HSBC Bank plc

Capital and Risk Management Pillar 3 Disclosures at 31 December 2014

HSBC

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Presentation of information

This document comprises the Capital and Risk Management Pillar 3 Disclosures as at 31 December 2014 ('Pillar 3 Disclosures 2014') for HSBC Bank plc ('the bank') and its subsidiary undertakings (together 'the group'). Its principal purpose is to meet regulatory disclosure requirements under European legislation (chiefly CRD IV) and PRA rules/UK legislation.

References to either 'HSBC' or 'the Group' within this document mean HSBC Holdings plc together with its subsidiaries.

Cautionary statement regarding forward-looking statements

These Pillar 3 Disclosures 2014 contain certain forward-looking statements with respect to the financial condition, results of operations and business of the group.

Statements that are not historical facts, including statements about beliefs and expectations, are forward-looking statements. Words such as 'expects', 'anticipates', 'intends', 'plans', 'believes', 'seeks', 'estimates', 'potential' and 'reasonably possible', variations of these words and similar expressions are intended to identify forward-looking statements. These statements are based on current plans, estimates and projections, and therefore undue reliance should not be placed on them. Forward-looking statements speak only as of the date they are made. The bank makes no commitment to revise or update any forward-looking statements to reflect events or circumstances occurring or existing after the date of any forward-looking statements.

Written and/or oral forward-looking statements may also be made in the periodic reports to the US Securities and Exchange Commission, summary financial statements to shareholders, proxy statements, offering circulars and prospectuses, press releases and other written materials, and in oral statements made to third parties (including financial analysts) by Directors, officers or employees of HSBC or the group.

Forward-looking statements involve inherent risks and uncertainties. Readers are cautioned that a number of factors could cause actual results to differ, in some instances materially, from those anticipated or implied in any forward-looking statement. These factors include changes in general economic conditions in the markets in which we operate, changes in government policy and regulation and factors specific to the group.

Verification

The Pillar 3 Disclosures 2014 have been verified internally but have not been audited by the group's external auditor.

Frequency

The bank publishes its Pillar 3 disclosures annually in accordance with Article 433 of CRD IV Capital Requirements Regulation ('CRR').

Media and location

The HSBC Holdings plc Pillar 3 Disclosures 2014 and other information on the Group are available on HSBC's investor relations website: www.hsbc.com/investor-relations.

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Introduction

The bank is a wholly owned subsidiary of HSBC Holdings plc. HSBC is one of the largest banking and financial services organisations in the world, with a market capitalisation of US$ 182 billion at 31 December 2014.

The group provides a comprehensive range of banking and related financial services and divides its activities into four business segments: Retail Banking, Commercial Banking, Global Banking and Markets, and Global Private Banking.

Further details of the group's principal activities can be found on page 2 of the HSBC Bank plc Annual Report and Accounts 2014 ('HSBC Bank 2014 Accounts').

Regulatory framework for disclosures

HSBC is supervised on a consolidated basis in the UK by the Prudential Regulatory Authority ('PRA').

As the PRA supervises HSBC on a consolidated basis, it receives information on the capital adequacy of, and sets capital requirements for, the Group as a whole. Individual banking subsidiaries are directly regulated by their local banking supervisors, including the PRA itself in certain circumstances (for example, the bank), who set and monitor local capital adequacy requirements.

In most jurisdictions, non-banking financial institutions are also subject to the supervision and capital requirements of local regulatory authorities.

At consolidated Group and bank level, capital was calculated for prudential regulatory reporting purposes throughout 2014 using the Basel III framework of the Basel Committee on Banking Supervision ('Basel Committee') as implemented by the European Union ('EU') in the amended Capital Requirements Directive, known as CRD IV, and in the PRA's Rulebook for the UK banking industry.

The PRA's final rules deployed available national discretion in order to accelerate significantly the transition timetable to full 'end point' CRD IV compliance. Notwithstanding this, and other major developments in regulation during 2014, important elements of the capital adequacy framework in the UK have yet to be clarified, so that uncertainties remain as to the amount of capital that banks will be required to hold. These include the quantification and interaction of capital buffers, Total Loss Absorbing Capital ('TLAC') and the impact of structural reform. In addition, various technical standards and guidelines remain to be issued by the European Banking Authority ('EBA'), requiring adoption by the European Commission to come legally into force.

Regulatory developments

Capital buffers

CRD IV establishes a number of capital buffers, to be met by CET1 capital, broadly aligned with the Basel III framework. CRD IV contemplates that these will be phased in from 1 January 2016, subject to national

discretion. Restrictions on distributions apply where a bank fails to meet some of these buffers.

Countercyclical capital buffer (CCB)

The CCB is expected to be set in the rage of 0-2.5% of relevant credit exposures, although it is uncapped. In June 2014, the Financial Policy Committee ('FPC') set the CCB rate for UK exposures at 0%. At its September 2014 meeting, the FPC left the CCB rate for UK exposures unchanged at 0% and recognised the 1% CCB rates introduced by Norway and Sweden to become effective from 3 October 2015.

Buffer for other systemically important institutions ('O-SIIs')

The PRA will be responsible for identifying O-SIIs from 1 January 2016. It intends to consult on and set out its policy for identifying O-SIIs in 2015.

Other regulatory developments

A summary of recent and forthcoming developments in the regulation of the bank, the group and HSBC can be found:

- on pages 26 - 27 of the HSBC Bank plc 2014 Accounts;
- on pages 252 – 256 of the HSBC Holdings plc Annual Report and Accounts 2014 ('HSBC Holdings plc 2014 Accounts');
- on pages 6 - 10 of the HSBC Holdings plc Pillar 3 Disclosures 2014.

Pillar 3 disclosures 2014

The Basel framework is structured around three 'pillars': the Pillar 1 minimum capital requirements and Pillar 2 supervisory review process are complemented by Pillar 3 market discipline.

Pillar 3 complements the minimum capital requirements and the supervisory review process. Its aim is to encourage market discipline by developing a set of disclosure requirements which allow market participants to assess certain specified information on: the scope of application of Basel III, capital, particular risk exposures and risk assessment processes, and hence the capital adequacy of the institution. Disclosures consist of both quantitative and qualitative information and are provided at the group level.

Banks are required to disclose all their material risks as part of the Pillar 3 framework. All material and non-proprietary information required by Pillar 3 is included in the HSBC Holdings plc Pillar 3 Disclosures 2014. HSBC Bank plc, as a significant subsidiary of HSBC Holdings plc, is required to publish certain limited Pillar 3 disclosures separately on a consolidated basis.

CRD IV permits certain Pillar 3 requirements to be satisfied by inclusion within a firm's financial statements. Where this is the case, this document provides page references to the relevant sections in the HSBC Bank plc 2014 Accounts and HSBC Holdings plc 2014 Accounts.

Comparison with the HSBC Bank plc 2014 Accounts

The Pillar 3 Disclosures 2014 have been prepared in accordance with regulatory capital adequacy concepts and rules, rather than in accordance with International Financial Reporting Standards ('IFRS'). Therefore, some information in the Pillar 3 Disclosures 2014 is not directly comparable with the financial information in the HSBC Bank plc 2014 Accounts. This is most pronounced for the credit risk disclosures, where credit exposure is defined as the amount estimated to be at risk under specified Basel III parameters. This differs from similar information in the HSBC Bank plc 2014 Accounts, which is mainly reported at the balance sheet date and therefore does not reflect the likelihood of future drawings of committed credit lines.

Capital and Risk

Capital management

A description of the bank's approach to capital management can be found on pages 84 - 86 of the HSBC Bank plc 2014 Accounts.

Pillar 1

Pillar 1 covers the capital resources requirements for credit risk, market risk and operational risk. Credit risk includes counterparty credit risk and securitisation requirements. These requirements are expressed in terms of RWA.

The table below sets out the Pillar 1 risk categories, their approaches available for calculating capital requirements and the approaches adopted by the group.

Risk category	Scope of permissible approaches	Approach adopted by HSBC
Credit risk	The Basel framework applies three approaches of increasing sophistication to the calculation of Pillar 1 credit risk capital requirements. The most basic level, the standardised approach, requires banks to use external credit ratings to determine the risk weightings applied to rated counterparties. Other counterparties are grouped into broad categories and standardised risk weightings are applied to these categories. The next level, the IRB foundation approach, allows banks to calculate their credit risk capital requirements on the basis of their internal assessment of counterparty's probability of default ('PD'), but subjects their quantified estimates of exposure at default ('EAD') and loss given default ('LGD') to standard supervisory parameters. Finally, the internal ratings-based ('IRB') advanced approach allows banks to use their own internal assessment in both determining PD and quantifying EAD and LGD.	For consolidated group reporting, we have adopted the IRB advanced approach for the majority of our business. Certain portfolios remain on the standardised or foundation approaches: • pending the issuance of local regulations or model approval: • following supervisory prescription of a non-advanced approach; or • under exemptions from IRB treatment.
Counterparty credit risk	Three methods to calculating counterparty credit risk and determining exposure values are defined by Basel: standardised, mark-to-market and internal model method ('IMM'). These exposure values are used to determine capital requirements under one of the credit risk approaches: standardised, IRB foundation and IRB advanced.	We use the mark-to-market and IMM approaches for counterparty credit risk. Details of the IMM permission we have received from the PRA can be found in the Financial Services Register on the PRA website. Our aim is to increase the proportion of positions on IMM over time.
Equity	Equity exposures can be assessed under standardised or IRB approaches.	For group reporting purposes all equity exposures are treated under the standardised approach.
Securitisation	Basel specifies two methods for calculating credit risk requirements for securitisation positions in the non-trading book: the standardised approach and the IRB approach, which incorporates the Ratings Based Method ('RBM'), the Internal Assessment Approach ('IAA') and the Supervisory Formula Method ('SFM').	For the majority of the securitisation non-trading book positions we use the IRB approach, and within this principally the RBM, with lesser amounts on IAA and SFM. Securitisation positions in the trading book are treated within Market Risk, using PRA standardised rules.
Market risk	Market risk capital requirements can be determined under either the standard rules or the internal models approach. The latter involves the use of internal value at risk ('VAR') models to measure market risks and determine the appropriate capital requirement. The incremental risk charge ('IRC') also applies.	The market risk capital requirement is measured using internal market risk models, where approved by the PRA, or the PRA standard rules. Our internal market risk models comprise VAR, stressed VAR and IRC. Non-proprietary details of the scope of our IMA permission are available in the Financial Services Register on the PRA website. We are in compliance with the requirements set out in Articles 104 and 105 of the Capital Requirements Regulation.
Operational risk	Basel allows for firms to calculate their operational risk capital requirement under the basic indicator approach, the standardised approach or the advanced measurement approach.	We have historically adopted and currently use the standardised approach in determining our operational risk capital requirement. We are in the process of developing and implementing an AMA-compliant model, which we will use for economic capital calculation. Our medium-term aim is to move to an AMA approach for our operational risk capital requirement calculation.

Consolidation basis

The basis of consolidation for financial accounting purposes is described in Note 1 - Basis of preparation of the notes on the financial statements on page 113 of the HSBC Bank plc 2014 Accounts. This differs from that used for regulatory purposes. Investments in banking associates are equity accounted in the financial accounting consolidation, whereas their exposures are proportionally consolidated for regulatory purposes.

Subsidiaries and associates engaged in insurance and non-financial activities are excluded from the regulatory consolidation and are deducted from regulatory capital subject to thresholds. The regulatory consolidation does not include Special Purpose Entities ('SPEs') where significant risk has been transferred to third parties. Exposures to these SPEs are risk-weighted as securitisation positions.

Table 1: Reconciliation of balance sheets – financial accounting to regulatory scope of consolidation

	Ref	At 31 December 2014			
		Accounting balance sheet £m	Deconsolidation of insurance/ other entities £m	Consolidation of banking associates £m	Regulatory balance sheet £m
Assets					
Cash and balances at central banks		42,853	-	86	42,939
Items in the course of collection from other banks		973	-	-	973
Trading assets		130,127	1,213	-	131,340
Financial assets designated at fair value		6,899	-	-	6,899
Derivatives		187,736	(69)	-	187,667
Loans and advances to banks		25,262	(18)	14	25,258
Loans and advances to customers, of which:		257,252	(6,862)	-	250,390
- impairment allowances on IRB portfolios	*h*	2,179	-	-	2,179
- impairment allowances on standardised portfolios	*j*	658	-	-	658
Reverse repurchase agreements (non-trading)		41,945	-	-	41,945
Financial investments		76,194	(20,657)	-	55,537
Prepayments, accrued income and other assets, of which:		20,396	(1,446)	37	18,987
- goodwill and intangible assets in disposal groups held for sale	*g*	77	-	-	77
- retirement benefit assets	*f*	3,060	-	-	3,060
Current tax assets		190	-	-	190
Interests in associates and joint ventures		69	(6)	(22)	41
Goodwill and intangible assets	*g*	7,217	(474)	-	6,743
Deferred tax assets		176	-	-	176
Total assets		**797,289**	**(28,319)**	**115**	**769,085**
Liabilities and equity					
Liabilities					
Deposits by banks		27,590	-	87	27,677
Customer accounts		346,507	(91)	-	346,416
Reverse repurchase agreements (non-trading)		23,353	-	-	23,353
Items in the course of transmission to other banks		667	-	-	667
Trading liabilities		82,600	(30)	-	82,570
Financial liabilities designated at fair value, of which:		22,552	-	-	22,552
- other instruments disallowed in tier 1 capital	*i*	317	-	-	317
- term subordinated debt included in tier 2 capital	*l*	2,503	-	-	2,503
Derivatives		188,278	17	-	188,295
Debt securities in issue		27,921	(6,262)	-	21,659
Accruals, deferred income and other liabilities, of which:		12,417	(3,589)	23	8,851
- retirement benefit liabilities	*f*	333	(1)	7	339
- contingent liabilities and contractual commitments, of which:					
- credit-related provisions on IRB portfolios	*h*	14	-	-	14
- credit-related provisions on standardised portfolios	*j*	2	-	-	2
Current tax liabilities		255	(50)	1	206
Liabilities under insurance contracts issued		17,522	(17,522)	-	-
Provisions		1,707	(16)	4	1,695
Deferred tax liabilities		364	-	-	364
Subordinated liabilities, of which:		8,858	-	-	8,858
- other instruments disallowed in tier 1 capital	*i*	1,402	-	-	1,402
- perpetual subordinated debt included in tier 2 capital	*k*	2,841	-	-	2,841
- term subordinated debt included in tier 2 capital	*l*	3,284	-	-	3,284
Total liabilities		**760,591**	**(27,543)**	**115**	**733,163**
Equity					
Called up share capital		797	-	-	797
Share premium account, of which:		20,733	-	-	20,733
- preference share premium disallowed in tier 1 capital	*b*	431	-	-	431
Other equity instruments		2,196	-	-	2,196
Other reserves		772	-	-	772
Retained earnings	*a*	11,580	(776)	-	10,804
Total equity attributable to the shareholders of the parent company	***a***	**36,078**	**(776)**	**-**	**35,302**
Non-controlling interests, of which:	*c*	620	-	-	620
- preference shares issued by subsidiaries disallowed in tier 1 capital	*d*	150	-	-	150
- surplus non-controlling interest disallowed in CET 1	*e*	117	-	-	117
Total equity		**36,698**	**(776)**	**-**	**35,922**
Total equity and liabilities		**797,289**	**(28,319)**	**115**	**769,085**

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1. The references (a) – (l) identify balance sheet components which are used in the calculation of regulatory capital on page 6.

Regulatory capital

Table 2 below sets out the composition of the group's regulatory capital and risk-weighted assets at 31 December 2014.

Table 2: Composition of regulatory capital – CRD IV transitional basis

	Ref	CRD IV year 1 transition At 31 December 2014 £m	Basel 2.5 At 31 December 2013 £m
Tier 1 capital			
Shareholders' equity[1]		34,562	31,993
Shareholders' equity per balance sheet	*a*	36,079	32,370
Foreseeable interim dividend		(315)	-
Preference share premium	*b*	(431)	(431)
Deconsolidation of special purpose entities[2]	*a*	(86)	53
Deconsolidation of insurance entities	*a*	(685)	1
Non-controlling interests		353	399
Non-controlling interests per balance sheet	*c*	620	549
Preference share non-controlling interests	*d*	(150)	(150)
Surplus non-controlling interest excluded from CET 1	*e*	(117)	-
Regulatory adjustments to the accounting basis		(5,444)	(1,389)
Unrealised gains/(losses) on available-for-sale debt and equities[3]		(837)	(656)
Own credit spread		245	218
Debit valuation adjustment		(88)	-
Defined benefit pension fund adjustment[4]	*f*	(2,400)	(946)
Cash flow hedging reserve		(163)	13
Reserves arising from revaluation of property		-	(16)
Other equity instruments		(2,195)	-
Other regulatory adjustments		(6)	(2)
Deductions		(8,380)	(8,565)
Goodwill and intangible assets	*g*	(6,822)	(7,218)
Deferred tax assets that rely on future profitability (excluding temporary differences)		(21)	-
Additional valuation adjustment (referred to as PVA)		(588)	-
50% of securitization positions		-	(902)
50% of excess of expected losses over impairment allowances	*h*	-	(477)
50% of tax credit adjustment for expected losses		-	32
Excess of expected losses over impairment allowances	*h*	(949)	-
Common equity tier 1		**21,091**	**22,438**
Additional tier 1 capital			
Other tier 1 capital before deductions		4,047	2,353
Preference shares and related premium	*b*	464	581
Other instruments	*i*	3,583	1,772
Deductions		-	(683)
Unconsolidated investments[5]		-	(715)
50% of tax credit adjustment for expected losses		-	32
Tier 1 capital		**25,138**	**24,108**
Tier 2 capital			
Total qualifying tier 2 capital before deductions		8,628	11,582
Reserves arising from revaluation of property and unrealised gains in available-for-sale equities		-	221
Collective impairment allowances[6]	*j*	-	139
Perpetual subordinated debt	*k*	2,844	2,683
Term subordinated debt	*l*	5,784	8,539
Total deductions other than from tier 1 capital		(210)	(2,147)
Unconsolidated investments[5]		(210)	(715)
50% of securitisation positions		-	(902)
50% of excess of expected losses over impairment allowances		-	(477)
Other deductions		-	(53)
Total regulatory capital		**33,556**	**33,543**

	Ref	CRD IV year 1 transition At 31 December 2014 £m	Basel 2.5 At 31 December 2013 £m
Risk-weighted assets		243,652	185,879
Credit risk		168,600	129,459
Counterparty credit risk		30,364	16,450
Market risk		22,437	17,931
Operational risk		22,251	22,039
Capital ratios			
Common equity tier 1 ratio		8.7%	12.1%
Tier 1 ratio		10.3%	13.0%
Total capital ratio		13.8%	18.0%

1. Includes externally verified profits for the year to 31 December 2014 and the interim dividend of £315 million declared by the Board of Directors after 31 December 2014. 2013 figures exclude the dividend of £630m declared in February 2014.

2. Mainly comprises unrealised gains on available-for-sale securities owned by deconsolidated special purpose entities.

3. Under CRD IV transitional rules, unrealised gains on available-for-sale securities must be excluded from capital resources.

4. CRD IV rules require banks to exclude from capital resources any surplus in a defined benefit pension scheme.

5. Mainly comprises investment in insurance entities. Under CRD IV rules, the value of unconsolidated investments in insurance entities in 2014 falls below the 10% threshold for deductions.

6. Under previous PRA rules, collective impairment allowances on loan portfolios under the standardised approach were allowable in tier 2 capital.

Table 3: Reconciliation of regulatory capital from transitional basis to an estimated CRD IV end point basis

	At 31 December 2014
CET1 on year 1 transitional basis	**21,091**
Unrealised gains in available-for-sale reserves	837
CET1 on end point basis	**21,928**
AT1 on year 1 transitional basis	4,047
Grandfathered instruments	(1,852)
Preference share premium	(345)
Other instruments	(1,507)
AT1 on end point basis	2,195
T2 on year 1 transitional basis	8,418
Grandfathered instruments	(2,326)
Term subordinated debt	(2,326)
T2 on end point basis	6,092
Total capital on end point basis	**30,215**

Credit risk

Overview

Credit risk is the risk of financial loss if a customer or counterparty fails to meet a payment obligation under a contract. It arises principally from direct lending, trade finance and leasing business, but also from off-balance sheet products such as guarantees and credit derivatives, and from the group's holdings of debt and other securities.

For credit risk, with the PRA's approval, the group has adopted the IRB advanced approach for the majority of its business, with the remainder on either IRB foundation or standardised approaches. A rollout plan is in place to extend coverage of the advanced approach over the next few years, leaving a residue of exposures on the standardised approach.

The environment for approval and operation of internal risk-based ('IRB') analytical models remains challenging. The PRA has introduced a number of measures to constrain modelling approaches used to calculate RWAs; these generally have driven higher capital requirements. These measures included a 45% floor for LGD on sovereign and bank IRB exposures and a requirement to adopt supervisory slotting for certain commercial real estate exposures. Given that the majority of European Economic Area ('EEA') sovereign exposures are treated under the standardised approach, the sovereign LGD floor in practice applies to non-EEA sovereign exposures. The PRA consulted during 2014 on a proposal (CP12/14) to remove the Advanced IRB approach permissions for a number of low default wholesale portfolios, such as Banks, Sovereigns, Public Sector Entities and Financial Sector Entities which would require firms to adopt a Foundation IRB Approach. Final rules are still awaited.

A more fundamental review of the IRB framework is expected during 2015 with the European Banking Authority mandated under the CRR to issue a number of technical standards to fix identified deficiencies in the current IRB framework. Work is also being taken forward at the International level to ensure greater consistency of calculation and reporting of IRB models.

As part of the introduction of the Capital Requirements Regulation firms are required to attest on an annual basis that their risk rating system complies with the requirements of the CRR and the PRA's Supervisory Statement (SS11/13) issued in December 2013. Where a firm is unable to demonstrate full compliance they may be subject to the imposition of additional regulatory floors or required to revert to less advanced approaches for the affected portfolios. As a result of these requirements, three small portfolios reverted from an AIRB to a standardised approach in January 2014 and a further two portfolios have reverted from AIRB to FIRB in January 2015.

The tables below set out details of the group's credit risk exposures by exposure class and approach. Further explanation of the group's approach to managing credit risk (including details of the group's past due and impaired exposure, and its approach to credit risk impairment) can be found:

- on pages 37 - 57 of the HSBC Bank plc 2014 Accounts;
- on pages 129 - 140 of the HSBC Holdings plc 2014 Accounts;
- on pages 34 - 71 of the HSBC Holdings plc Pillar 3 Disclosures 2014.

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Table 4: Credit risk exposure - by exposure class

	Exposure value £m	Average exposure value £m	RWA £m	Capital required[1] £m
IRB advanced approach	333,742	366,480	100,014	8,000
Retail:				
- secured by mortgages on immovable property SME	1,550	1,599	376	30
- secured by mortgages on immovable property non-SME	92,450	93,366	5,130	410
- qualifying revolving retail	22,373	22,204	4,453	356
- other SME	8,438	9,089	3,788	303
- other non-SME	14,881	14,672	3,550	284
Total retail	139,692	140,930	17,297	1,383
Central governments and central banks	16,464	17,289	3,336	267
Institutions	18,537	20,706	7,451	596
Corporates	159,049	187,555	71,930	5,754
IRB foundation approach	12,268	11,087	8,208	656
Institutions	28	14	6	-
Corporates	12,240	11,073	8,202	656
IRB Securitisation positions	22,406	23,217	25,675	2,054
IRB Non-credit obligation assets	6,587	6,046	3,309	265
Standardised approach	126,809	136,352	31,394	2,512
Central governments or central banks	79,692	87,999	83	7
Public sector entities	25	19	5	-
International organisations	2,126	2,187	-	-
Institutions	10,305	10,235	2,800	224
Corporates	24,290	22,509	19,419	1,554
Retail	3,590	4,122	2,587	207
Secured by mortgages on immovable property	2,830	2,933	1,005	80
Exposures in default	696	761	876	70
Items associated with particularly high risk	673	672	1,009	81
Collective investment undertakings	133	98	133	11
Equity exposures	769	1,133	1,648	132
Other items[2]	1,680	3,684	1,829	146
At 31 December 2014	**501,811**	**543,182**	**168,600**	**13,487**
IRB advanced approach	270,815	277,686	82,805	6,624
Retail:				
- secured by mortgages on immovable property SME	-	-	-	-
- secured by mortgages on immovable property non-SME	93,608	93,372	5,639	451
- qualifying revolving retail	22,329	21,854	4,761	381
- other SME	10,402	9,526	5,122	410
- other non-SME	15,633	15,125	4,754	380
Total retail	141,972	139,877	20,276	1,622
Central governments and central banks	18,150	20,597	3,103	248
Institutions	12,045	20,412	4,855	388
Corporates	98,648	96,800	54,571	4,366
IRB foundation approach	10,104	9,876	5,937	475
Institutions	-	-	-	-
Corporates	10,104	9,876	5,937	475
IRB Securitisation positions	24,276	25,998	11,417	913
IRB Non-credit obligation assets	-	-	-	-
Standardised approach	155,224	156,320	29,300	2,344
Central governments or central banks	101,075	93,090	17	1
Public sector entities	-	-	-	-
International organisations	1,176	1,203	-	-
Institutions	10,416	9,829	2,132	170
Corporates	23,839	31,432	14,731	1,178
Retail	4,647	4,668	3,663	293
Secured by mortgages on immovable property	3,351	4,331	1,350	107
Exposures in default	433	427	530	42
Items associated with particularly high risk	303	211	454	36
Collective investment undertakings	80	76	80	6
Equity exposures	833	833	941	75
Other items[2]	9,071	10,220	5,402	432
At 31 December 2013	**460,419**	**469,880**	**129,459**	**10,356**

1. *In this, and all following tables where the term appears, capital required is calculated as 8% of RWA.*
2. *Includes items such as tangible fixed assets, prepayments, deferred taxation and immaterial exposure classes under the standardised approach.*

Capital and Risk Management Pillar 3 Disclosures at 31 December 2014

Table 5: Credit risk exposure - by region

	United Kingdom £m	Continental Europe £m	Other £m	Total £m
IRB advanced approach	282,522	46,287	4,932	333,742
Retail:				
- secured by mortgages on immovable property SME	26	1,524	-	1,550
- secured by mortgages on immovable property non-SME	90,610	1,840	-	92,450
- qualifying revolving retail	22,372	1	-	22,373
- other SME	5,690	2,748	-	8,438
- other non-SME	4,244	10,637	-	14,881
Total retail	122,942	16,749	-	139,692
Central governments and central banks	10,801	2,351	3,312	16,464
Institutions	13,475	3,442	1,620	18,537
Corporates	135,304	23,745	-	159,049
IRB foundation approach	110	12,158	-	12,268
Institutions	-	28	-	28
Corporates	110	12,130	-	12,240
IRB Securitisation positions	20,332	2,073	-	22,406
IRB Non-credit obligation assets	5,453	944	190	6,587
Standardised approach	83,915	35,637	7,257	126,809
Central governments or central banks	64,516	15,118	58	79,692
Public sector entities	-	25	-	25
International organisations	-	2,126	-	2,126
Institutions	3,739	6,549	17	10,305
Corporates	12,567	7,447	4,276	24,290
Retail	559	857	2,174	3,590
Secured by mortgages on immovable property	576	1,716	538	2,830
Exposures in default	17	517	162	696
Items associated with particularly high risk	507	156	10	673
Collective investment undertakings	-	133	-	133
Equity exposures	151	618	-	769
Other items[2]	1,283	375	22	1,680
At 31 December 2014	**392,332**	**97,099**	**12,380**	**501,811**
IRB advanced approach	217,667	47,921	5,227	270,815
Retail:				
- secured by mortgages on immovable property SME				
- secured by mortgages on immovable property non-SME	91,309	2,299	-	93,608
- qualifying revolving retail	22,318	11	-	22,329
- other SME	5,966	4,436	-	10,402
- other non-SME	4,823	10,810	-	15,633
Total retail	124,416	17,556	-	141,972
Central governments and central banks	11,951	2,420	3,779	18,150
Institutions	6,818	3,779	1,448	12,045
Corporates	74,482	24,166	-	98,648
IRB foundation approach	168	9,936	-	10,104
Institutions	-	-	-	-
Corporates	168	9,936	-	10,104
IRB Securitisation positions	22,351	1,925	-	24,276
IRB Non-credit obligation assets	-	-	-	-
Standardised approach	105,239	41,330	8,655	155,224
Central governments or central banks	80,205	20,870	-	101,075
Public sector entities	-	-	-	-
International organisations	-	1,176	-	1,176
Institutions	3,751	6,663	2	10,416
Corporates	12,499	6,992	4,348	23,839
Retail	768	1,206	2,673	4,647
Secured by mortgages on immovable property	679	1,983	689	3,351
Exposures in default	16	268	149	433
Items associated with particularly high risk	216	87	-	303
Collective investment undertakings	-	80	-	80
Equity exposures	227	182	424	833
Other items[2]	6,876	1,823	372	9,071
At 31 December 2013	**345,425**	**101,112**	**13,882**	**460,419**

Capital and Risk Management Pillar 3 Disclosures at 31 December 2014

Table 6: Credit risk exposure - by industry sector

	Personal £m	Manu-facturing £m	Inter-national trade and services £m	Property and other business activities £m	Government and public admin-istration £m	Other commercial £m	Financial £m	Non-customer assets £m	Total £m
IRB advanced approach	129,705	27,482	40,407	57,212	19,045	21,982	37,907	-	333,742
Retail:									
- secured by mortgages on immovable property SME	-	8	20	1,485	7	13	17	-	1,550
- secured by mortgages on immovable property non-SME	92,450	-	-	-	-	-	-	-	92,450
- qualifying revolving retail	22,373	-	-	-	-	-	-	-	22,373
- other SME	-	528	1,484	4,608	437	1,230	151	-	8,438
- other non-SME	14,881	-	-	-	-	-	-	-	14,881
Total retail	129,704	536	1,504	6,093	444	1,243	168	-	139,692
Central governments and central banks	-	-	-	-	12,572	-	3,892	-	16,464
Institutions	-	-	-	-	-	-	18,537	-	18,537
Corporates	1	26,946	38,903	51,119	6,030	20,740	15,310	-	159,049
IRB foundation approach	145	5,017	2,952	737	252	1,433	1,732	-	12,268
Institutions	-	-	-	-	-	-	28	-	28
Corporates	145	5,017	2,952	737	252	1,433	1,704	-	12,240
IRB Securitisation positions	-	-	-	-	-	-	22,406	-	22,406
IRB Non-credit obligation assets	-	-	-	-	-	-	-	6,587	6,587
Standardised approach	7,029	6,005	3,657	2,724	36,229	2,604	67,760	801	126,809
Central governments or central banks	-	-	-	-	33,501	-	46,061	130	79,692
Public sector entities	-	-	-	-	25	-	-	-	25
International organisations	-	-	-	-	2,126	-	-	-	2,126
Institutions	-	-	-	-	-	-	10,305	-	10,305
Corporates	1,117	5,721	3,464	2,114	523	2,313	9,038	-	24,290
Retail	2,988	135	80	306	24	38	19	-	3,590
Secured by mortgages on immovable property	2,690	79	40	3	2	16	-	-	2,830
Exposures in default	234	70	72	83	28	205	4	-	696
Items associated with particularly high risk	-	-	1	134	-	32	506	-	673
Collective investment undertakings	-	-	-	--	-	-	133	-	133
Equity exposures	-	-	-	84	-	-	685	-	769
Other items[2]	-	-	-	-	-	-	1,009	671	1,680
At 31 December 2014	**136,879**	**38,504**	**47,016**	**60,673**	**55,526**	**26,019**	**129,805**	**7,388**	**501,811**

Capital and Risk Management Pillar 3 Disclosures at 31 December 2014

	Personal £m	Manu-facturing £m	Inter-national trade and services £m	Property and other business activities £m	Government and public admin-istration £m	Other commercial £m	Financial £m	Non-customer assets £m	Total £m
IRB advanced approach	132,214	17,914	19,048	41,479	17,102	15,800	27,258	-	270,815
Retail:									
- secured by mortgages on immovable property SME	-	-	-	-	-	-	-	-	-
- secured by mortgages on immovable property non-SME	93,608	-	-	-	-	-	-	-	93,608
- qualifying revolving retail	22,329	-	-	-	-	-	-	-	22,329
- other SME	-	508	879	8,171	163	430	251	-	10,402
- other non-SME	15,633	-	-	-	-	-	-	-	15,633
Total retail	131,570	508	879	8,171	163	430	251	-	141,972
Central governments and central banks	-	-	-	-	12,892	-	5,258	-	18,150
Institutions	-	-	-	-	90	-	11,955	-	12,045
Corporates	644	17,406	18,169	33,308	3,957	15,370	9,794	-	98,648
IRB foundation approach	19	4,445	2,696	444	169	809	1,522	-	10,104
Institutions	-	-	-	-	-	-	-	-	-
Corporates	19	4,445	2,696	444	169	809	1,522	-	10,104
IRB Securitisation positions	-	-	-	-	-	-	24,181	95	24,276
IRB Non-credit obligation assets	-	-	-	-	-	-	-	-	-
Standardised approach	7,379	5,488	3,401	1,883	32,445	3,436	96,823	4,369	155,224
Central governments or central banks	-	-	-	-	30,556	-	70,519	-	101,075
Public sector entities	-	-	-	-	-	-	-	-	-
International organisations	-	-	-	-	1,176	-	-	-	1,176
Institutions	-	-	-	-	-	-	10,412	4	10,416
Corporates	159	5,155	3,199	1,380	652	3,256	10,038	-	23,839
Retail	3,783	251	144	329	48	67	25	-	4,647
Secured by mortgages on immovable property	3,213	45	32	37	3	21	-	-	3,351
Exposures in default	224	37	26	45	8	91	2	-	433
Items associated with particularly high risk	-	-	-	87	-	-	216	-	303
Collective investment undertakings	-	-	-	-	-	-	80	-	80
Equity exposures	-	-	-	6	-	-	827	-	833
Other items[2]	-	-	-	-	2	-	4,703	4,366	9,071
At 31 December 2013	**139,612**	**27,847**	**25,145**	**43,806**	**49,716**	**20,045**	**149,784**	**4,464**	**460,419**

Capital and Risk Management Pillar 3 Disclosures at 31 December 2014

Table 7: Credit risk exposure - by residual maturity

	Less than 1 year £m	Between 1 and 5 years £m	More than 5 years £m	Undated £m	Total £m
IRB advanced approach	127,803	84,153	121,786	-	333,742
Retail:					
- secured by mortgages on immovable property SME	37	107	1,406	-	1,550
- secured by mortgages on immovable property non-SME	1,574	1,481	89,395	-	92,450
- qualifying revolving retail	22,363	9	1	-	22,373
- other SME	1,779	4,384	2,275	-	8,438
- other non-SME	860	4,710	9,311	-	14,881
Total retail	26,613	10,691	102,388	-	139,692
Central governments and central banks	6,359	6,831	3,274	-	16,464
Institutions	12,255	5,379	903	-	18,537
Corporates	82,576	61,252	15,221	-	159,049
IRB foundation approach	5,008	6,393	867	-	12,268
Institutions	28	-	-	-	28
Corporates	4,980	6,393	867	-	12,240
IRB Securitisation positions	5,862	2,868	13,676	-	22,406
IRB Non-credit obligation assets	-	-	-	6,587	6,587
Standardised approach	78,021	30,343	16,837	1,608	126,809
Central governments or central banks	46,245	21,817	11,630	-	79,692
Public sector entities	-	2	23	-	25
International organisations	183	1,109	834	-	2,126
Institutions	10,296	9	-	-	10,305
Corporates	18,143	4,899	1,248	-	24,290
Retail	1,712	1,599	279	-	3,590
Secured by mortgages on immovable property	138	467	2,225	-	2,830
Exposures in default	316	201	179	-	696
Items associated with particularly high risk	14	240	419	-	673
Collective investment undertakings	-	-	-	133	133
Equity exposures	-	-	-	769	769
Other items[2]	973	-	-	707	1,680
At 31 December 2014	**216,694**	**123,757**	**153,166**	**8,195**	**501,811**
IRB advanced approach	73,676	79,502	117,637	-	270,815
Retail:					
- secured by mortgages on immovable property SME	-	-	-	-	-
- secured by mortgages on immovable property non-SME	1,426	1,859	90,323	-	93,608
- qualifying revolving retail	22,308	10	11	-	22,329
- other SME	1,987	5,159	3,256	-	10,402
- other non-SME	1,082	5,349	9,202	-	15,633
Total retail	26,803	12,377	102,792	-	141,972
Central governments and central banks	9,137	7,116	1,897	-	18,150
Institutions	6,221	5,437	387	-	12,045
Corporates	31,515	54,572	12,561	-	98,648
IRB foundation approach	4,207	5,184	713	-	10,104
Institutions	-	-	-	-	-
Corporates	4,207	5,184	713	-	10,104
IRB Securitisation positions	-	-	22,351	1,925	24,276
IRB Non-credit obligation assets	-	-	-	-	-
Standardised approach	94,758	36,491	13,734	10,241	155,224
Central governments or central banks	67,912	24,347	8,816	-	101,075
Public sector entities	-	-	-	-	-
International organisations	-	1,176	-	-	1,176
Institutions	8,418	1,980	18	-	10,416
Corporates	16,529	4,894	2,416	-	23,839
Retail	1,425	3,000	222	-	4,647
Secured by mortgages on immovable property	225	980	2,146	-	3,351
Exposures in default	248	70	115	-	433
Items associated with particularly high risk	-	-	-	303	303
Collective investment undertakings	-	-	-	80	80
Equity exposures	-	-	-	833	833
Other items[2]	1	44	1	9,025	9,071
At 31 December 2013	**172,641**	**121,177**	**154,435**	**12,166**	**460,419**

Specialised lending

The table below sets out the specialised lending exposures by credit rating category. Specialised lending relates to financing of individual projects where repayment is dependent on the performance of the underlying assets or collateral. The group aligns exposures to specialised lending categories by taking into account the financial strength of the project, political and legal environment, asset characteristics, strength of the sponsor and developer.

Table 8: Specialised lending – by credit rating category

	Exposure	
	At 31 December 2014	At 31 December 2013
	£m	£m
Category 1 - strong	6,447	4,663
Category 2 - good	4,255	4,721
Category 3 - satisfactory	1,686	2,554
Category 4 - weak	708	664
Category 5 - default	978	1,215
	14,074	13,817

Table 9: IRB expected loss and impairment – by exposure class

	Expected loss at 31 December	Impairment	
		Allowances at 31 December	Charge for the year[1]
	£m	£m	£m
IRB exposure classes			
Central governments and central banks	9	1	1
Institutions	80	20	-
Corporates	1,893	1,534	406
Retail:	1,095	638	14
- secured by mortgages on immovable property SME	20	10	-
- secured by mortgages on immovable property non-SME	253	182	(51)
- qualifying revolving retail	223	103	(5)
- other SME	446	228	-
- other non-SME	153	115	70
2014	**3,077**	**2,193**	**421**
IRB exposure classes			
Central governments and central banks	10	1	-
Institutions	93	21	-
Corporates	2,239	1,655	774
Retail:	1,254	1,050	84
- secured by mortgages on immovable property SME	-	-	-
- secured by mortgages on immovable property non-SME	213	202	(21)
- qualifying revolving retail	265	198	68
- other SME	533	434	2
- other non-SME	243	216	35
2013	**3,595**	**2,727**	**858**

1. *Details of amounts written off and recoveries taken straight to the income statement can be found in the tables on page 51 of the HSBC Bank plc 2014 Accounts.*

Table 10: IRB expected loss and impairment – by region

		Impairment	
	Expected loss at 31 December £m	Allowances at 31 December £m	Charge for the year £m
United Kingdom	2,347	1,606	326
Continental Europe	710	582	95
Other	20	5	-
2014	**3,077**	**2,193**	**421**
United Kingdom	2,836	2,109	771
Continental Europe	735	613	87
Other	23	5	-
2013	**3,595**	**2,727**	**858**

Credit risk mitigation ('CRM')

Mitigation of credit risk is a key aspect of effective risk management. Specific, detailed policies cover the acceptability, structuring and terms of various types of business with regard to the availability of credit risk mitigation, for example in the form of collateral security. These policies, together with the setting of suitable valuation parameters, are subject to regular review to ensure that they are supported by empirical evidence and continue to fulfil their intended purpose.

Collateral

The most common method of mitigating credit risk is to take collateral. In our retail residential and CRE businesses, a mortgage over the property is usually taken to help secure claims. Physical collateral is also taken in various forms of specialised lending and leasing transactions where income from the physical assets that are financed is also the principal source of facility repayment. In the commercial and industrial sectors, charges are created over business assets such as premises, stock and debtors. Loans to private banking clients may be made against a pledge of eligible marketable securities, cash or real estate. Facilities to SMEs are commonly granted against guarantees given by their owners and/or directors. Guarantees may be taken from third parties where the group extends facilities without the benefit of any alternative form of security, e.g. where it issues a bid or performance bond in favour of a non-customer at the request of another bank.

Further information regarding collateral held over residential and CRE property is provided on page 146 of the HSBC Holdings plc 2014 Accounts.

Financial collateral

In the institutional sector, trading facilities are supported by charges over financial instruments such as cash, debt securities and equities. Financial collateral in the form of marketable securities is used in much of the group's over-the-counter ('OTC') derivatives activities and in securities financing transactions ('SFT's) such as repos, reverse repos, securities lending and borrowing. Netting is used extensively and is a prominent feature of market standard documentation.

In the banking book we provide customers with working capital management products. Some of these products have loans and advances to customers and customer accounts where we have rights of offset and comply with the regulatory requirements for on balance sheet netting. Under on-balance sheet netting, the customer accounts are treated as cash collateral and the effects of this collateral are incorporated in our LGD estimates. For risk management purposes, the net exposures are subject to limits which are monitored and the relevant customer agreements are subject to review and update, as necessary, to ensure the legal right of offset remains appropriate.

Other forms of CRM

Our Global Banking and Markets business utilises credit risk mitigation to manage the credit risk of its portfolios, with the goal of reducing concentrations in individual names, sectors or portfolios. The techniques in use include credit default swap ('CDS') purchases, structured credit notes and securitisation structures. Buying credit protection creates credit exposure against the protection provider, which is monitored as part of the overall credit exposure to them. Where applicable the transaction is entered into directly with a central clearing house counterparty, otherwise our exposure to CDS protection providers is diversified among mainly banking counterparties with strong credit ratings. Further information on our use of CDS mitigants can be found on page 149 of the HSBC Holdings plc 2014 Accounts.

Policy and procedures

Policies and procedures govern the protection of our position from the outset of a customer relationship, for instance in requiring standard terms and conditions or specifically agreed documentation permitting the offset of credit balances against debt obligations, and through controls over the integrity, current valuation and, if necessary, realisation of collateral security.

Valuing collateral

Valuation strategies are established to monitor collateral mitigants to ensure that they continue to provide the anticipated secure secondary repayment source. Market trading activities such as collateralised OTC derivatives and SFTs typically include daily

valuations in support of margining arrangements. In the residential mortgage business, Group policy prescribes revaluation at intervals of up to three years, or more frequently where market conditions are subject to significant change. Residential property collateral values are determined through a combination of professional appraisals, house price indices or statistical analysis.

Local market conditions determine the frequency of valuation for CRE. Revaluations are sought where, for example, as part of the regular credit assessment of the obligor, material concerns arise in relation to the performance of the collateral. CRE revaluation also commonly occurs where a decline in the obligor's credit quality gives cause for concern that the principal payment source may not fully meet the obligation.

Recognition of risk mitigation under the IRB approach

Within an IRB approach, risk mitigants are considered in two broad categories: first, those which reduce the intrinsic PD of an obligor; and second, those which affect the estimated recoverability of obligations and thus LGD.

The first typically include full parental guarantees – where one obligor within a group of companies guarantees another. This is usually factored into the estimate of the latter's PD, as it is expected that the guarantor will intervene to prevent a default. PD estimates are also subject to a 'sovereign ceiling', constraining the risk ratings assigned to obligors in higher risk countries if only partial parental support exists. In certain jurisdictions, typically those on the Foundation IRB approach, certain types of third party guarantee are also recognised through substitution of the obligor's PD by the guarantor's PD.

In the second category, LGD estimates are affected by a wider range of collateral including cash, charges over real estate property, fixed assets, trade goods, receivables and floating charges such as mortgage debentures. Unfunded mitigants, such as third party guarantees, are also taken into consideration in LGD estimates where there is evidence that they reduce loss expectation.

The main providers of guarantees are banks, other financial institutions and corporates, the latter typically in support of subsidiaries of their company group. Across HSBC, the nature of such customers and transactions is very diverse and the creditworthiness of guarantors accordingly spans a wide spectrum. The creditworthiness of providers of unfunded credit risk mitigation is taken into consideration as part of the guarantor's risk profile when, for example, assessing the risk of other exposures such as direct lending to the guarantor. Internal limits for such contingent exposure are approved in the same way as direct exposures.

EAD and LGD values, in the case of individually assessed exposures, are determined by reference to regionally approved internal risk parameters based on the nature of the exposure. For retail portfolios, credit risk mitigation data is incorporated into the internal risk parameters for exposures and feeds into the calculation of the EL band value summarising both customer delinquency and product or facility risk. Credit and credit risk mitigation data form inputs submitted by all Group offices to centralised databases and processing, including performance of calculations to apply the relevant CRD IV rules and approach, . A range of collateral recognition approaches are applied to IRB capital treatments:

- unfunded protection, which includes credit derivatives and guarantees, is reflected through adjustment or determination of PD or LGD;
- eligible financial collateral is taken into account in LGD models (under Advanced IRB) or by adjusting regulatory LGD values (under Foundation IRB). The adjustment to LGD is based on the degree to which the exposure value would be adjusted if the Financial Collateral Comprehensive Method ('FCCM') were applied; and
- for all other types of collateral, including real estate, the LGD for exposures calculated under the IRB advanced approach is calculated by models. For IRB foundation, base regulatory LGDs are adjusted depending on the value and type of the asset taken as collateral relative to the exposure. The types of eligible mitigant recognised under the IRB foundation approach are more limited.

The table below sets out, for IRB exposures, the exposure value and the effective value of credit risk mitigation expressed as the exposure value covered by the credit risk mitigant. Further information on credit risk mitigation may be found on pages 212 – 214 of the HSBC Holdings plc 2014 Accounts.

Table 11: IRB exposure – credit risk mitigation

	2014			2013		
	Exposure value covered by eligible financial collateral £m	Exposure value covered by credit derivatives or guarantees £m	Total IRB exposure value covered by CRM £m	Exposure value covered by eligible financial collateral[1] £m	Exposure value covered by credit derivatives or guarantees £m	Total IRB exposure value covered by CRM £m
IRB advanced approach		10,224	10,224		18,239	18,239
Central governments and central banks		189	189		5	5
Institutions		281	281		106	106
Corporates		1,240	1,240		5,527	5,527
Retail		8,514	8,514		12,601	12,601
IRB foundation approach	298	277	575	319	81	400
Institutions	-	-	-	-	-	-
Corporates	298	277	575	319	81	400
At 31 December	**298**	**10,501**	**10,799**	**319**	**18,320**	**18,639**

Recognition of risk mitigation under the standardised approach

Where credit risk mitigation is available in the form of an eligible guarantee, non-financial collateral, or credit derivatives, the exposure is separated into covered and uncovered portions:

- the covered portion attracts the risk weight of the provider and is determined after applying an appropriate 'haircut' for currency and maturity mismatch (and for omission of restructuring clauses for credit derivatives, where appropriate) to the amount of the protection provided.
- the uncovered portion attracts the risk weight of the obligor. For exposures fully or partially covered by eligible financial collateral, the value of the exposure is adjusted under the FCCM using supervisory volatility adjustments, including those arising from currency mismatch, which are determined by the specific type of collateral (and, in the case of eligible debt securities, their credit quality) and its liquidation period. The adjusted exposure value is subject to the risk weight of the obligor.

Table 12 sets out the credit risk mitigation for exposures under the standardised approach, expressed as the exposure value covered by the credit risk mitigant.

Table 12: Standardised exposure – credit risk mitigation

	2014			2013		
	Exposure value covered by eligible financial and other collateral £m	Exposure value covered by credit derivatives or guarantees £m	Total standardised exposure value covered by CRM £m	Exposure value covered by eligible financial and other collateral[1] £m	Exposure value covered by credit derivatives or guarantees £m	Total standardised exposure value covered by CRM £m
Standardised approach						
Central governments or central banks	1	-	1	-	1,262	1,262
Institutions	-	-	-	-	2,057	2,057
Corporates	850	517	1,367	956	1,973	2,929
Retail	118	-	118	108	1	109
Secured by mortgages on immovable property	-	-	-	3	-	3
Exposures in default	15	-	15	-	-	-
Items associated with particularly high risk	7	-	7	-	-	-
At 31 December	**991**	**517**	**1,508**	**1,067**	**5,293**	**6,360**

Counterparty credit risk

Counterparty credit risk is the risk that the counterparty to a transaction may default before completing the satisfactory settlement of the transaction. It arises on OTC and exchange traded derivatives, securities financing transactions and exposures to central clearing counterparties ('CCP') in both the trading and non-trading books.

The table below sets out details of the group's counterparty credit risk exposures by exposure class and

approach. Further explanation of the group's approach to managing counterparty credit risk can be found:

- on pages 85 of the HSBC Bank plc 2014 Accounts;
- on pages 149 – 150 of the HSBC Holdings plc 2014 Accounts;
- on pages 72 - 78 of the HSBC Holdings plc Pillar 3 Disclosures 2014.

Table 13: Counterparty credit risk exposure – by exposure class and product

	At 31 December 2014		At 31 December 2013	
	RWA £m	Capital required £m	RWA £m	Capital required £m
By exposure class				
IRB advanced approach	18,237	1,459	12,556	1,005
Central governments and central banks	358	29	271	22
Institutions	7,951	636	4,124	330
Corporates	9,928	794	8,161	653
IRB foundation approach	1,373	110	842	67
Central governments and central banks	-	-	-	-
Institutions	-	-	-	-
Corporates	1,373	110	842	67
Standardised approach	4,069	326	3,052	244
Central governments or central banks	-	-	-	-
Institutions	3,558	285	2,590	207
Corporates	511	41	462	37
CVA Advanced approach	2,515	201	-	-
CVA Standardised approach	3,292	263	-	-
CCP Standardised approach	878	70	-	-
	30,364	**2,429**	**16,450**	**1,316**
By product				
Derivatives	19,819	1,586	13,324	1,066
Securities financing transactions	3,331	267	2,408	193
Other	878	70	718	57
CVA Advanced approach	2,515	201	-	-
CVA Standardised approach	3,292	263	-	-
CCP default fund contribution	529	42	-	-
	30,364	**2,429**	**16,450**	**1,316**

1. Includes settlement risk and free deliveries not deducted from regulatory capital.

Market risk

Market risk is the risk that movements in market risk factors, including foreign exchange rates, commodity prices, interest rates, credit spreads and equity prices will reduce the group's income or the value of its portfolios. Market risk is measured using internal market risk models where approved by the PRA, PRA approved local VAR models or the standardised approach for position risk under CRD IV.

The tables below set out details of the group's market risk exposures by type and approach. Further explanation of the group's approach to managing market risk can be found:

- on pages 67 - 74 of the HSBC Bank plc 2014 Accounts;
- on pages 176 – 185 of the HSBC Holdings plc 2014 Accounts;
- on pages 83 – 90 of the HSBC Holdings plc Pillar 3 Disclosures 2014.

Table 14: Market risk capital requirements

	2014		2013	
	RWA £m	Capital required[1] £m	RWA £m	Capital required[1] £m
Internal models based	**17,510**	**1,401**	**15,326**	**1,226**
VAR	3,870	310	2,415	193
Stressed VAR	5,540	443	2,897	232
Incremental risk charge	4,470	358	4,736	379
VAR and Stressed VAR from CRD-equivalent jurisdictions[2]	3,630	290	5,278	422
PRA standard rules	**4,927**	**393**	**2,605**	**208**
Interest rate position risk	1,351	108	1,375	110
Equity position risk	141	11	38	3
Commodity position risk	78	6	51	4
CIU	1	-	3	-
Securitisations	3,356	268	1,138	91
At 31 December	**22,437**	**1,794**	**17,931**	**1,434**

1. Calculated as 8% of RWAs.

2. Covers a) France and Germany (local VAR approval), and b) Turkey, Armenia, and Russia (treated as consolidation by aggregation).

Operational risk

The current Basel requirements include a capital requirement for operational risk, based on three levels of sophistication. The capital required under the basic indicator approach is a simple percentage of gross revenues, whereas under the standardised approach it is one of three different percentages of gross revenues allocated to each of eight defined business lines. Both these approaches use an average of the last three financial years' revenues. Finally, the advanced measurement approach (AMA) uses a bank's own statistical analysis and modelling of operational risk data to determine capital requirements. We have historically adopted, and currently use, the standardised approach in determining our operational risk capital requirements.

We are in the process of developing and implementing an AMA compliant model which we will use for economic capital calculation purposes, and it is our medium-term aim to move to the advanced measurement approach for our operational risk capital requirement calculation.

The tables below set out the group's operational risk capital requirement. Further explanation of the group's approach to managing operational risk can be found:

- on pages 74 - 76 of the HSBC Bank plc 2014 Accounts;
- on pages 186 – 189 of the HSBC Holdings plc 2014 Accounts;
- on pages 91 - 95 of the HSBC Holdings plc Pillar 3 Disclosures 2014.

Table 15: Operational risk capital requirements

	At 31 December 2014		At 31 December 2013	
	RWA	Capital required	RWA	Capital required
Operational risk analysis by approach	£m	£m	£m	£m
Standardised approach	**22,251**	**1,780**	22,039	1,763

Internal assessment of capital adequacy

Overview

The group assesses the adequacy of its capital by considering the resources necessary to cover unexpected losses arising from discretionary risks, being those which it chooses to accept (such as credit risk and market risk), and from non-discretionary risks, being those which arise by virtue of its operations (such as operational risk and business risk). The group's capital management and allocation policy is underpinned by its capital management framework. The capital management framework and related policies define the Internal Capital Adequacy Assessment Process ('ICAAP') by which the Board of Directors of HSBC Bank plc ('the Board') and senior management examine the risk profile

from both regulatory and economic capital viewpoints to ensure that the group's level of capital:

- remains sufficient to support the group's risk profile and outstanding commitments;
- exceeds the group's formal minimum regulatory capital requirements by an agreed margin;
- is capable of withstanding a severe economic downturn stress scenario; and
- remains consistent with the group's strategic and operational goals, and shareholder and rating agency expectations.

The regulatory and economic capital assessments rely upon the use of models that are integrated into the group's management of risk.

Economic capital is the internally calculated capital requirement which the group deems necessary to support the risks to which it is exposed. Regulatory capital is the minimum level of capital which the group is required to hold in accordance with the rules set by the PRA (in the case of the bank and the consolidated group) and by local regulators (for individual subsidiary companies).

The economic capital assessment is the more risk-sensitive measure as it covers a wider range of risks and takes account of the substantial diversification of risk accruing from the group's operations. The group's economic capital models, based on those developed by HSBC, are calibrated to quantify the level of capital that is sufficient to absorb potential losses over a one-year time horizon to a 99.95 per cent level of confidence for its banking activities and to a 99.5 per cent level of confidence for its insurance activities and pension risks. The group's approach to capital management is aligned to its corporate structure, business model and strategic direction.

The group's discipline around capital allocation is maintained within established processes and benchmarks, in particular the approved annual group capital plan.

Regulatory and economic capital are the metrics by which risk is measured and linked to capital within the group's risk appetite framework. The framework expresses the types and quantum of risks to which the group wishes to be exposed. It is approved and monitored by the Board and senior management.

The group identifies and manages risk through a defined risk management framework and continuous monitoring of the risk environment. It assesses and manages certain of these risks via the capital planning process.

Risks assessed via capital

Credit (including counterparty credit), market and operational risk

The group assesses economic capital requirements for these risk types utilising the embedded operational infrastructure used for the calculation of regulatory capital requirements, together with an additional suite of models that take into account, in particular:

- the increased level of confidence required to meet the group's strategic goals (99.95per cent); and
- internal assessments of diversification or concentration of risks within the group's portfolios.

When assessing the total requirement post diversification, the group's economic capital assessment typically demonstrates a lower overall capital requirement than the regulatory equivalent, as a result of diversification benefits within and between risk types. However, the group maintains a prudent stance on capital coverage, ensuring that any model risk is mitigated.

Interest rate risk in the banking book

Interest rate risk in the banking book ('IRRBB') is defined as the exposure of our non-trading products to interest rates.

This risk arises in such portfolios principally from mismatches between the future yield on assets and their funding costs, as a result of interest rate changes. Analysis of this risk is complicated by having to make assumptions on embedded optionality within certain product areas such as the incidence of mortgage prepayments, and from behavioural assumptions regarding the economic duration of liabilities which are contractually repayable on demand such as current accounts. IRRBB economic capital is measured as the amount of capital necessary to cover an unexpected loss in the value of our non-trading products over one year to a 99.95% level of confidence. The group's management of this risk is also described on pages 72 - 73 of the HSBC Bank plc 2014 Accounts.

Insurance risk

The group operates a bancassurance model which primarily provides insurance products for customers with whom the group has a banking relationship. Many of these insurance products are manufactured by group subsidiaries but, where the group considers it operationally more effective, third parties are engaged to manufacture and provide insurance products which the group sells through its banking network. When manufacturing products, the group underwrites the insurance risk and retains the risks and rewards associated with writing insurance contracts. In appropriate circumstances, the group will reduce the amount of insurance risk retained via use of reinsurance contracts. The group works with a limited number of market-leading partners and reinsurers respectively to provide or reinsure these products. The group's risk management of insurance operations is described in more detail on pages 77 - 81 of the HSBC Bank plc 2014 Accounts.

Economic capital methodologies are in use at the group's two principal life insurance subsidiaries and we continue to make progress towards implementing similar measures for the group's remaining insurance businesses.

Pension risk

The group's management of pension risk is also described on pages 82 - 83 of the HSBC Bank plc 2014 Accounts.

We operate a number of pensions; some of them are defined benefit plans. Sponsoring Group companies (and in some instances, employees) make regular contributions in accordance with advice from actuaries and in consultation with the plans' trustees (where relevant). In situations where a funding deficit emerges, sponsoring Group companies agree to make additional contributions to the plans, to address the deficit over an appropriate repayment period.

The defined benefit plans invest these contributions in a range of investments designed to meet their long-term liabilities.

Pension risk principally arises from the potential for a deficit in a defined benefit plan from a number of factors, including:

- investments delivering a return below that required to provide the projected plan benefits. This could arise, for example, when there is a fall in the market value of equities, or when increases in long-term interest rates cause a fall in the value of fixed income securities held;
- the prevailing economic environment leading to corporate failures, thus triggering write-downs in asset values (both equity and debt);
- a change in either interest rates or inflation expectations causing an increase in the value of the plan liabilities; and
- plan members living longer than expected (known as longevity risk).

Pension risk is assessed by way of an economic capital model that takes into account potential variations in these factors, using a VAR methodology.

Risks not explicitly assessed via capital

Liquidity risk

Liquidity and funding risk management is described in detail on pages 59 - 65 of the HSBC Bank plc 2014 Accounts.

The group uses cash-flow stress testing as part of its control processes to assess liquidity risk. In common with standard industry practice, the group does not manage liquidity through the explicit allocation of capital as this is not considered to be an appropriate or adequate mechanism for managing these risks. However, the group recognises that a strong capital base can help to mitigate liquidity risk both by providing a capital buffer to allow an entity to raise funds and deploy them in liquid positions and by serving to reduce the credit risk taken by providers of funds to the group.

Structural foreign exchange risk

Structural foreign exchange risk is described in detail on page 72 of the HSBC Bank plc 2014 Accounts.

Structural foreign exchange risks arise from our net investments in subsidiaries, branches and associates, the functional currencies of which are other than the British Pound. Unrealised gains or losses due to revaluations of structural foreign exchange exposures are reflected in reserves, whereas other unrealised gains or losses arising from revaluations of foreign exchange positions are reflected in the income statement.

The group's structural foreign exchange exposures are managed with the primary objective of ensuring, where practical, that the group's consolidated capital ratios and the capital ratios of the individual banking subsidiaries are largely protected from the effect of changes in exchange rates. This is usually achieved by

ensuring that, for each subsidiary bank, the ratio of structural exposures in a given currency to risk-weighted assets denominated in that currency is broadly equal to the capital ratio of the subsidiary in question. The group evaluates residual structural foreign exchange exposures using a VAR model, but typically does not assign any economic capital for these, since they are managed within appropriate economic capital buffers.

Residual risk

Residual risk is primarily the risk that mitigation techniques prove less effective than expected. This category also includes risks that arise from specific reputational or business events that give rise to exposures not deemed to be included in the major risk categories. The group conducts economic capital assessments of such risks on a regular, forward-looking basis to ensure that their impact is adequately covered by its capital base.

Reputational risk

Details of the group's management of reputational risk can be found on pages 81 - 82 of the HSBC Bank plc 2014 Accounts.

As a banking group, the group's reputation depends upon the way in which it conducts its business, but it can also be affected by the way in which clients to whom it provides financial services conduct themselves. The group's reputation is paramount and safeguarding it is the responsibility of all members of staff, supported by a global risk management structure, underpinned by relevant policies and practices, readily available guidance and regular training.

Business risk

The PRA specifies that banks, as part of their internal assessment of capital adequacy process, should review their exposure to business risk.

Business risk is the potential negative impact on profits and capital as a result of the group not meeting its strategic objectives, as set out in the rolling operating plan, owing to unforeseen changes in the business and regulatory environment, exposure to economic cycles and technological changes. The group does not explicitly set aside capital against business risk as a distinct category.

Business risk is managed and mitigated through the business planning and stress testing processes, which ensure that the business model and planned activities are appropriately resourced and capitalised consistent with the commercial, economic and risk environment in which the group operates and that the potential vulnerability to the business plans are identified at an early stage so that mitigating actions can be taken proactively.

Scenario analysis and stress testing

Scenario analysis and stress testing form a key component of the group's integrated risk management framework. They provide a forward-looking assessment of risk, identify key variables under a range of scenarios, and facilitate the development of appropriate mitigating actions and contingency plans across a range of stressed conditions. As part of the group's risk appetite process, scenario analysis and stress testing support the setting of Risk Appetite tolerances, and inform business, capital planning and strategic decision making.

Regulatory capital supply is regularly assessed against demand under a range of stress scenarios, including projected global and local economic downturns. Qualitative and quantitative techniques are used to estimate the potential impact on the group's capital position under such scenarios. The group also participates, where appropriate, in standard scenario analyses requested by regulatory bodies. During 2014 the Group (and certain subsidiaries) participated in the completion of the PRA, the EBA and the ECB stress testing exercises.

The Group Stress Testing Management Board, chaired by the Group Finance Director, with appropriate subordinate Steering Committees at regional level, ensures appropriate senior management oversight and governance of stress testing exercises.

Remuneration

As a wholly owned subsidiary, HSBC Bank plc is subject to the remuneration policy established by the Group. Details of the Group's remuneration policy, including details on the Remuneration Committee membership and its activities, our remuneration strategy and tables showing the remuneration details of HSBC's Identified Staff and Material Risk Takers may be found in the Remuneration Policy on our website (http://www.hsbc.com/investor-relations/governance) and in the Directors' Remuneration Report on pages 300 - 323 of the HSBC Holdings plc Annual Report and Accounts 2014.

The following tables show the remuneration awards made to Identified Staff and Material Risk Takers ('MRTs') in HSBC Bank plc for 2014. Individuals have been identified as MRTs based on the qualitative and quantitative criteria set out in the Regulatory Technical Standard EU 604/2014 that came into force in June 2014. This replaces the criteria that were previously used to identify Code Staff for the purposes of Prudential Regulation Authority's and Financial Conduct Authority's Remuneration Code. The tables below include the total remuneration of HSBC Bank plc senior management and other individuals identified as HSBC MRTs based on their role and professional activities and whose remuneration costs are borne by HSBC Bank plc or its subsidiaries. This includes certain individuals employed by the group who have broader roles within HSBC, for example those with global roles.

These disclosures reflect the requirements of the Financial Conduct Authority's Prudential Sourcebook for Banks.

Table 16: Aggregate remuneration expenditure

	By Global business					
	Retail Banking and Wealth Management £m	Commercial Banking £m	Global Banking and Markets £m	Global Private Banking £m	Other £m	Total £m
Aggregate remuneration expenditure[1]						
2014	**7.1**	**16.5**	**230.0**	**10.1**	**50.6**	**314.3**

1. Includes salary and incentives awarded in respect of performance in the year 2014 (including deferred component) and any pension or benefits outside of policy.

Table 17: Remuneration – fixed and variable amounts

	2014		
	MRTs		
	Senior management	Non-senior management	Total
Number of MRTs	27	408	435
	£m	£m	£m
Fixed			
Cash based	10.4	124.1	134.5
Shares based	10.3	25.3	35.6
Total fixed	20.7	149.4	170.1
Variable[1]			
Cash	3.1	34.1	37.2
Non-deferred shares[2]	3.1	32.4	35.5
Deferred cash	4.3	30.3	34.6
Deferred shares	5.9	30.8	36.7
Total variable pay[3]	16.4	127.6	144.0

1. Variable pay awarded in respect of performance in the year 2014.

2. Vested shares, subject to a six-month retention period.

3. In accordance with shareholder approval received on 23 May 2014, for each MRT the variable component of remuneration for any one year is limited to 200% of fixed component of total remuneration of the MRT.

Table 18: Deferred remuneration[1]

	2014		
	MRTs		
	Senior management	Non-senior management	Total
	£m	£m	£m
Deferred remuneration at 31 December 2014			
Outstanding, unvested	45.2	171.6	216.8
Awarded during the year	20.3	89.5	109.8
Paid out	7.4	51.0	58.4
Reduced through malus	-	-	-

1. This table provides details of actions taken during the performance year 2014. For details of variable pay awards granted for the performance years 2014, please refer to both the Remuneration tables above.

Table 19: Sign-on and severance payments

	2014		
	MRTs		
	Senior management	Non-senior management	Total
Sign-on payments			
Made during year (£m)	-	0.3	0.3
Number of beneficiaries	-	1	1
Severance payments			
Made during year (£m)	-	1.1	1.1
Number of beneficiaries	-	5	5
Highest such award to single person (£m)	-	0.3	0.3

Table 20: MRT remuneration by band[1]

	Number of MRTs		
	Senior management	Non-senior management	Total
€0 – €1,000,000	10	298	308
€1,000,001 – €1,500,000	5	71	76
€1,500,001 – €2,000,000	3	16	19
€2,000,001 – €2,500,000	2	10	12
€2,500,001 – €3,000,000	2	6	8
€3,000,001 – €3,500,000	2	4	6
€3,500,001 – €4,000,000	–	2	2
€4,000,001 – €4,500,000	2	–	2
€4,500,001 – €5,000,000	–	1	1
€5,000,001 – €6,000,000	–	–	–
€6,000,001 – €7,000,000	–	–	–
€7,000,001 – €8,000,000	1	–	1

1. Table prepared in euros in accordance with Article 450 of the CRR, using the rates published by the European Commission for financial programming and budget for December 2014 as published on their website.

Main features of CET1, AT1 and T2 instruments issued by the group

All capital securities included in the regulatory capital base of the group have been issued either in accordance with the rules and guidance in the PRA's General Prudential Sourcebook ('GENPRU') and have been included in the capital base, either by virtue of the application of the CRD IV grandfathering provisions, or issued as fully-compliant CRD IV securities. For regulatory purposes, the group's capital base is divided into three main categories, namely Common Equity Tier 1, Additional tier 1 and Tier 2, depending on the degree of permanence and loss absorbency exhibited. The main features of capital securities issued by the group are described below.

Non-CRD IV compliant additional tier 1 and tier 2 instruments benefit from a grandfathering period. This progressively reduces the eligible amount by 10% annually, following an initial reduction of 20% on 1 January 2014, until they are fully phased out by 1 January 2022.

Tier 1 capital

Tier 1 capital comprises shareholders' equity, related non-controlling interests (subject to limits) and qualifying capital instruments, after certain regulatory adjustments.

Common Equity Tier 1

Called up ordinary shares issued by the bank to its parent are fully paid-up and the proceeds of issuance are immediately and fully available. There is no obligation to pay a coupon or dividend to the shareholder arising from this type of capital. The share capital is available for unrestricted and immediate use to cover any risks and losses.

Additional tier 1 capital

Preference shares and related premium

Preference shares are securities which rank higher than ordinary shares for dividend payments and in the event of a winding-up, but generally carry no voting rights. These instruments have no stated maturity date but may be called and redeemed by the issuer, subject to prior consent from the PRA, and, where applicable, the local banking regulator. There must also be no obligation to pay a dividend, and (if not paid) the dividend may not cumulate.

Further details of the HSBC Bank plc non-cumulative third dollar preference share capital can be found in note 32 – Called up share capital and other equity instruments of the Notes on the Financial Statements on pages 177 - 178 of the HSBC Bank plc 2014 Accounts.

Other tier 1 capital securities

Other tier 1 capital securities are deeply subordinated securities with some equity features that may be included as tier 1 capital. Other tier 1 capital securities are instruments for which there is no obligation to pay a coupon and if not paid, the coupon is not cumulative. Such securities do not generally carry voting rights and rank higher than ordinary shares for coupon payments and in the event of a winding-up. The securities may be called and redeemed by the issuer, subject to prior consent from the PRA, and, where applicable, the local banking regulator. If not redeemed, coupons payable may step-up and become floating rate related to interbank offered rates.

Further details of these instruments can be found in note 28 – Subordinated Liabilities of the Notes on the Financial Statements on pages 171 - 172 of the HSBC Bank plc 2014 Accounts.

Qualifying CRD IV additional tier 1 instruments are perpetual securities on which there is no obligation to

apply a coupon and, if not paid, the coupon is not cumulative. Such securities do not carry voting rights but rank higher than ordinary shares for coupon payments and in the event of a winding-up. Fully-compliant CRD IV additional tier 1 instruments issued by the bank include a provision whereby the instrument will be written down in whole in the event the group's common equity tier 1 ratio falls below 7.00%.

These instruments are accounted for as equity. Further details of qualifying CRD IV additional tier 1 instruments can be found in note 32 – Called up share capital and other equity instruments of the Notes on the Financial Statements on pages 177 - 178 of the HSBC Bank plc 2014 Accounts.

Tier 2 capital

Tier 2 capital comprises eligible capital securities and any related share premium and other qualifying tier 2 capital securities subject to limits. Holdings of tier 2 capital of financial sector entities are deducted.

Perpetual and Term Subordinated debt

Tier 2 capital securities are either perpetual subordinated securities or dated securities on which there is an obligation to pay coupons.

These instruments or subordinated loans comprise dated loan capital repayable at par on maturity and must have an original maturity of at least five years. Some subordinated loan capital may be called and redeemed by the issuer subject to prior consent from the PRA and, where applicable, the consent of the local banking regulator. If not redeemed, interest coupons payable may step-up or become floating rate related to interbank offered rates. For regulatory purposes, it is a requirement that tier 2 instruments are amortised on a straight-line basis in their final five years to maturity, thus reducing the amount of capital that is recognised for regulatory purposes.

Further details of these instruments can be found in note 28 – Subordinated Liabilities of the Notes on the Financial Statements on pages 171 - 172 of the HSBC Bank plc 2014 Accounts.

A list of the features of our capital instruments in accordance with Annex III of the Commission Implementing Regulation 1423/2013 is also being published on HSBC's website with reference to our balance sheet on 31 December 2014.

Appendix I

Table 21: Transitional own funds disclosure

	At 31 December 2014 £m	CRR prescribed residual amount £m	Final CRD IV text £m
Common equity tier 1 (CET1) capital: instruments and reserves			
Capital instruments and the related share premium accounts	21,100	-	21,100
Retained earnings	9,928	-	9,928
Accumulated other comprehensive income (and other reserves, to include unrealised gains and losses under applicable accounting standards)	866	-	866
Minority interests (amount allowed in consolidated CET1)	353	-	353
Independently reviewed interim net profits net of any foreseeable charge or dividend	467	-	467
Common equity tier 1 capital before regulatory adjustments	32,714	-	32,714
Common equity tier 1 capital: regulatory adjustments			
Additional value adjustments	(588)	-	(588)
Intangible assets (net of related deferred tax liability)	(6,821)	-	(6,821)
Deferred tax assets that rely on future profitability excluding those arising from temporary	(21)	-	(21)
Fair value reserves related to gains or losses on cash flow hedges	(163)	-	(163)
Negative amounts resulting from the calculation of expected loss amounts	(950)	-	(950)
Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	245	-	245
Debit valuation adjustment	(88)		(88)
Defined-benefit pension fund assets	(2,400)	-	(2,400)
Regulatory adjustments applied to common equity tier 1 in respect of amounts subject to pre-CRR treatment			
Regulatory adjustments relating to unrealised gains and losses	(837)	837	-
Total regulatory adjustments to Common equity tier 1 (CET1)	**(11,623)**	**837**	**(10,786)**
Common equity tier 1 (CET1) capital	**21,091**	**837**	**20,254**
Additional Tier 1 (AT1) capital: instruments			
Capital instruments and the related share premium accounts	2,195	-	2,195
Amount of qualifying items and the related share premium accounts subject to phase out from AT1	1,852	(1,852)	--
Additional Tier 1 (AT1) capital	**4,047**	**(1,852)**	**2,195**
Tier 1 capital (T1 = CET1 + AT1)	**25,138**	**(1,015)**	**24,123**
Tier 2 (T2) capital: instruments and provisions			
Capital instruments and the related share premium accounts	6,302	-	6,302
Amount of qualifying items and the related share premium accounts subject to phase out from T2	1,965	(1,965)	-
Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments) issued by subsidiaries and held by third parties, of which: instruments issued by subsidiaries subject to phase out	361	(361)	-
T2 capital before regulatory adjustments	8,628	(2,326)	6,302
Tier 2 (T2) capital: regulatory adjustments			
Direct and indirect holdings by the institution of the T2 instruments and subordinated loans of financial sector entities where the institution has a significant investment in those entities (net of eligible short positions)	(210)	-	(210)
Total regulatory adjustments to Tier 2 (T2) capital	**(210)**	**-**	**(210)**
Tier 2 (T2) capital	**8,418**	**(2,326)**	**6,092**
Total capital (TC = T1 + T2)	**33,556**	**(3,341)**	**30,215**
Total risk weighted assets	**243,652**	**-**	**243,652**
Capital ratios and buffers			
Common equity Tier 1	8.7%		9.1%
Tier 1	10.3%		10.0%
Total capital	13.8%		12.5%

	At 31 December 2014 £m	CRR prescribed residual amount £m	Final CRD IV text £m
Amounts below the threshold for deduction (before risk weighting)			
Direct and indirect holdings of the capital of financial sector entities where the institution does not have a significant investment in those entities (amount below 10% threshold and net of eligible short positions	1,241	-	1,241
Direct and indirect holdings by the institution of the CET 1 instruments of financial sector entities where the institution has a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	586	-	586
Deferred tax assets arising from temporary differences (amount below 10% threshold, net of related tax liability)	619	-	619
Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2013 and 1 Jan 2022)			
Current cap on AT1 instruments subject to phase out arrangements	80%		
Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	463	(463)	-
Current cap on T2 instruments subject to phase out arrangements	80%		
Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)	-	-	-

Appendix II

Glossary

Term	Definition
A	
Available-for-sale ('AFS') financial assets	Those derivative financial assets that are designated as available for sale or are not classified as a) loans and receivables b) held-to-maturity investments or c) financial assets at fair value through profit or loss.
B	
Basel II	The capital adequacy framework issued by the Basel Committee on Banking Supervision in June 2006 in the form of the 'International Convergence of Capital Measurement and Capital Standards'.
Basel 2.5	The update to Basel II including changes to capital and disclosure requirements for securitisation and market risk, which took effect in December 2011.
Basel III	In December 2010, the Basel Committee issued 'Basel III rules: a global regulatory framework for more resilient banks and banking systems' and 'International framework for liquidity risk measurement, standards and monitoring'. Together these documents present the Basel Committee's reforms to strengthen global capital and liquidity rules with the goal of promoting a more resilient banking sector. In June 2011, the Basel Committee issued a revision to the former document setting out the finalised capital treatment for counterparty credit risk in bilateral trades. The Basel III requirements were phased in with full implementation by 1 January 2019.
C	
Capital conservation buffer	A capital buffer, prescribed by regulators under Basel III, and designed to ensure banks build up capital buffers outside periods of stress which can be drawn down as losses are incurred. Should a bank's capital levels fall with in the capital conservation buffer range, capital distributions will be constrained by regulator.
Capital requirements directive ('CRD')	A capital adequacy legislative package issued by the European Commission and adopted by EU member states. The first CRD legislative package gave effect to the Basel II proposals in the EU and came into force on 20 July 2006. CRD II, which came into force on 31 December 2010, subsequently updated the requirements for capital instruments, large exposure, liquidity risk and securitisation. A further CRD III amendment updated market risk capital and additional securitisation requirements and came into force on 31 December 2011. The CRD IV package comprises a recast Capital Requirements Directive ('CRD') and a new Capital Requirements Regulation ('CRR'). The package implements the Basel III Capital proposals together with transitional arrangements for some of its requirements. CRD IV proposals came into force on 1 January 2014.
Common equity tier 1 capital ('CET 1')	The highest quality form of regulatory capital under Basel III that comprises common shares issued and related share premium, retained earnings and other reserves excluding the cash flow hedging reserve, less specified regulatory adjustments.
Countercyclical capital buffer ('CCB')	A capital buffer, prescribed by regulators under Basel III, which aims to ensure that capital requirements take account of the macro-financial environment in which banks operate. This aims to provide the banking sector with additional capital to protect it against potential future losses, when excess credit growth in the financial system as a whole is associated with an increase in system-wide risk.
CRE	Commercial real estate
D	
Derivatives	Financial instruments whose value is based on the performance of one or more underlying assets, for example bonds or currencies.
E	
Economic capital	The internally calculated capital requirement which is deemed necessary by the group

	to support the risks to which it is exposed.
Expected loss ('EL')	A regulatory calculation of the amount expected to be lost on an exposure using a 12-month time horizon and downturn loss estimates. EL is calculated by multiplying the PD (by the EAD (an amount) and LGD (a percentage).
Exposure	A claim, contingent claim or position which carries a risk of financial loss.
Exposure at default ('EAD') or exposure value	The amount expected to be outstanding after any credit risk mitigation, if and when the counterparty defaults. EAD reflects drawn balances as well as allowance for undrawn amounts of commitments and contingent exposures.
F	
Fair value	Fair value is the price that would be received to sell and asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.
I	
Incremental risk charge ('IRC')	The IRC model captures the potential distribution of profit and loss due to default and migration for a portfolio of credit positions. For credit positions held on the trading book, and subject to specific interest rate risk VAR for regulatory capital, an IRC based on the 99.9th percentile of the IRC distribution, over a 0ne-year capital horizon, is used as a capital add-on to VAR.
Institutions	Under the standardised approach, Institutions comprise credit institutions or investment firms. Under the IRB approach, Institutions also include regional governments and local authorities, public sector entities and multilateral development banks.
Insurance risk	A risk, other than financial risk, transferred from the holder of a contract to the insurance provider. The principal insurance risk is that, over time, the combined cost of claims, administration and acquisition of the contract may exceed the aggregate amount of premiums received and investment income.
Internal model method ('IMM')	One of three methods defined in the Basel framework to determine exposure values for counterparty credit risk.
Internal capital adequacy assessment process ('ICAAP')	The group's own assessment of the levels of capital that it needs to hold through an examination of its risk profile from regulatory and economic capital viewpoints.
Internal ratings-based approach ('IRB')	A method of calculating credit risk capital requirements using internal, rather than supervisory, estimates of risk parameters.
IRB advanced approach	A method of calculating credit risk capital requirements using internal PD, LGD and EAD models.
IRB foundation approach	A method of calculating credit risk capital requirements using internal PD models but with supervisory estimates of LGD and conversion factors for the calculation of EAD.
L	
Liquidity risk	The risk that the group does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash flows.
Loss given default ('LGD')	The estimated ratio (percentage) of the loss on an exposure to the amount outstanding at default (EAD) upon default of a counterparty.
P	
Pillar 1	Minimum capital requirements – the calculation of regulatory capital for credit, market and operational risk.
Pillar 2	The supervisory review process – sets out the process by which a bank should review its overall capital adequacy and the processes under which the supervisors evaluate how well financial institutions are assessing their risks and take appropriate actions in response to the assessments.
Pillar 3	Market discipline – sets out the disclosure requirements for banks to publish certain details of their risks, capital and risk management, with the aim of strengthening market discipline.
Probability of default ('PD')	The probability that an obligor will default within one year.

Prudential Regulatory Authority ('PRA')	The Prudential Regulation Authority in the UK is responsible for prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms.
Q	
Qualifying revolving retail exposures	Retail IRB exposures that are revolving, unsecured, and, to the extent they are not drawn, immediately and unconditionally cancellable, such as credit cards and overdrafts.
R	
Regulatory capital	The capital that a bank holds, determined in accordance with rules established by the PRA for the consolidated group and by local regulators for individual group companies.
Risk appetite	The aggregate level and types of risk a firm is willing to assume within its risk capacity to achieve its strategic objectives and business plan.
Risk-weighted assets ('RWA')	Calculated by assigning a degree of risk expressed as a percentage (risk weight) to an exposure value in accordance with the applicable Standardised and IRB approach rules.
S	
Securitisation	A transaction or scheme whereby the credit risk associated with an exposure, or pool of exposures, is tranched and where payments to investors in the transaction or scheme are dependent upon the performance of the exposure or pool of exposures. A traditional securitisation involves the transfer of the exposures being securitised to an SPE which issues securities. In a synthetic securitisation, the tranching is achieved by the use of credit derivatives and the exposures are not removed from the balance sheet of the originator.
Securities financing transactions ('SFT')	The act of loaning or borrowing a stock, derivative, or other security to or from an investor or firm.
Special purpose entity ('SPE')	A corporation, trust or other non-bank entity, established for a narrowly defined purpose, including for carrying on securitisation activities. The structure of the SPE and its activities are intended to isolate its obligations from those of the originator and the holders of the beneficial interests in the securitisation.
Standardised approach	In relation to credit risk, method for calculating credit risk capital requirements using supervisory risk weights. In relation to operational risk, a method of calculating the operational capital requirement by the application of a supervisory defined percentage charge to the gross income of eight specified business lines.
Standard market risk PRR rules	The PRA's rules regarding the calculation of market risk capital requirements for trading book exposures which are not subject to VAR model permissions. The rules divide risks into a number of standard types, within which risk is measured by the application of defined percentage charges to both net and gross exposures.
Stressed VAR	A market risk measure based on potential market movements for a continuous one-year period of stress for a trading portfolio.
T	
Tier 1 capital	A component of regulatory capital, comprising common equity tier 1 capital and other tier 1 capital. Other tier 1 capital includes qualifying capital instruments such as non-cumulative perpetual preference shares and other tier 1 capital securities.
Tier 2 capital	A component of regulatory capital, comprising qualifying subordinated loan capital and related non-controlling interests.
V	
Value at risk ('VAR')	A measure of the loss that could occur on risk positions as a result of adverse movements in market risk factors (e.g. rates, prices, volatilities) over a specified time horizon and to a given level of confidence.

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