- DC presented the paper on the proposed up to €7bn Celtic 14 securitisation.
- DC noted that the current value of the proposed securitisation is €5bn.
- RG questioned why this securitisation would be done as it would result in additional cost but with no access to new investors. RG also noted that mortgages are currently pledged directly to the ECB and questioned what the benefit would be of doing the securitisation. DC noted that there is currently a Mortgage Backed Promissory Note Programme with the ECB but that the mortgages eligible to be pledged through this scheme are restricted (e.g. maximum LTV is 80%). There will be a larger pool of mortgages available for pledging through the securitisation vehicle.
- DC noted that the cost of the securitisation would be approximately £1m. DC also noted that RBS intend on charging 0.10% for assisting with the transaction but that UB Group Treasury are currently challenging this charge.
- MB noted that the cost of 0.10% (€5m cost based on a €5bn deal) from RBS is unacceptable and that this should be escalated to Cormac McCarthy if UB Group Treasury are unsuccessful in agreeing a reduction.
- The members agreed to approve the transaction. The RBS transaction charge for Celtic 14 must be challenged before launch of the transaction.

(iv) Liquidity Stress Testing Report – May 2008

- DC presented the paper on the liquidity stress testing carried out as at May 2008.
- OB noted that if one stress was to occur it may result in other stresses (e.g. if the wholesale market was to collapse it would also result in there being no access to the CP or CD market). DC noted that the stress calculation for there being no access to the wholesale market included the collapse of the CP and CD markets.
- DC noted that each stress is taken in isolation.
- The members approved the paper.

3. Capital Management

c) Restructure of Preference Shares Issued By Ulster Bank Ireland (Holdings)

- DC presented the paper on the restructure of the preference shares issued by Ulster Bank Ireland (Holdings).
- DC noted that it is proposed to change the shares from Preference Shares to Ordinary Shares.
- MB noted that the Boards of the companies involved must sign off the proposed restructure and prior to sign off would seek assurance that all legal issues were satisfactory.
- The members approved the paper.

4. Any Other Business

a) GALCO Terms of Reference

- DC presented the GALCO Terms of Reference.
- RG noted that liquidity and funding are currently the most important issues affecting UBG and they are given insufficient coverage in the Terms of Reference (e.g. there is no reference to minimising the cost of funds).
- RG noted that there is confusion in UBG with regard to the funding strategy and that this needs to be documented. Included in Action Log Ref 1.6.
- RG noted that Finance should deliver a funding plan that displays the current and optimal funding mix. RG also noted that the business plans should be done in parallel with the funding plan. Included in Action Log Ref 1.6.
- DC noted that RBS will be issuing a new liquidity policy but it has not yet been approved by RBS GALCO. DC explained the draft policy requires the following:
  - A liquidity buffer to be held by RBS, the cost of which will be allocated to the divisions.
  - Some matched funding of assets will be introduced.
  - Assets must have the ability to be securitised or easily sold to 3rd parties i.e. easily removed from the balance sheet.
- DC noted that the timeline for implementation of the policy, when approved, has not yet been distributed by RBS.
- RG and MB requested that a copy of the draft liquidity policy be sent to them. Action added to Action Log Ref 1.10.

- RG noted that it was his opinion that all of the funding costs should not be transferred to the business in order to ensure that Finance have an incentive to keep the cost of funds low.
- The Terms of Reference were not approved and will be brought back to GALCO at a later date. Action added to Action Log Ref 1.11.

The chairman called the meeting to a close.

D Corbett
Chairman

ACTION LOG

Date First raised (Minute reference)	Issue	Responsibility	Date to be reported back to GALCO
May 2008 (1.3)	**Calculation of ROCE** – Group Treasury to liaise with Retail and Corporate Finance Delivery Teams in order to agree ROCE for those divisions.	DC	October 2008
June 2008 (1.5)	**FRN/Securitisation Timeline** – Group Treasury to include a timetable of Securitisation and FRN repricing in the GALCO pack.	DC	October 2008
Sept 2008 (1.6)	**Reporting of Funding Gap** – • Group Treasury to display the current and forecasted funding gap as part of the Balance Sheet Forecast in the GALCO pack. • Highlight if the funding gap at 2008 year end will be larger than that at 2007 year end. • Clarity and documentation required around the funding strategy. • Deliver a funding plan with the current and optimal funding mix.	DC	October 2008
Sept 2008 (1.7)	**Inclusion of Securitisation Run Offs in Funding Maturities Matrix** – Group Treasury to incorporate the run off of Securitisations in the UBG Funding Maturities Matrix.	DC	October 2008
Sept 2008 (1.8)	**Funding of Maturing Liabilities** – Group Treasury and Money Markets to show how UBG intend funding the maturing liabilities	DC & PT	October 2008
Sept 2008 (1.9)	**Funding Elements** – Group Treasury to bring a paper to GALCO on the various elements of funding in order to improve understanding and the funding strategy of UBG	DC	November 2008
Sept 2008 (1.10)	**Liquidity Policy** – Group Treasury to forward the draft version of the RBS Liquidity Policy to Mike Bamber and Robert Gallagher	DC	October 2008
Sept 2008 (1.11)	**Terms of Reference** – Group Treasury to update GALCO Terms of Reference	DC	November 2008

ULSTER BANK IRELAND LIMITED

BALANCE SHEETS
as at 31 December 2007

	Notes	Group 2007 €m	Group 2006 €m	Bank 2007 €m	Bank 2006 €m
Assets					
Cash and balances at central banks	7	**293**	166	**293**	166
Treasury and other eligible bills	7	**1**	1	**1**	1
Loans and advances to banks	7	**24,315**	11,433	**18,460**	12,413
Loans and advances to customers	7	**36,476**	31,999	**35,082**	30,627
Debt securities subject to repurchase agreements		**28**	1,146	**15**	1,146
Other debt securities		**1,289**	295	**1,302**	295
Debt securities	7, 10	**1,317**	1,441	**1,317**	1,441
Equity shares	7, 11	**13**	8	**13**	8
Investments in Group Undertakings	7, 12	**-**	-	**29**	29
Derivatives	7, 15	**1,372**	1,050	**1,350**	992
Intangible assets	7, 13	**43**	49	**35**	42
Property plant and equipment	7, 14	**211**	177	**208**	173
Prepayments, accrued income and other assets	7, 16	**99**	209	**76**	188
Deferred taxation	7, 18	**21**	27	**21**	27
Total assets		**64,161**	46,560	**56,885**	46,107
Liabilities					
Deposits by banks	7	**34,022**	16,142	**32,529**	16,142
Customer accounts	7	**17,492**	22,983	**17,283**	25,904
Debt securities in issue	7	**7,492**	3,875	**2,219**	8
Derivatives	7, 15	**1,702**	1,025	**1,596**	983
Accruals, deferred income and other liabilities	7, 17	**224**	168	**219**	869
Retirement benefit liabilities	7, 3	**111**	109	**111**	109
Deferred taxation	7, 18	**6**	15	**6**	15
Subordinated liabilities	7, 19	**541**	12	**541**	12
Total liabilities		**61,590**	44,329	**54,504**	44,042
Equity					
Minority Interests	21	**85**	80	**-**	-
Shareholders' equity:					
Called up share capital	20, 21	**1,047**	643	**1,047**	643
Reserves	21	**1,439**	1,508	**1,334**	1,422
Total equity		**2,571**	2,231	**2,381**	2,065
Total liabilities and equity		**64,161**	46,560	**56,885**	46,107
Memorandum Items					
Contingent liabilities:	27				
- acceptances and endorsements		**-**	-	**-**	-
- guarantees and assets pledged as collateral security		**9,336**	5,114	**9,336**	5,114
- other contingent liabilities		**265**	338	**265**	338
Total contingent liabilities		**9,601**	5,452	**9,601**	5,452
Commitments: - other commitments	27	**8,229**	6,421	**8,229**	6,421

The accounts were approved by the Board of Directors on 14February 2008 and signed on its behalf by:

N Brennan
Chairman

C McCarthy
Group Chief Executive

S Murphy
Group Finance Director

M Mullen
Secretary

THEME: B4

Impact of the property valuation methodologies on banks' credit risk management

LINE OF INQUIRY: B4c

Adequacy of internal controls over perfection of security and policy exceptions

Group Internal Audit

Dublin Mortgage Centre

December 2006 – Final

Ulster Bank Group, Manufacturing

Make it happen

The Royal Bank of Scotland Group

www.group.rbs.co.uk/gia

To:

Richard Hemsley

Rob Pike

John West

From:

Dick Palette

cc:

Ken Kennedy

Paul Molumby

Audit Team:

Peter Brazier (Team Leader) and a team of auditors

Executive Summary

Dublin Mortgage Centre was established in May 2006 and is responsible for processing all mortgage business for First Active, Ulster Bank Ireland Ltd (Republic of Ireland) and for the legacy book of Ulster Bank Ltd (Northern Ireland).

In recent months the centre has experienced considerable change including the migration to the Group Mortgage System (GMS) in June and Ulster Bank integration in October. This together with staff inexperience, weak centre management and cultural issues amongst the staff all combined to threaten operational stability and accordingly, service delivery. Changes have now been made to the management team. Issues identified by them and Manufacturing Risk, including reconciliations, concerns management, workflow and training are either under incident management or being prioritised into a plan to recover and stabilise the operation.

We have also identified the following:

- Weaknesses in how the payment messaging system (ServiceLink) is administered; local Systems Administrators could set up unauthorised user accounts and use these to input and authorise (release) a fraudulent payment up to €10 million or multiple payments up to the overall daily limit of €60 million for the centre without detection. Management responded immediately to close this gap. Controls in the payments process are also inadequate and ineffective; poor ServiceLink performance has led to payments being released without an effective check of the payment beneficiary details in all cases to enable payments to be processed before cut-off. Reconciliation controls are currently deemed ineffective albeit recovery action is underway. In addition a number of instances of non-compliance with the Payment Security Standards were identified e.g. authentication tokens are regularly left on desks. This further increases the risk of a fraudulent or inaccurate payment being made. We have raised this as a **Major Issue. See Issue 1 Appendix 1.**

We have also raised six **Significant** issues:

- Completeness checks made before draw down of new mortgages are not robust or controlled. The potential exists for a mortgage to be drawn down before all terms and conditions or documentation requirements have been completed. **See Issue 2 Appendix 1.**
- Control of documentation required to obtain legal title over mortgaged properties is inadequate and ineffective. Legal documentation e.g. guarantees or solicitors undertakings is held in the wrong legal entity name i.e. Ulster Bank Ltd and not Ulster Bank Ireland Ltd in whose name the debt is held. Additionally, GMS has no capability to monitor receipt of deeds or for return of deeds which have been sent out to solicitors. The group may therefore be left in an unprotected position in the event that a mortgage falls into default. **See Issue 3 Appendix 1.**
- A clearly defined process or controls for the handling of non-performing debt is not currently in place. The centre is unaware of the overall level of arrears within the mortgage book or how much is actually at risk i.e. where a shortfall exists in security against the actual level of indebtedness. We found weaknesses in security taking, recording and monitoring procedures across the centre which potentially mean that higher than expected levels of shortfalls exist. **See Issue 4 Appendix 1.**
- Mortgage Manager access controls are inadequate and a member of staff could obtain access to set up a further advance and authorise a payment up to €1 million. A check of payments instructions over €1 million would detect a fraud. **See Issue 5 Appendix 1.**
- Physical security procedures, including the managing of passes, confidential waste and adherence to clear desk policy is weak. Similar weaknesses were found in our audit of First Active last year and whilst improvements were made, these have not been sustained. **See Issue 6 Appendix 1.**

- The centre is unable to complete the Quarterly Risk Certification accurately as the risk management framework is inadequate and management has been unable to accurately identify the level of risk in the centre. Whilst a structure is in place, risk awareness is poor and inconsistent. **See Issue 7 Appendix 1.**

We have reduced the scope of the audit to allow for the establishment and embedding of the recovery activity which we propose to monitor. See **Appendix 2** for details of the processes we have excluded.

<table>
<tr><th>Control Issue No 2.</th><th>Action Plan</th><th>Date</th></tr>
<tr><td>Mortgages are processed to completion without sufficient consideration being given to whether all terms and conditions, and documentation requirements, have been satisfied

Classification : Significant

Enterprise Risk Type : Processes</td><td>Owner: Rob Pike, Director, Ulster Bank Manufacturing</td><td></td></tr>
<tr><td>Issue
Before a new mortgage can proceed to completion, standard terms and conditions (T&Cs) as well as specific T&Cs applicable to individual cases must be satisfied to provide the bank with effective cover in the event that the mortgage subsequently falls into default or the borrower is unable to maintain repayments (e.g. on death).

The 'end to end' process does not require an overall completeness check prior to drawdown. Individual tasks throughout the process are handled by a number of staff across a number of departments within the mortgage centre e.g. valuations & offers, completions, underwriting. Checking, and the notes on file, are insufficient at each stage to validate that prior tasks have been completed correctly before case progression or that individuals discretionary limits have been observed.

The current process does not require (or result in) full copies of the Mortgage Offer Letter (OL) being held on file, either in paper form or electronically. For switcher mortgages (remortgages) the current process does not require the centre to have sight of the signed OL at all.

As a result:
1) Mortgages are being drawn down before all T&Cs and documentation requirements have been completed which, could lead to the bank being unable to rely on legal recourse to either the customer, other guarantors or third party service providers should the need arise e.g. in the case of default;
2) The absence of full customer accepted documentation e.g. offer letters could also leave the bank exposed to loss or reputational damage in the event of a customer dispute. The need to retain a full copy of the OL is a legal requirement and any breach could result in legal censure;</td><td>Working party to be established with responsibility for preparing a detailed action plan. This plan, to be published by 20/01/07, will be linked with ongoing work within Mortgage Operations on process re-engineering.

Once plan has been agreed and implemented controls will be monitored through regular AYIC testing. Generic AYIC testing to be supplemented by DMC specific AYIC testing where appropriate.</td><td>Interim Milestone Date
20/01/07

Completion date
20/06/07
Issue target closure date
15/07/07</td></tr>
</table>

Control Issue No 2.	Action Plan	Date
3) Insufficient audit trails could also make meaningful internal testing difficult or could hinder customer service if the notes are unclear to a third party e.g. telephonist. **Detail** Our file sample of 20 completed Ulster Bank (RoI) mortgages cases from the period 16th August to 13th November identified: • One file [redacted] where the facility was sanctioned on the basis that it was in the joint names of the principal applicant and a relative whose income was relied upon as a guaranteeing party. The property was to be purchased in the sole name of the principal applicant. The mortgage was completed in the sole name of the principal applicant meaning that the bank has no recourse to the other party in the event of default; • One file [redacted] where the buildings cover arranged on the property is below that recommended by the valuer (also outside of the 10% discretion allowed); • Three files [redacted] where the actual valuation received was lower than that expected. Whilst the impact on the loan to value (LTV) is minimal, no evidence is on file to suggest that these differences were identified and recorded as valid exceptions; • 13 files where a full copy or customer signed copy of the OL are not held on file; • Valuation reports have been received that are addressed to Ulster Bank Limited rather than Ulster Bank Ireland limited; • 1 file where the underwriter has sanctioned the use of a non panel valuer without having the necessary discretion to do so; and • In the majority of files reviewed, the quality and detail input into the GMS system made an independent review from input to completion very difficult to undertake. Within the end to end process we are advised that staff have discretion to act outside of policy in completing certain process requirements e.g. on receipt of a valuers report staff can accept the valuation if it is lower than expected if the difference is less than 10%. We have been unable to locate any documentation that effectively sets out what discretions are available within the E2E process and to whom they have been granted. The absence of effective process checking also means that compliance is not being validated.		

Control Issue No 3.	Action Plan	Date
Control of documentation required to obtain legal title over mortgaged properties is inadequate and ineffective Classification : **Significant** Enterprise Risk Type : **Processes** **Issue** Control of documentation required to obtain and retain proper legal title over mortgaged properties is inadequate and ineffective. Legal documentation e.g. guarantees or solicitors undertakings is held in the wrong legal entity name i.e. Ulster Bank Ltd and not Ulster Bank Ireland Ltd in whose name the debt is held. GMS has no system to monitor receipt of deeds or diary system to monitor for return of deeds which have been sent out to solicitors. Deeds under the legacy system have not been chased for receipt for approximately 4 years and a prior exercise to chase was undertaken without records being updated. As a result legal documentation may not be available or could be unenforceable resulting in financial loss in the event of default or need to force a sale of the property. **Detail** Specifically we found: <u>Documentation</u> • Solicitor's undertakings and power of attorney documents refer to Ulster Bank Limited in cases where indebtedness is to Ulster Bank Ireland Limited. Guarantee forms taken in support of borrowing are in favour of Ulster Bank Limited in cases where the lending is by Ulster Bank Ireland Limited; • In the event a second charge is completed (on legacy Northern Ireland cases) the customer's signature is not checked on the mortgage questionnaire and no check is made to see if our security covers any other Ulster Bank Group borrowing;	Owner: Rob Pike, Director, Ulster Bank Manufacturing Working party to be established with responsibility for preparing a detailed action plan. This plan, to be published by 20/01/07, will be linked with ongoing work within Mortgage Operations on process re-engineering. Once plan has been agreed and implemented controls will be monitored through regular AYIC testing and reporting. Generic AYIC testing to be supplemented with DMC specific AYIC testing where appropriate.	Interim Milestone date 20/01/07 Completion date 20/06/07 Issue target closure date 15/07/07

Control Issue No 3.	Action Plan	Date
<u>Security / Documentation Records</u> • GMS has no system to monitor receipt of deeds or diary system to monitor for return of deeds which have been sent out to solicitors. Deeds under the legacy system have not been chased for receipt for approximately 4 years and a prior exercise to chase was undertaken without records being updated; • The figure quoted in respect of our reliance on the security is given as that of the outstanding mortgage balance with no check being made to see if any other Ulster Bank borrowing is covered by the charge, thereby weakening the bank's security. • Deeds, in some cases, are held offsite but records indicate that they are still awaited with the result that we cannot rely on our records. Plans have been discussed to undertake a full review but this will be a lengthy exercise and no timescale or resource availability has been agreed.		

<table>
<tr><th>Control Issue No 4.</th><th>Action Plan</th><th>Date</th></tr>
<tr><td>A clearly defined process or controls for the handling of non-performing debt is not currently in place.

Classification : Significant

Enterprise Risk Type : Processes

Issue
A clearly defined process or controls for the handling of non-performing debt is not currently in place. The centre are unaware of the overall level of arrears within the mortgage book or how much is actually at risk i.e. where there is a shortfall in security against the actual level of indebtedness. We found weaknesses in the security taking, recording and monitoring procedures across the centre which potentially mean that higher than expected levels of shortfalls exist.

The timely and complete monitoring or recovery of arrears is ineffective due to volumes of work and a lack of clear supervision / overview. The process to identify arrears cases is heavily manual and no check for completeness is made.

The process for handling deceased customers is split across four teams. Ownership of specific cases is accordingly unclear and action is inconsistent across the teams. A log of deceased customers is not maintained and following receipt of notification, no system to monitor repayment is in place.

As at 9/11/06 there were 1950 UB RoI mortgage cases in arrears by one or more repayments. Total balances across these accounts are €332m with €84m in arrears for three months or longer. Only those that have been in arrears for longer than 8 months are being chased with action often consisting only of a telephone call or letter to the customer.

As a result:
Ineffective and inconsistent treatment of arrears and recoveries cases could lead to reputational damage and / or financial loss. In addition untimely or incomplete action could lead to the Groups position being weakened with other creditors being given preference. The level of arrears or provisions could also be incorrectly stated in Ulster Bank's or First Active's annual accounts; and</td><td>Owner: Rob Pike, Director, Ulster Bank Manufacturing

Working party to be established with responsibility for preparing a detailed action plan. This plan, to be published by 20/01/07, will be linked with ongoing work within Mortgage Operations on process re-engineering.

Once plan has been agreed and implemented controls will be monitored through regular AYIC testing and reporting. Generic AYIC testing to be supplemented with DMC specific testing where appropriate.</td><td>Interim Milestone date
20/01/07

Completion date
20/06/07

Issue target closure date
15/07/07</td></tr>
</table>

Control Issue No 4.	Action Plan	Date
• Ineffective and inconsistent treatment of deceased cases could lead to reputational damage through emotional stress to the representatives of the deceased and/or financial loss to the Group.		

THEME: B5

Impact of the remuneration arrangements on banks' risk management

LINE OF INQUIRY: B5a

Adequacy of the incentive and remuneration arrangements to promote sound risk governance

Banking Inquiry

Remuneration schemes linked to commercial real estate and/or residential real estate loan volumes – for the period 2001 – 2008

Companies covered:

- Ulster Bank Ireland Ltd
- First Active

Ulster Bank Ireland Ltd 2001 - 2008

1. Remuneration schemes

The Bank rewarded staff through the use of Discretionary and Incentive based remuneration schemes.

Any reward scheme in place rewarded both financial and non financial performance supporting the business strategy. The schemes measured business and individual performance against targets that were specific, measurable, set at the beginning of the year and communicated to employees. Any variable reward/bonus pools created would have been assessed against the context of a range of performance metrics (a “balanced scorecard”).

The incentive schemes in place were reviewed and approved through a Variable Pay Committee (VPC) in the parent company RBS. Payments made through the scheme were as a result of employees meeting the performance criteria outlined in the scheme (see table in section 3).

For those on Discretionary schemes allocation of any variable award depended on individual performance and on each employee’s performance rating. Ratings were based on an assessment of performance in the round, against a full range of measures including both financial and non-financial measures.

Employees participated in either scheme and no employee would have been permitted to be rewarded through both schemes at the same time.

2. Discretionary scheme – scope

Under the reward arrangements in place during this period a discretionary bonus opportunity was restricted to managerial staff; this was based on performance against a range of performance measures. Within the Retail and Corporate Banking areas, although we don’t have documents detailing the objectives, it would be reasonable to assume that these performance measures would have included Commercial/Residential real estate loan volumes. Changes were made to the bonus arrangements at individual manager level from 2005 onwards, but not broadly across the Bank until 2007 onwards.

3. Incentive Schemes

From our records we can see that Incentive schemes were in operation in Retail and Corporate Banking during, but not for the total period under review. The table below shows the schemes we believe were in place during the period. Whilst we don't have documented evidence it would be reasonable to assume that the financial measures would have included Commercial/Residential real estate loan volumes.

Business Area	**Scheme**	**Date Available**	**Measures**
Retail	Performance Plus Branch Banking – all staff below Branch Manager level	2002 onwards	Service Sales Balance Growth Customer Retention
Retail	Incentive Scheme Area Managers	2006 onwards	Financial targets Operations Efficiency Customer Satisfaction People Satisfaction
Retail	Incentive Scheme Branch Managers	2007 onwards	Sales Balance growth Customer numbers Customer Service Control measures People measures
Corporate	Corporate Banking and Property Finance (incl First Active) Relationship Managers levels A – D	2006 onwards	Tier 1 & 2 Income Customer Acquisition Operational measures People measures

Corporate	Commercial Area Managers	2006 onwards	Tier 1 & 2 Income Customer Acquisition Operational measures People measures
Corporate	Wealth Wealth Managers	2008 onwards	Financial income targets People Customer Operational Excellence
Corporate	Business Centres Commercial Officers	2007	Performance objectives and rating

First Active 2001 – 2008

1. Discretionary scheme – scope

During this period First Active paid Discretionary Bonus linked to Manager Contract as follows:

- Up to 10% of base Salary based on a satisfactory performance against business objectives for role.
- Up to 20% of base Salary for Senior Managers based on a satisfactory performance against business objectives for role.

During the period following the purchase of First Active by Ulster Bank (2004 onwards) a discretionary bonus scheme was introduced for managers who were not part of an incentive scheme; this was based on performance against a range of performance measures. Whilst we don't have documented evidence it would be reasonable to assume that the financial measures within the Corporate Banking area would have included Commercial/Residential real estate loan volumes.

2. Retail Incentives

From our records we can see that Incentive schemes were in operation in First Active - Retail during, but not for the total period under review. The table below shows the schemes we believe were in place during the period. Whilst we don't have documented evidence it would be reasonable to assume that the financial measures would have included Commercial/Residential real estate loan volumes.

Business Area	Scheme	Date Available	Measures
First Active - Retail	Incentive All Branch Staff: Manager Loan Advisor Savings & Loans Advisor	2002 - 2008	Net Interest Income Non Interest Income Activity Management Customer Satisfaction
First Active - Retail	Incentive Area Managers	2002 - 2008	Net Interest Income Non Interest Income Activity Management Customer Satisfaction
First Active - Customer Service Unit	Incentive Team based incentive	2004 – end date not known	Service Levels Branch Satisfaction ratings Customer Satisfaction ratings

Bonus Details for FA Top Role holders - 2001-2003

ID Number	First Name	Surname	Employee Description	Year	Bonus	Exec Share Option scheme (ESOS)	ESOS option price
[redacted] Customer Information						80000	€2.86
			Employee 14	2001	65,000	300000	€1.90
						50000	€2.65
			Employee 15	2001	45,000	200000	€2.14
						120000	€2.86
			Employee 34	2001	25,000	30000	€2.65
						50000	€2.86
			Employee 35	2001	25,000	22500	€2.65
						120000	€2.86
			Employee 20	2001	25,000	30000	€2.65
						120000	€2.86
			Employee 37	2001	25,000	30000	€2.65
			Employee 36	2001	0	75000	€ 2.91
			Employee 18	2001	0	150000	€ 2.91
			Employee 34	2002	84,137	58000	€ 3.75
			Employee 20	2002	72,085	60000	€ 3.75
			Employee 18	2002	50,000	210000	€ 3.75
			Employee 35	2002	0	25500	€ 3.75
			Employee 14	2002	0	100000	€ 3.75
			Employee 15	2002	0	100000	€ 3.75
			Employee 36	2002	0	85000	€ 3.75
			Employee 38	2002	0	200000	€ 4.90
			Employee 14	2003	257,250		
			Employee 15	2003	224,543		
			Employee 18	2003	10,700		
			Employee 38	2003	10,160		
			Employee 34	2003	8,916		
			Employee 20	2003	8,333		
			Employee 35	2003	0		

Bonus Details for UB Top Role holders - 2001-2008

ID Number	First Name	Surname	Employee Description	UBL/UBIL	Year	Converted £ to €	Exec Share Option scheme (ESOS)	ESOS option price	MPP	RSP
[redacted]			Employee 1	UBL	2001	178726	16,000	£17.18	25,229	
			Employee 2	UBIL	2001	178250	4,700	£17.18		
			Employee 3	UBL	2001	81187	8,900	£17.18		
			Employee 4	UBL	2001	72359	6,600	£17.18		
			Employee 9	UBL	2001	69480	8,400	£17.18		
			Employee 5	UBL	2001	61526	6,500	£17.18		
			Employee 34	UBL	2001	60299	6,500	£17.18		
			Employee 6	UBL	2001	44461	4,700	£17.18		
			Employee 7	UBL	2001	41003	5,100	£17.18		
			Employee 13	UBL	2001	32160	5,600	£17.18		
			Employee 2	UBIL	2002	263529	3,300	£18.18		
	Employee Information		Employee 1	UBL	2002	262405	15,200	£18.18	16,137	
			Employee 4	UBL	2002	107349	6,200	£18.18		
			Employee 3	UBL	2002	92637	8,500	£18.18		
			Employee 9	UBIL	2002	79371	7,100	£18.18		
			Employee 34	UBL	2002	72082	3,750	£18.18		
			Employee 5	UBL	2002	71247	6,200	£18.18		
			Employee 13	UBL	2002	50930	5,100	£18.18		
			Employee 35	UBL	2002	50930	5,100	£18.18		
			Employee 6	UBL	2002	47312	4,700	£18.18		
			Employee 1	UBL	2003	108382	25,100	£12.37	9,002	
			Employee 11	UBL	2003	85983	10,200	£12.37	3,630	
			Employee 12	UBL	2003	73812	7,900	£12.37	3,775	
			Employee 28	UBIL	2003	71000				
			Employee 13	UBIL	2003	46332	9,400	£12.37		
			Employee 7	UBL	2003	43280	6,100	£12.37		
			Employee 5	UBL	2003	42486	9,800	£12.37		
			Employee 6	UBL	2003	41185	8,300	£12.37		
			Employee 8	UBIL	2003	29332				
			Employee 19	UBIL	2003	4300				

ID Number	First Name	Surname	Employee Description	UBL/UBIL	Year	Converted £ to €	Exec Share Option scheme (ESOS)	ESOS option price	MPP	RSP
[redacted]			Employee 14	UBIL	2004	450,000	22,100	£17.34	17,612	
[redacted]			Employee 1	UBL	2004	274,053				
[redacted]			Employee 3	UBL	2004	141,447	9,900	£17.34	3,432	
[redacted]			Employee 11	UBL	2004	88,248	10,100	£17.34	4,037	
[redacted]			Employee 7	UBL	2004	87,644	5,800	£17.34	2,019	
[redacted]			Employee 19	UBIL	2004	86,422	3,327	£17.34		
[redacted]			Employee 12	UBL	2004	77,354	7,800	£17.34	2,725	
[redacted]			Employee 13	UBIL	2004	72,416	8,600	£17.34	3,425	
[redacted]			Employee 6	UBL	2004	71,437	3,028	£17.34		
[redacted]			Employee 5	UBL	2004	67,825				
[redacted]			Employee 14	UBIL	2005	500,017	30,163	£17.29	20,109	
[redacted]			Employee 15	UBIL	2005	229,618	18,475	£17.29	7,390	
[redacted]			Employee 3	UBL	2005	124,305				
[redacted]			Employee 16	UBL	2005	119,538	11,929	£17.29	4,772	
[redacted]			Employee 17	UBIL	2005	99,358				
[redacted]			Employee 18	UBIL	2005	96,186	11,864	£17.29	2,373	
[redacted]			Employee 6	UBL	2005	93,308	8,169	£17.29	1,634	
[redacted]			Employee 13	UBIL	2005	89,518	7,842	£17.29	3,922	
[redacted]			Employee 19	UBIL	2005	86,422	9,250	£17.29	1,851	
[redacted]			Employee 20	UBL	2005	81,781	7,541	£17.29	3,771	
[redacted]			Employee 14	UBIL	2006	577522	30,597	£18.52	20,399	
[redacted]			Employee 17	UBIL	2006	427361	18,544	£18.52		3,709
[redacted]			Employee 27	UBIL	2006	226400				
[redacted]			Employee 16	UBL	2006	132023	12,149	£18.52		2,430
[redacted]			Employee 26	UBIL	2006	117506	9,040	£18.52		1,809
[redacted]			Employee 18	UBIL	2006	107262				
[redacted]			Employee 20	UBIL	2006	103750	7,417	£18.52		1,855
[redacted]			Employee 28	UBIL	2006	101290				834
[redacted]			Employee 6	UBL	2006	93883	6,479	£18.52		1,296
[redacted]			Employee 19	UBIL	2006	93550	7,232	£18.52		1,447

ID Number	First Name	Surname	Employee Description	UBL/UBIL	Year	Converted £ to €	Exec Share Option scheme (ESOS)	ESOS option price	MPP	RSP
[redacted]			Employee 14	UBIL	2007	1,045,018	141,299	£5.61	21,092	
[redacted]			Employee 17	UBIL	2007	440,000	20,910	£20.99		3,485
[redacted]			Employee 27	UBIL	2007	300,800	9,523	£20.99		1,524
[redacted]			Employee 29	UBIL	2007	231,000				
[redacted]			Employee 16	UBL	2007	223,579	11,613	£20.99		2,323
[redacted]			Employee 15	UBIL	2007	214,518	16,615	£20.99		3,323
[redacted]			Employee 26	UBIL	2007	165,750	10,455	£20.99		1,743
[redacted]			Employee 28	UBIL	2007	164,980				827
[redacted]			Employee 13	UBIL	2007	156,000	7,457	£20.99		1,865
[redacted]			Employee 6	UBL	2007	153,434	9,335	£20.99		1,494
[redacted]			Employee 14	UBIL	2008	1,105,002	290,249	£3.55	161,250	
[redacted]			Employee 17	UBIL	2008	580,500	152,079	£3.55		25,347
[redacted]			Employee 27	UBIL	2008	271,700	73,264	£3.55		11,723
[redacted]			Employee 29	UBIL	2008	270,054				7,849
[redacted]			Employee 33	UBIL	2008	262,500	94,377	£3.55		18,876
[redacted]			Employee 16	UBL	2008	183,659	73,949	£3.55		14,790
[redacted]			Employee 26	UBIL	2008	182,750	76,040	£3.55		12,674
[redacted]			Employee 13	UBIL	2008	161,000	53,932	£3.55		13,483
[redacted]			Employee 21	UBIL	2008	148,400	64,716	£3.55		10,355
[redacted]			Employee 20	UBIL	2008	136,500	47,566	£3.55		11,892

Notes - shares

The number of shares highlighted should represent the number at the time of grant, i.e. the award made in that year

There were are number of corporate actions from 2007 onwards including a share split, rights issue, cap issue and share consolidation that impacted any awards that were outstanding at the relevant record dates

And in terms of any value being delivered to the participant for MPP and RSP, this would depend on whether any performance conditions had been achieved, whether the employee left and if so when/under what circumstances and the share price on the vesting / exercise date.

We have provided awards granted in each of these years rather than any resulting vesting amounts.

Notes - Bonuses

Sterling amounts have been converted based on an average exchange rate for the year in question
IR £ amounts converted to Euro